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Flash Notes

China: PBoC to the Rescue

PBoC Moves to Support Housing Market

- PBoC on Tue (30 Sep) announced loosening of mortgage loan and other property-related measures, in one of its most direct efforts to prop up the country's housing market. Housing prices in China had been under pressure in the past years ever since home purchase restrictions measure started to take hold in 2010, usually taking the form of limits on housing prices and on purchases of multiple homes, as well as raising requirements for mortgages and down payments. These tightening measures subsequently spread to second and third tier cities as well, in a bid to curb excessive demand and price increases.

- Home prices have been coming under increasing downward pressure since late 1Q14 as the broader economy slows down. For instance new home prices fell on m/m basis in 68 of the 70 cities in Aug, up from 64 cities in Jul. This is sharp jump compared to the Nov 2013-Mar 2014 period when only an average of about 3 cities each month faced with falling prices.

- In response to such downward pressure, as far back as Apr 2014, there were already signs that smaller cities in China were loosening property market measures on their own, led by city of Wuxi, apparently with tacit consent from the central government.

- For instance, Tongling in Anhui and Ningbo, in Zhejiang began providing tax subsidies to first-home buyers, and cut down-payment rates to 20% from 30% for select buyers. In the subsequent months, more cities joined in the fray. This is unlike in 2011, when the central government compelled Foshan, in Guangdong to reverse an earlier decision to partially ease the city's property- purchase restrictions.

- Currently, there only 4 tier one cities (Beijing, Shanghai, Guangzhou, and Shenzhen), out of the 46 cities that had restrictive policies, are holding to home purchase restrictions. As such, the latest measures from PBoC should be seen in the context of formalization of the progress taking place over the past 6 months.

Loosening of Mortgage Loan and Related Measures:

- Briefly, here are the latest measures from PBoC:

  1) Purchasers of second homes could now be considered as first-time home buyers, giving them access to lower down payments and mortgage rates. To qualify, the home buyers have to pay off any existing mortgage debt from their existing homes, thereby allowing them to enjoy first-home measures such as a minimum down payment of 30% and the mortgage interest rate at 0.7 of the benchmark lending rate (In comparison, non-first home purchasers are subjected to down payment of at least 60% and mortgage rates of at least 1.1x benchmark rate).

2) Banks are encouraged to issue MBS and other long-term special financial bonds to fund their mortgage portfolios to satisfy first-home or upgrading demand.

3) Financial institutions are also encouraged to lend to property developers with reasonable limits and risk parameters, and by increasing financing channels via bond funding and to develop pilot programs for REITs.

4) The major impetus is actually contained in the first paragraph of PBoC's statement, where it urges increased financial support for social housing and shantytown redevelopment with stronger support from banks, including allowing loans tenors of up to 25 years, as well as inclusion of redevelopment loans for housing projects coordinated by local governments to be classified in "financial development" category, for preferential regulatory treatment.

- The latest move marks the first direct action by the central government this year. Prior to the announcement it had largely allowed local governments to loosen local curbs against big price jumps and property speculation and jawboned banks into make more mortgage loans.

- A report in August by Kansas City Federal Reserve Bank ("China's Slowing Housing Market and GDP Growth;" Aug 2014, http://www.kc.frb.org/publicat/research/macrobulletins/mb14Nie-Cao0825.pdf) highlighted the difficulty in managing the current slowdown in China. The report suggested that given the real estate sector accounts for about 15% of China's GDP, and if real estate investment growth pace maintains its 11% growth pace of 1H2014 vs. 17% pace in 2013, the impact would see China's headline GDP expansion slowing to 6.8% in the absence of any stimulus measures, which is well below that of the official target of 7.5%.

- The latest announcement came on the back of recent slowdown in non-real estate sectors such as manufacturing (which accounts for about more than 30% of China's GDP), with manufacturing PMI hovering at just around the 50 levels. Whether these measures would have a significant impact on broader economy remains to be seen, but it is conceivable that risks of hard landing are further reduced.

- For now, we are keeping to our full year forecast of 7.4% for 2014, and 7.5% for 2015. We also expect no change to China's policy rates for now as targeted measures look to be preferred tools. We look for the headline RRR for major banks to remain at 20%, and benchmark deposit and lending rates unchanged at 3% and 6%, respectively. We are also keeping to our end-2014 RMB forecast to 6.10/USD.

- As China is on its National Day Golden Week holiday (1-7 Oct) and Hong Kong also away for National Day (Wed-Thur), market reaction will be only visible on Fri the earliest. Nevertheless, the latest news should be positive for property developers and other property- and home-related sectors.

Further details on PBoC announcement:
http://www.pbc.gov.cn/publish/goutongjiaoliu/524/2014/20140930160525301502298/20140930160525301502298_.html