China’s real estate crisis deepens amid homebuyer boycott movement

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The crisis in China’s property market, exemplified by the default of Evergrande, the country’s most indebted real estate developer last November, is spreading. It is threatening a significant fall in economic growth under conditions where the government is battling to deal with the effects of the COVID pandemic.

Over the past few weeks, a home-buyer boycott movement has developed in which purchasers are refusing to continue payments for apartments they have purchased but which are still under construction.

In the past, the pre-delivery sales agreements have been a mainstay for property development as real estate companies have received money for projects not yet completed, enabling them to finance the next one.

The movement is extending with the Australian Broadcasting Corporation (ABC) reporting that hundreds of smaller companies involved in property development are threatening to halt loan payments because they are not receiving payments from the major developers.

The ABC cited a joint statement signed by a group of suppliers to Evergrande in Hubei province saying they are “broke” and will stop paying loans. Addressed to banks and provincial authorities, the statement said: “Evergrande should be held responsible for any consequence that follows because of the chain reaction of the supply-chain crisis.”

While the home-buyer boycott movement is so far relatively small in relation to the total market—the *Financial Times* reported earlier this month that some 300 projects were involved—its growth has sparked concern at top levels of the government.

The FT reported on Monday that China’s State Council last week passed a plan to establish a real estate fund worth up to 300 billion renminbi ($44.4 billion) to support at least a dozen property development companies.

Initially the China Construction Bank and China’s central bank will inject 80 billion renminbi into the fund, and then possibly to 300 billion renminbi, to revive stalled construction projects.

The amounts of money involved are not small. According to a report published by Bloomberg on Monday: “Construction halts may affect 4.7 trillion yuan worth of homes in China, and up to 1.4 trillion yuan, or about 1.3 percent of the nation’s gross domestic product, may be needed to complete them.” [The yuan is another name for the renminbi.]

The Bloomberg report noted that while halted real estate projects were not unheard of “the depth of the current turmoil is unprecedented.”

The move by the State Council came a week after the city of Zhengzhou set up a property developer development fund, backed by the financial arms of the local government authority, in response to the growing home-buyer boycott movement.

The extent of the crisis was revealed in a report earlier this month in the FT that developers in some parts of China had agreed to accept garlic, as well as watermelons, barley, and wheat as down payments from farmers on new apartments.

One real estate agent in Zhengzhou, the capital of the Henan province, said that, despite home prices falling to record lows, market activity was depressed.

The Henan province was also the scene of protests on July 10 when hundreds of people protested after deposits totalling 40 billion renminbi had been frozen by four rural banks. The protests were defused when Chinese banking regulator, Liu Rong, promised that protestors who had lost money due to fraud would be reimbursed.

The issue attracted the attention of the representatives of global capital and finance. According to analysts at the US bank Citi, whose remarks were reported in the FT: "We are not worried about the rural banks in Henan per se. However, the situation could worsen if the public were to start worrying about other banks, especially some of the larger financial institutions."

The real estate crisis is having major financial effects, especially in the higher yield or junk bond market. A report by Bloomberg earlier this month said that the housing woes were hitting every corner of the real estate industry "with distress signs once again flashing in debt markets."

Pessimism, it said, had become so entrenched that a property firm that had been the subject of a state rescue in May suffered major losses in the dollar bond market.

Bloomberg Intelligence analyst Daniel Fan said: "Investors are concerned that it's just a matter of time for liquidity stress to spread to larger, healthier developers. If the offshore refinancing channel remains shut, the continued repaying of debt with their own cash is not a sustainable strategy and will eventually hurt cash flow."

Meanwhile the situation at Evergrande goes from bad to worse. The company announced last Friday that its CEO Xia Haijun had been forced to resign as the result of an investigation into how 13.4 billion renminbi of deposits ($2 billion) were used as security for third parties to obtain bank loans, some of which the borrowers failed to repay.

Evergrande is due to announce a restructuring plan by the end of the month. It has around $300 billion worth of liabilities, of which around $20 billion are in dollar-denominated bonds. At this stage creditors have no idea as to how, or even if, they will be repaid. The nature of the restructuring agreement will be critical for the maintenance of confidence in financial markets more broadly.

It has been estimated that real estate firms that have issued high-yield debt need to repay a total of $3.7 billion in offshore bonds and $6.1 billion worth of domestic debt between July and September.

The turmoil in the real estate sector and associated financial markets is exacerbating the mounting problems in the economy as a whole. Annualised growth in the June quarter was only 0.4 percent, meaning that China barely escaped an outright contraction.

Growth estimates for the full year have been revised down. A number of economists expect that the economy will contract in the current quarter and growth for the year will be well below the government's target of 5.5 percent, which was itself the lowest for 30 years.

Analysts at the Japanese financial firm Nomura have repeated the widely held view that "some fundamentals" may be worse than official data claim. It noted that the road freight index, a key gauge of economic activity, is down 20 percent over the past year and new home sales have dropped by a third.

There has been a significant rise in the number of unemployed young people, with the jobless rate for those aged between 18 and 24 rising to a record high of 18.4 percent. At least 10 million university students are coming on to the jobs market in the next few weeks.

The growing economic crisis will have political ramifications. The Xi Jinping regime, which represents the Chinese financial oligarchy, has sought to base itself on sections of the middle class that have been able to make gains from the full-scale restoration and development of capitalism initiated at the end of the 1980s.

But growing numbers of this social layer, which collectively has an estimated 70 percent of its wealth tied up in housing, are being hit, under conditions of a marked slowdown in economic growth and the contraction of job opportunities.

In the past, the response of the regime would have been to initiate economic and financial stimulus packages. But this road is being increasingly closed off under conditions of rising and increasingly unstable debt and the tightening of interest rates globally by the major central banks.