CHINA'S PROPERTY SECTOR

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OVERVIEW

China’s Property Sector

- China’s property market has been a formative driver of both the local and global economy that largely began with liberalization reforms in the late 1970s, with broader household and property reforms occurring in both the 80s and 90s.
- This transformation to a market-driven system established greater demand in the real estate and property sectors within China.
- Crisis within China’s property and housing sector dates back to the early 2000s, with a growing housing bubble caused by overbuilding, risky investments, government regulations, and developer defaults.
- These events largely culminated to the Chinese property sector collapse involving valuable real estate companies such as Evergrande, Country Garden and other property sector giants.

HISTORY AND FINANCIALIZATION OF THE REAL ESTATE SECTOR.

1

1949-1978

CHINA INHERITED THE REAL ESTATE SYSTEM OF THE SOVIET UNION , WELFARE HOUSING SYSTEM. PROPERTIES BELONGED TO GOVERNMENTAL AGENTS OR COLLECTIVE COMPANIES.

2

1978-1987

THE SECTOR EVOLVED TO THE 1/3 MODEL, WITHOUT SIGNICANT CHANGE.

3

1987-1991

THE REAL ESTATE SECTOR BEGAN TO OPEN. LAND TRANSFERS WAS APPROVED BUT MOST OWNERSHIP REMAINED PUBLIC

4

1992-1997

RAPID DEVELOPMENT OF THE REAL ESTATE, , LESS REGULATIONS, DEVELOPMENT OF COMPANIES PROVIDING REAL ESTATE SERVICES

5

1998-NOW

Abolition of the welfare housing system

Early 2000s, China's rapid urbanization and demand for housing.

Ratio of real estate to GDP raised from 36.7% in 1997 to 42.6% in 2005.

Investment in real estate grew from 5% in 1997 to 15% in 2014.

Heavy reliance on the real estate after GFC to sustain high growth rates.

Financialization in China’s Property Sector

- China’s property and real estate sectors essential to the country’s financial system
- Property sector as a financial asset
- Urbanization and globalization have established property and real estate sectors as engines for China’s economic growth

Broader Implications :

- Speculative buying
- Greater loan distribution
- Systemic risk
- Unbalenced resource allocation

What did Financialization mean for China?

A state led reform process of the banking system

China went through a state-led reform process of the Chinese banking system, creating a layered banking structure with the central bank at the top of the hierarchy.

Development of capital and money markets to accomodate international trade

China developed its capital and money markets to better accommodate international trade. This evolution was driven by market forces, evident in the expansion of shadow banking. The instruments and lending practices it offered catered to the increasing investors seeking investments with higher returns.

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WHY IS THE PROPERTY SECTOR FINANCIALIZED

Shift in investments from stocks to real estate

The volatility of the Chinese stock market has led to inconsistent financial outcomes for investors, with some achieving large gains while others large losses. In contrast, the real estate market had more stability and consistent growth.

Consequence: many investors turned to the property sector as a safer and more attractive investment option.

Large credit expansion

The liberalization in the 1970s and significant housing reforms in the late 1980s led to an explosive growth in the property sector and aggressive investment strategies. The sector has seen massive credit expansion and investment, which has led to high levels of debt and speculation. Chinese developers would launch a project for pre sales, get the money from home buyers, and immediately invest it into new land parcels to keep expanding. This mechanism turned real estate into a financial commodity.

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SUBORDINATION FACTOR

The predominant investors in China's property market were **domestic Chinese investors**, specifically middle- and upper-income households.

This segment was responsible for inflating the bubble, investing heavily due to speculative motives. Indeed, Chinese households have 70% or more of their asset wealth in their apartments.

This trend highlights that while the real estate sector in China is highly influenced by financial practices, the major contributors were not institutional investors but individual homeowners.

The Role of Key Economic Actors

Government

The Chinese government has been a central figure through its policy decisions. Beginning with the liberalization reforms in the late 1970s and more definitive housing reforms in the late 1980s and 1998, the government transformed the housing system from a state-distributed model to a market-driven one.

Real Estate Developers

Companies like Evergrande capitalized on the growing demand for real estate and the availability of easy credit to start massive development projects.

Homeowners

China has one of the world's largest rates of homeownership (90% in 2020). This reflects a cultural element, as owning a home is traditionally seen as a prerequisite for marriage. Additionally, buying homes had been considered a savvy investment (and as much as 70% of household wealth is in property).

Banks

A substantial portion of funding for property developers comes from bank loans. Real estate loans accounted for 27.4% of total loans issued in 2020.

Shadow Banking

The shadow banking system offered loans and credit to participants in the real estate market who may not qualify for traditional bank financing. Shadow banking has helped fueling rapid growth in the Chinese real estate market.

