

Prudential Measures against Property Cycle and Financial Stability in China

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Content

- **Risks in the Real Estate Sector**
- **Regulatory Measures**
- **Macro-adjustment Policies**



Importance of the Real Estate Sector

- An Important Industry and Contributor to GDP
- Amplifier of People's Welfare
- Impact on Financial Stability
 - Real Estate as Collateral of Bank Loans
 - Property Bubble Causes Crisis in History



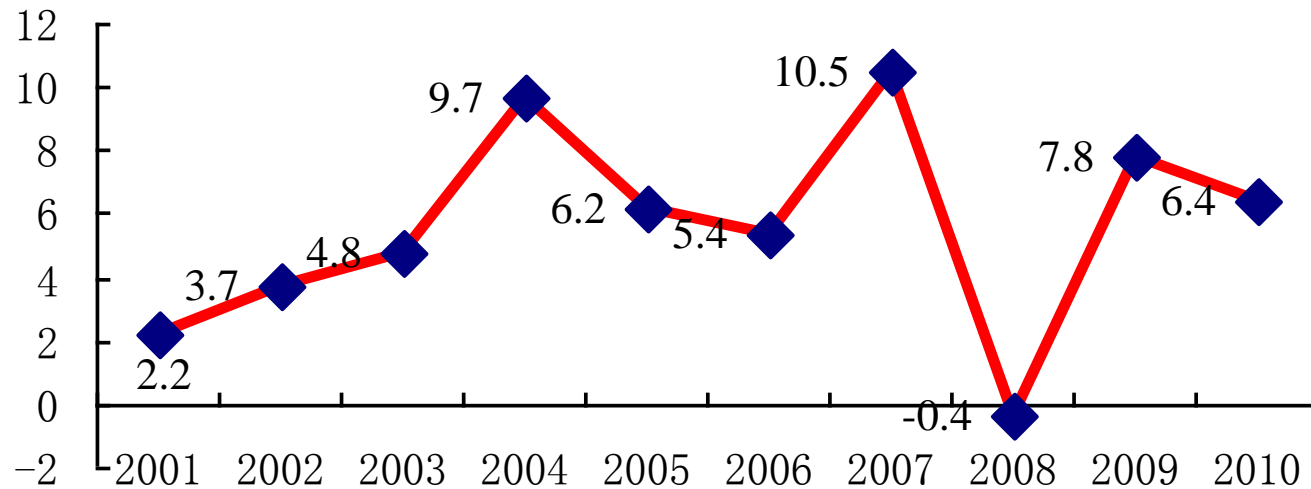
Strong Early Warning Signal of Crisis

BIS: Borio + Lowe (2002), Borio + Drehman (2008)

