



S&P: Success Of China's Property Intervention Hinges On Homebuyer Confidence, Report Says

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S&P Global
Ratings

Press Release

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HONG KONG (S&P Global Ratings) Dec. 5, 2022--Policy-driven, bank-led property lending will not fully reverse residential price declines in China. We forecast average national sales will drop by up to 8% next year. That's according to article we published today, titled "China Property Lifeline Won't Stretch To All."

"Banks have reasonable collateral buffers on real estate loans on average," said S&P Global Ratings credit analyst Harry Hu. "However, our sensitivity tests show sharp housing price corrections, exposure to regional weak spots, or even a change in valuation methods would leave banks holding more vulnerable loans."

We estimate loan-to-value (LTV) ratios on property development loans average about 50% at the national level. This implies sufficient room to absorb the circa 6% home price decline this year and up to 8% next year, as per our estimates.

Yet lower-tier cities may see sharper drops in valuation changes, thereby reducing the safety offered by the collateral. Also, some small regional banks have been more aggressive in granting these loans, with higher LTV ratios.

In our view, financial institutions will retain some selectivity as megabanks lead the efforts with plans to disperse more than Chinese renminbi 1.8 trillion (US\$256 billion) in fresh loans. For developers, it means survival of the fittest, as the stronger ones will get favorable treatment.

"The strongest developers will find it easier to obtain new bank lines," said S&P Global Ratings credit analyst Esther Liu. "Credit divergence thus will widen."

Recent policy initiatives give relief to homeowners waiting on pre-sold units to complete. Real estate rescue funds and other related special-funding targets are not designed to bail out troubled developers. Moreover, this new financing will get repayment priority--at the expense of existing secured creditors.

For banks, increased exposure to the risky property sector won't immediately appear in reported results, due to forbearance policies that allow banks more flexibility on classifying overdue loans as nonperforming. The delay in recognizing nonperforming loans and the provisions could embellish short-term profit and asset quality indicators for banks, though we expect a fair share of such loans would eventually become nonperforming if forbearance does not help borrowers recover.

Moreover, banks in China are generally not as prone as global peers to execute fire sales on collateral--an approach which benefits individual "first mover" banks, but can mean a downward spiral for broader asset prices.

This "collective stability" mindset means the chance of a hard landing for banks is remote at this stage. Still, as real estate rescue funds and other related special funding come in, project leverage will increase and collateral safety buffers wane. Pockets of regional sensitivities could chip banking sector health at the fringes. In a remoter scenario, policy missteps could lead to property risks becoming systemic.

"Ultimately, China's property ecosystem needs a buy-in from end-customers," said Mr. Hu.

Recent supports have not yet ushered in a rebound in homebuyer confidence. More visibility on the end of "zero COVID" policies would be a bigger impetus in reviving home sales, in our view.

Related Research

- [China Property Is Heading For A Transformation, And Maybe A Turnaround](#), Nov. 21, 2022
- [Global Bank Country-By-Country 2023 Outlook: Greater Divergence Ahead](#), Nov. 17, 2022
- [China Cities Diverge To Navigate Property Slowdown](#), Nov. 1, 2022
- [Banking Industry Country Risk Assessment: China](#), Sept. 13, 2022
- [Real Estate Funds, A First Aid To China's Property Slump](#), Aug. 18, 2022
- [China's Banks Face A Doubling In Real Estate NPLs](#), Dec. 15, 2021

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