Contemporary Timeline of China's Property Sector

2005: Chinese Property Bubble

2007/2008: GFC

2020: Covid-19 Crisis +Three Red Lines Poicy

2021: Crisis Escalation

2021-Present: Financial Contagion and Collapse

ECONOMIC AND FINANCIAL LANDSCAPE (2023)

GDP: 126,058.2 BILLION YUAN, 5.2% GROWTH.
GDP/ CAPITA: 89,358 ¥, UP BY 5.4%

UNEMPLOYMENT RATE: 5.2 %.
CPI WENT UP 0.2%

FOREIGN EXCHANGE RESERVES: 3,238.0 BILLION USD, AN INCREASE OF 110.3 BILLION US DOLLARS

- THE AVERAAGE EXCHANGE RATE IN 2023: 7.0467 RMB TO 1 USD, DEPRECIATING BY 4.5%

THE REAL ESTATE SECTOR ACCOUNTED FOR 21% OF GDP, FOLLOWED BY MANUFACTURING HIGH- TECH AND DIGITAL COMMERCE

Residental Property Prices

Prices have regressed to 2017 levels, erasing seven years of appreciation.

*Data: Federal Bank of Saint Louis

Development Market Constriction

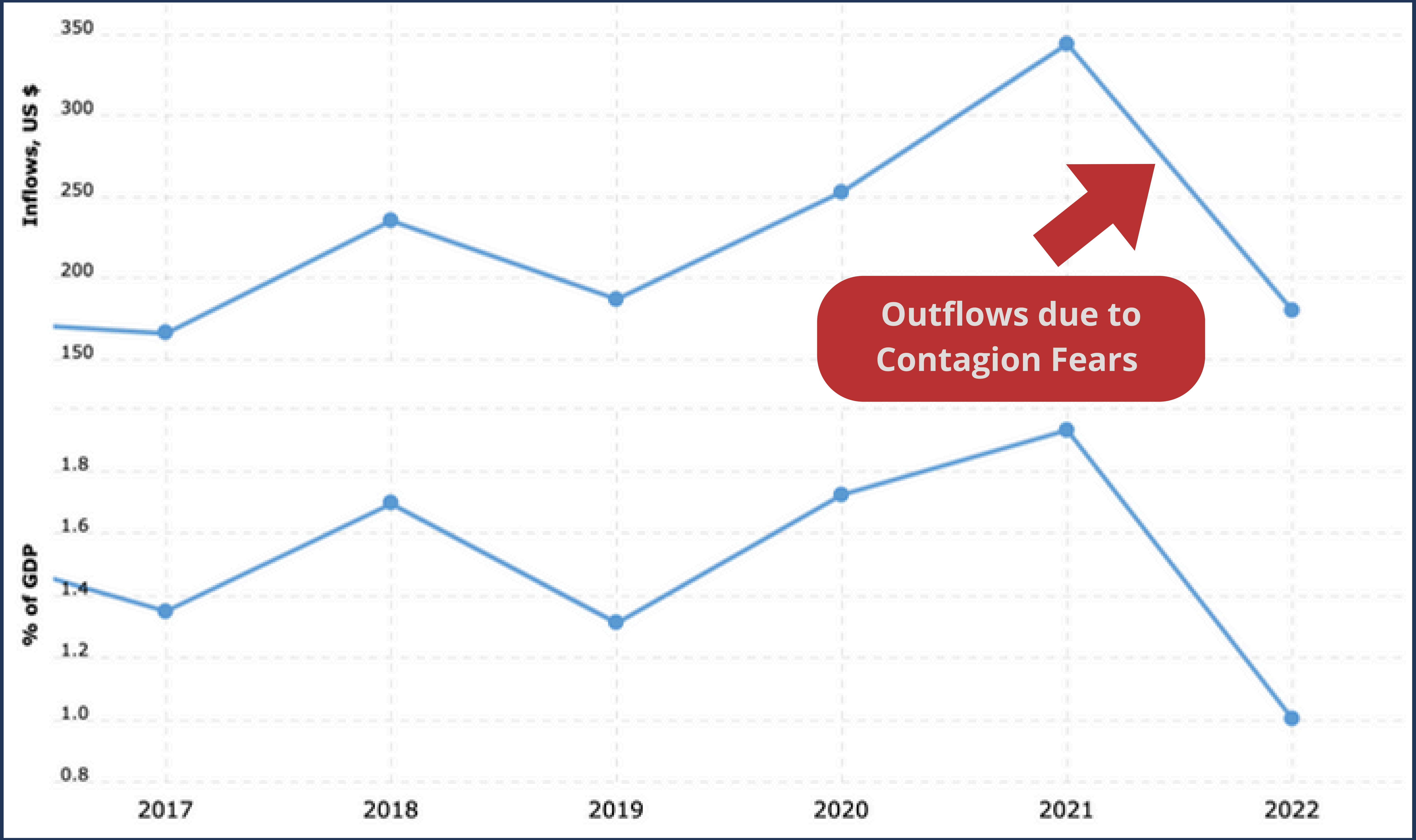
Chinese Developers Cut Jobs

Number of employees	Dec 31, 2020	June 30, 2023	Drop, %
Evergrande	123,276	109,085	-12%
Country Garden	93,899	58,140	-38%
Sunac	64,436	43,124	-33%
Shimao	6,364	1,393	-78%
Seazen	32,127	24,294	-24%

Over 83,000 jobs have been lost in the developer market.