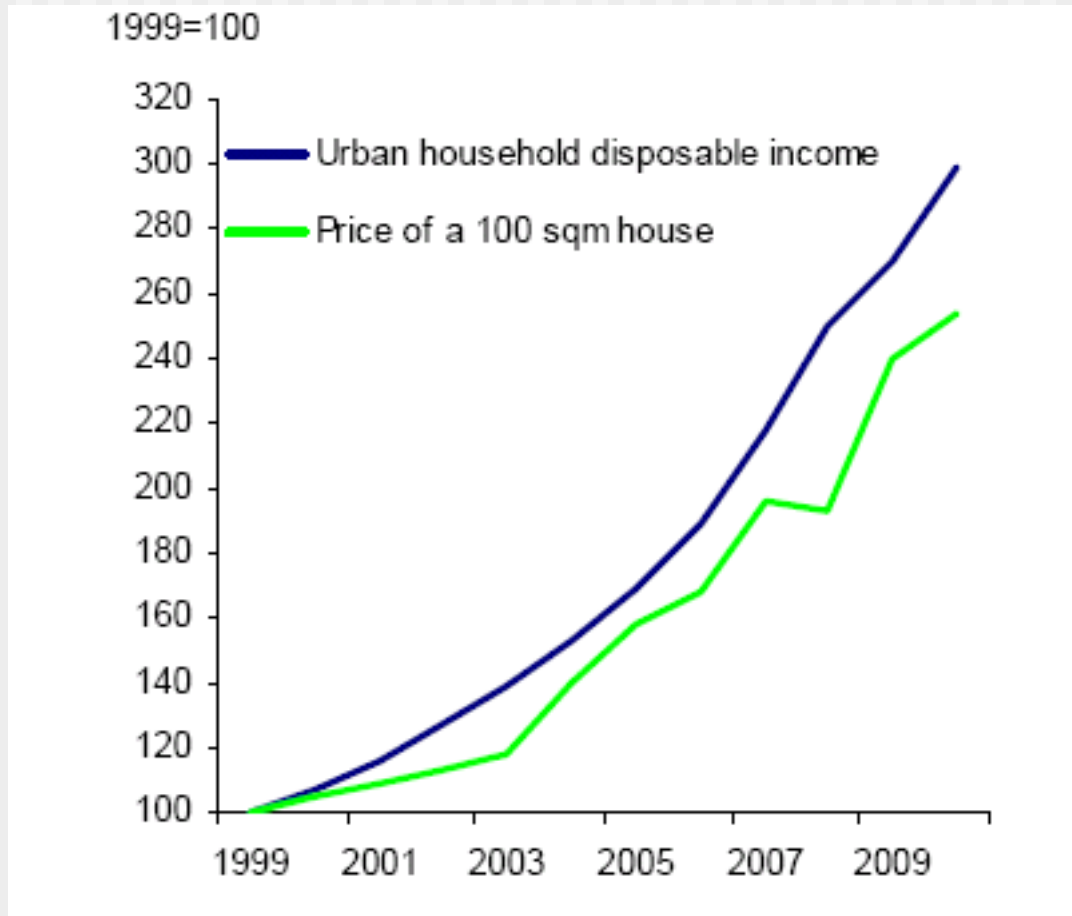
- Housing Price + Bank Credit:
 - Excessive Growth is Strong Early Warning Signal to Banking Crisis.
- Crisis Early Warning Signal: Gap Analysis
(the accumulated size of the variable departing from its long-term trend value)
 - ◆ Housing Price Gap $\geq 15\%$ or Stock Index Gap $\geq 60\%$
 - ◆ Credit Gap $\geq 6\%$
- Forecast Accuracy of Banking Crisis within 2 Years is 69%, Error Rate is 13%.

Housing Price in China

2001-2010 National Price Index of Real Estate Sales (%)

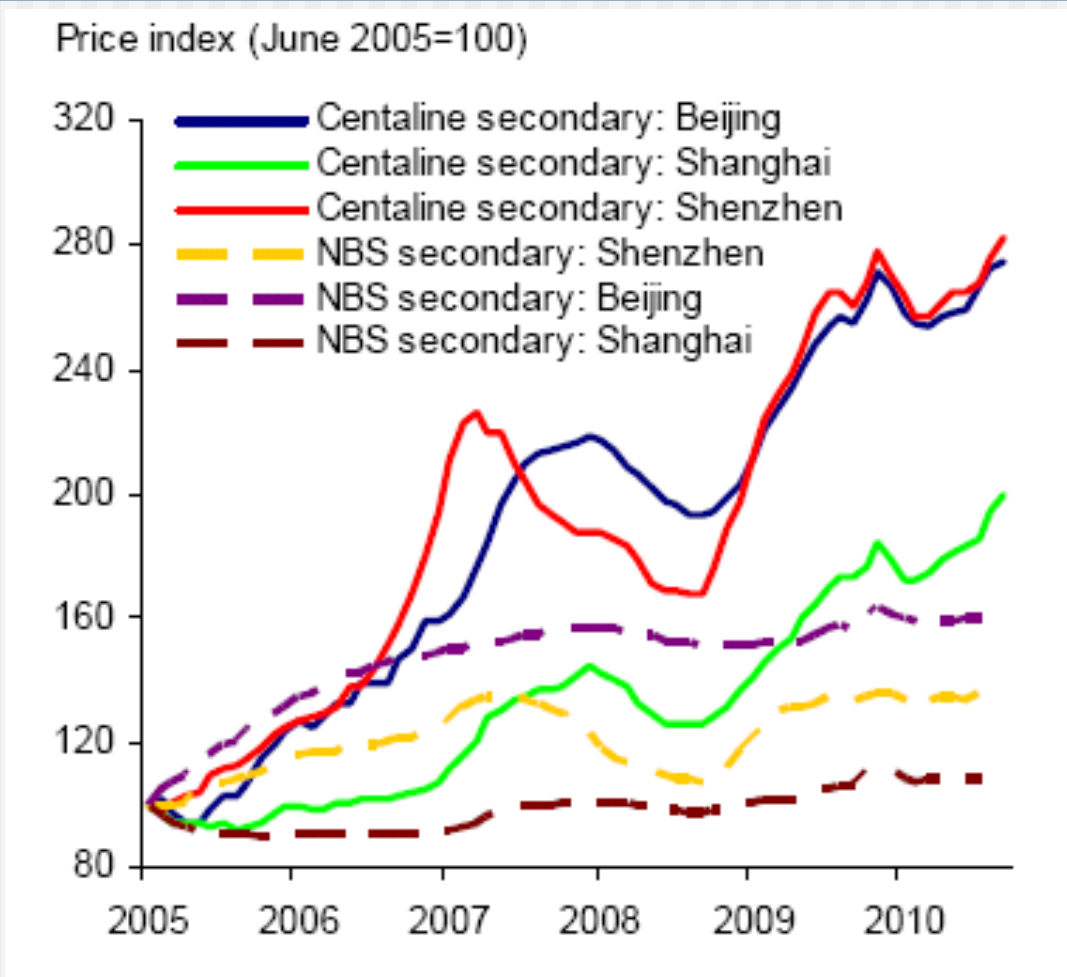


Housing prices have outpaced household income



Source: CEIC, UBS estimates

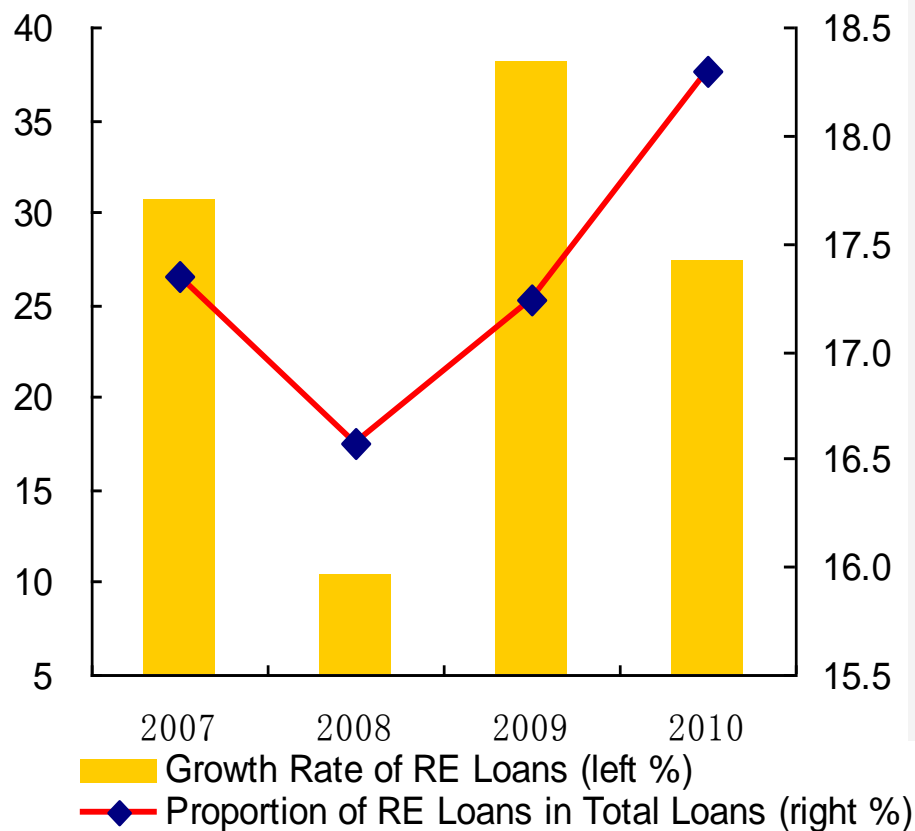
Housing prices increased dramatically in large cities