*Data: Woodstat & Sunnyside Financial Group

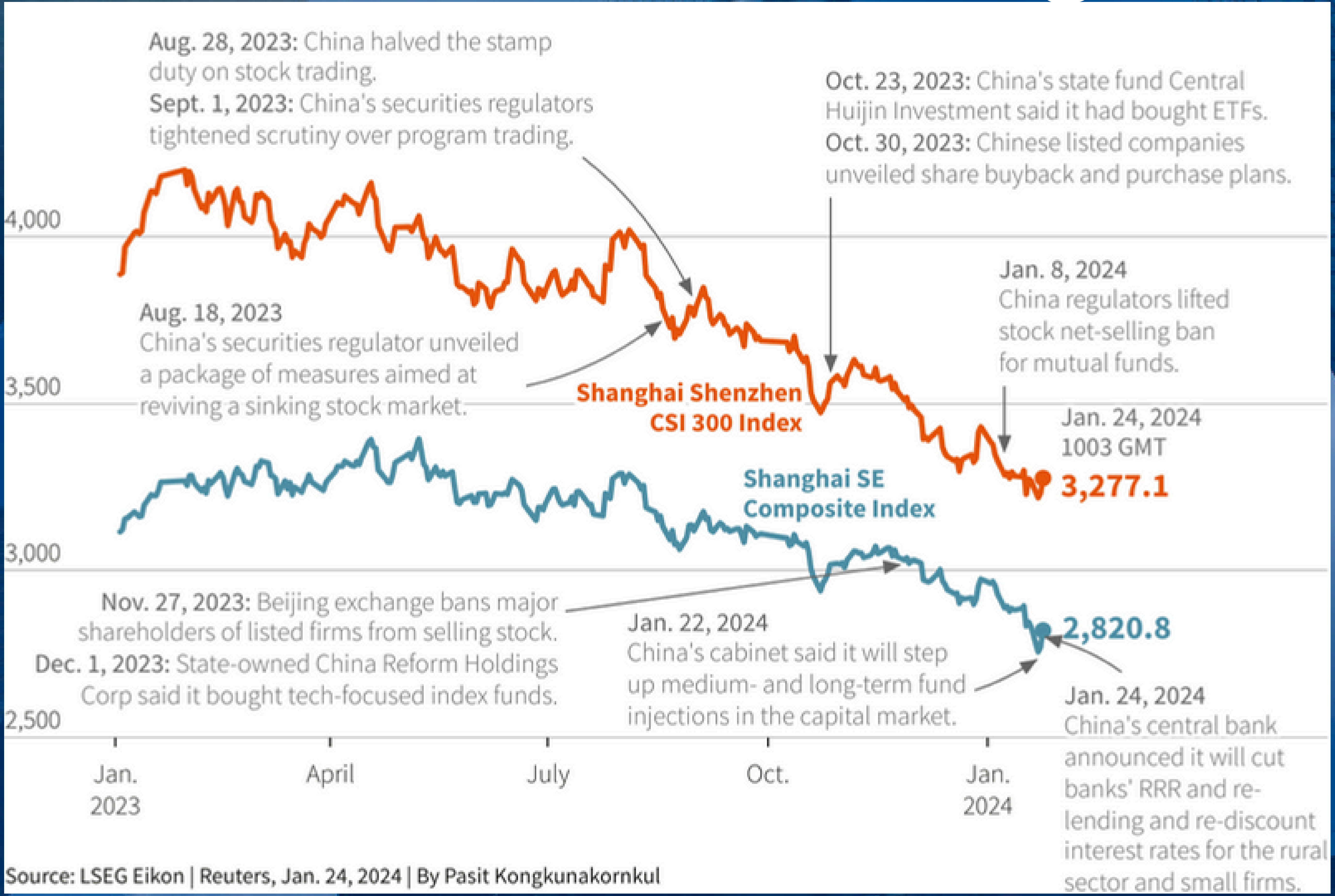
Foreign Direct Investment



*Data: MarcoTrends

Yuan Weakens

Stock Market Contagion



GOVERNMENT WORK REPORT 2023

POLICIES

- Issuance of ultra-long special treasury bonds.
- Increase quota for Special Purpose Bonds
- Tax deductions for R&D
- PBOC: 0.5% cut in the reserve requirement ratio for financial institutions.
- 24 points plan to attract FDI (FDI fell 8% in 2023)
- Industry priorities: emerging and future industries and development of the digital economy.
- May 2024:central bank announced the provision $42 billion in cheap loans for helping local state-owned entities buy unsold property

Conclusion

Large swaths of domestic Chinese developers and residental investors have lost substantial investment.

The pace of new construction has declined, concurrent with a weakening Chinese stock market due to the economic deceleration. Foreign investors have pulled backed, contributing to the depreciation of the Yuan against foreign currencies.

The Chinese government has enacted policies aimed at improving market conditions and invigorating investment activities.

The financialization of the Chinese housing sector resulted in Chinese retail investors and corporations becoming hyper-exposed to the market. This caused widespread financial ruin when the bubble collapsed.

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