Source: CEIC, Centaline, UBS estimates



Loans to Real Estate Sector

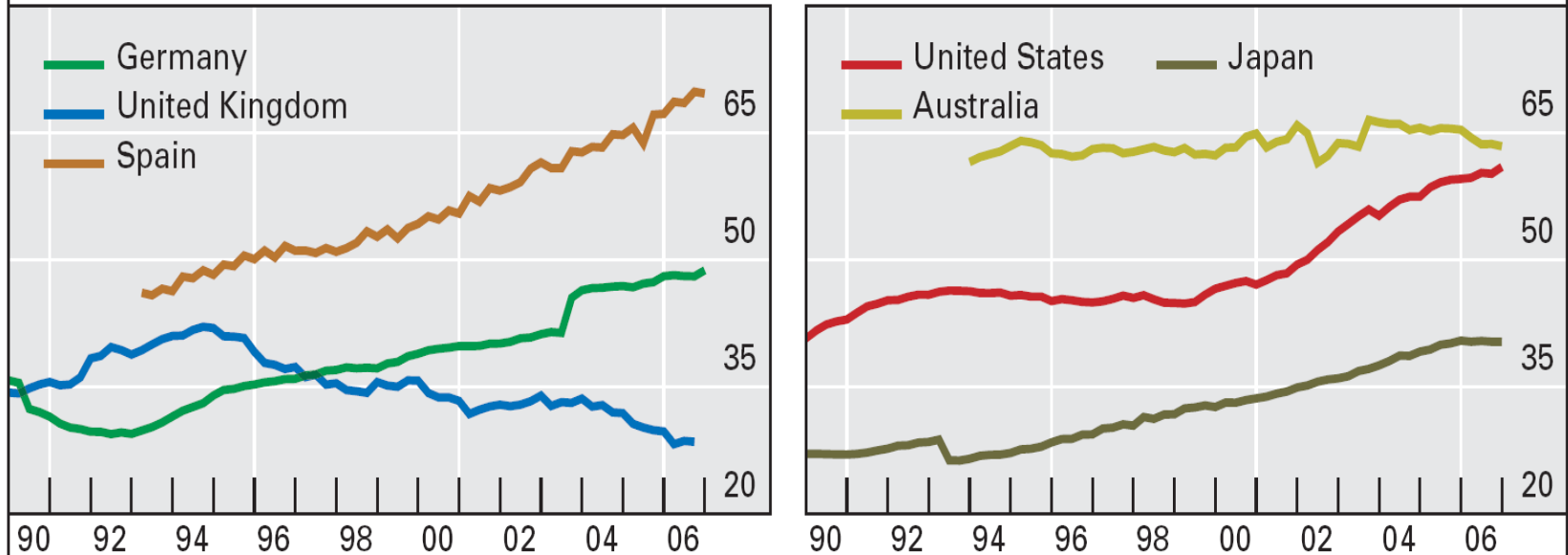


- Loans to real estate sector registered a YoY growth of 38.1% as of end-2009, the peak in recent years.
- RE loans account for more than 30% of the total in some Banks.



International Comparison

Banks' real estate exposure¹



¹ Ratio of banks' real estate-related lending to total lending. Definitions vary across countries.

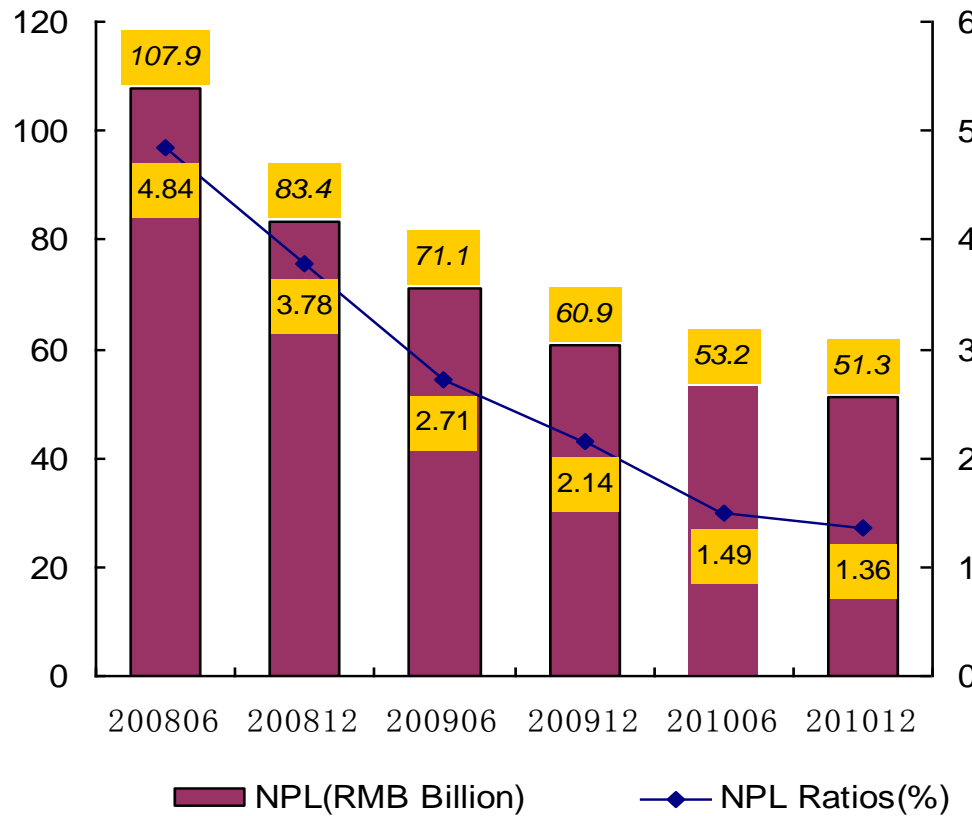
Source: National data.

Graph VII.5



The NPLs of Real Estate Sector is low, but potential risk should not be neglected

NPL Balances & Ratios



■ As of end-2010, the NPL balance and ratio registered RMB51.3 billion and 1.4% respectively.



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Enhanced supervisory intensity on real estate exposures

- **Supervisory advisories on risks in real estate sector**
- **More stringent LTV**
- **Prudential Debt Income Ratio**
- **Targeted on-site examinations**
- **Stress test**

CBRC's Regulatory Measures on RE (1): LTVs, Interest Rate (IR) and Debt Income Ratio (DIR)

	LTV	Interest Rate	DIR
Before Jun 2006	Economy housing $\leq 80\%$ Ordinary housing $\leq 70\%$	$\geq 85\%$ of Benchmark IR	$\leq 50\%$
Jun 2006 ~ Sep 2007	≤ 80 for the first home purchase if the floorage ≤ 90 sq.m $\leq 70\%$ for others	$\geq 85\%$ of Benchmark IR	
Sep 2007 ~ Nov 2008	$\leq 80\%$ for the first home purchase if the floorage is ≤ 90 sq.m $\leq 70\%$ for the first home purchase if the floorage is > 90 sq.m $\leq 60\%$ for the second home purchase	$\geq 85\%$ of Benchmark IR for the first home purchase; $\geq 110\%$ of Benchmark IR for the second	



CBRC's Regulatory Measures on RE (1): LTVs, Interest Rate (IR) and Debt Income Ratio (DIR)

	LTV	Interest Rate	DIR
Nov 2008 ~ Dec 2009	<p><=80% for the first home purchase or the second for improvement</p> <p><=60% for others</p>	<p>>= 70% of Benchmark IR for the first home purchase or the second for improvement</p> <p>For others: risk-pricing based on Benchmark IR</p>	<=50%
Jan 2010 ~ Apr 2010	<p><=80% for the first home purchase</p> <p><=60% for the second</p>	strictly adopt risk-pricing mechanism	



CBRC's Regulatory Measures on RE (1): LTVs, Interest Rate (IR) and Debt Income Ratio (DIR)

	LTV	Interest Rate	DIR
Apr 2010 ~ Sep 2010	<p><=70% for the first home purchase if the floorage is > 90 sq.m</p> <p><=50% for the second home purchase</p> <p>Based on risk, LTV declines to a great extent for others</p>	<p>>= 110% of Benchmark IR for the second home purchase</p> <p>For others: Based on risk, IR increased significantly</p>	<=50%
Sep 2010 ~ Jan 2011	<p><=70% for the first home purchase</p> <p><=50% for the second</p> <p>Hold for release for others</p>	<p>>= 110% of Benchmark IR for the second home purchase</p>	
Jan 2011 ~	<p><=40% for the second home purchase</p>	<p>>= 110% of Benchmark IR for the second home purchase</p>	



CBRC's Regulatory Measures on RE (2): Mortgages Requirement

- Banks should:
 - Strictly guard against illegal operations and fraudulent mortgages; Strictly conduct due diligence on home buyers and go through operational procedures such as “face to face talk”, “face to face contract signing;
 - Shall not pay commissions to housing brokers based on the percentage of the value of the mortgage; shall not outsource key businesses, including due diligence and credibility review, to brokers;
 - Manage LTVs dynamically and adopt a differentiated interest rate policy, with a view to warding off risks and speculations.

CBRC's Regulatory Measures on RE (3): Loans to Land Reserves

■ Banks Should:

- Well assess the credibility of local governments;
- Ensure the loans to be used to acquire land;
- Conservatively control the LTV.

CBRC's Regulatory Measures on RE (4): Loans to Developers

- Banks Should:
 - Attach great importance to the qualification and credibility of developers;
 - Pay high attention to the management of collaterals, i.e. buildings under construction, and keep the cashes recovered from housing sales in a closed account;
 - Closely monitor and assess the capital adequacy and proprietary funds of developers, and strictly control the LTVs in a dynamic manner;
 - Comprehensively evaluate developers, their parent companies and project companies before extending credit, including reviewing the legitimacy and adequacy of their capitals at the group level;
 - Keep close eyes on developers that acquire land by high prices, and on group companies that enter into real estate market astray from their core businesses, including monitoring their asset/liability ratios, capital management and fund chains, and strictly controlling their leverage ratios.



CBRC's Regulatory Measures on RE (5): On-site Examination

- CBRC conducts regular on-site examination to examine credit risk of RE loans.
- From 20th Sep. to 10th Oct. in 2010, CBRC's local offices conducted Special On-site Examination on the Implementation of the Differentiated Policy on Residential Mortgage in Beijing, Shanghai, Hangzhou, Shenzhen, Nanjing, Guangzhou, Xiamen and Sanya.
- From 20th Sep. to 30th Sep. in 2010, CBRC and the Ministry of Housing and Urban-Rural Development (MOHURD) jointly examined the Implementation of the Differentiated Policy on Residential Mortgage in the above mentioned eight cities.



CBRC's Regulatory Measures on RE (6): Stress Testing

■ May 2010, 1st Stress Test

Risk Factor	Low Pressure	Medium Pressure	Hard Pressure
Housing Price	X1 ↓	X2 ↓	X3 ↓
Benchmark IR	Y1 ↑	Y2 ↑	Y3 ↑

■ May 2011, 2nd Stress Test

Risk Factor		Low Pressure	Medium Pressure	Hard Pressure
Housing Price	High Risk Cities	S1 ↓	S2 ↓	S3 ↓
	Others	T1 ↓	T2 ↓	T3 ↓
Transaction Area		V1 ↓	V2 ↓	V3 ↓
Benchmark IR		W1 ↑	W2 ↑	W3 ↑



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A Package of Policies

- **Land Policies**
- **Taxation Policies**
- **Administrative Measures**
- **Financial Regulation**



Land Policies

- Land supply for medium-low price, small-medium dwelling-size (including affordable housing) and low-rent housing should account for more than 70% of total residential land supply annually.
- Land purchase by developers must be through fair auction.
- Terminate land supply of luxury villas, large dwelling-size housing and other strictly restricted lands.
- Levy on the land that has not been developed over 1 year after the contract agreement.
- Withdraw of the land that has not been developed over 2 years after the contract agreement.

Taxation Policies

- Dynamic Adjustment of Sales Tax on Property
- Property Tax Pilot Program in Shanghai & Chongqing
 - ◆ Shanghai: Rate 0.6%, Tax base: per capita living space ≥ 60 sq.m;
 - ◆ Chongqing: Rate 0.5-1.2%, Tax base: Transaction Price of Property.

Administrative Measures

➤ Purchase Restriction

There have been 41 cities, including Beijing, Shenzhen, Xiamen, Shanghai, Guangzhou, etc, that have taken restrictive measures of property purchase.,

➤ Set Limit on Housing Price

Local governments are required to set limits on housing price of new property:

- ◆ Shanghai: the growth of housing prices should be lower than the growth of local GDP and disposable income.
- ◆ Beijing: keep housing price stable with slight decline.

Cross-ministry Joint Meeting Mechanism

- The Cross-ministry Joint Meeting Mechanism under the State Council:
 - Lead Ministry:
 - ◆ Ministry of Housing and Urban-Rural Development (MOHURD);
 - Other members:
 - ◆ Ministry of Land and Resources (MLR), (National Development and Reform Commission) NDRC, Ministry of Finance (MOF), People's Bank of China (PBOC), State Administration of Taxation (SAT), National Bureau of Statistics (NBS) and CBRC;
 - Mission:
 - ◆ Monitoring the development of real estate market;
 - ◆ Communication and coordination among ministries;
 - ◆ Drafting policies and submitting them to the State Council for approval.



Challenges

- How Do We Define Bubbles?
- Market Vs Government?
- How to Construct Accurate Price Index?

THANK YOU !

