ASIA MONTHLY

September 2021

株式会社 日本総合研究所

https://www.jri.co.jp/en/reports/asia/

This report is the revised English version of the September 2021 issue of the original Japanese version (published 26th Aug.).

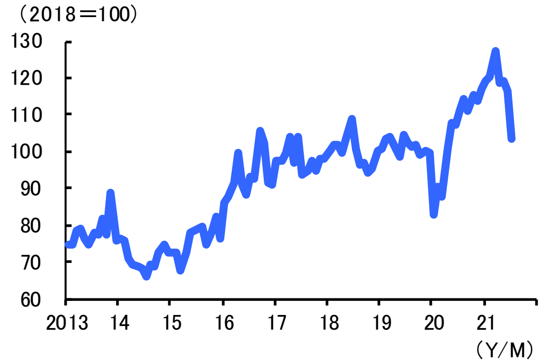
Topics The Chinese real estate market is headed for a soft landing

The Chinese real estate market has entered a correction phase following the government's measures to prevent it from overheating. For the time being, serious adjustments are unlikely to occur and the market is expected to make a soft landing. On the other hand, many problems remain to be solved for medium- to long-term growth.

■ China's real estate market has entered a correction phase following the government's control measures

The Chinese real estate market has entered a correction phase. Housing floor space for sale in July decreased 18.7% from its most recent peak in March (see the figure on the right). The increase in investment in real estate development is also slowing down, and the land area acquired by real estate companies has been significantly below the previous year's level. Sales of construction machinery also started to decrease compared to the previous year, and the average operating hours of construction machinery from Japanese manufacturers decreased 10% from the previous year. In July, the average price of new homes in 70 major cities rose 4.6% from a year earlier, a pace similar to that seen in the second half of last year. However, it is apparent that the pace of the price increases has slowed in some regions.

<China's Housing Floor Space for Sale (Seasonally-adjusted)>



Source: Prepared by The Japan Research Institute, Limited based on "National Real Estate Development Investment and Sales Report" by the National Bureau of Statistics of China

The main reason for this comes from the government's measures to curb overheating of the real estate market. For some time after the outbreak of COVID-19, overheating of the real estate market, coupled with the implementation of accommodative monetary policies, led to soaring real estate prices in some areas and a sharp increase in land acquisitions by real estate companies. The government has been taking measures to control overheating from both the supply and demand sides since the summer of 2020, fearing excessive investment and debt by real estate companies and soaring housing prices. The government implemented regulations on the total amount of housing loans and housing purchases as measures to curb demand, and tightened conditions for real estate companies to raise funds as measures to control supply.

In particular, attention has been focused on the "three red lines," which were introduced in the summer of 2020 to tighten funding conditions for real estate companies. The details of this measure have not been disclosed, but according to Xinhua News Agency, the main points are as follows. Real estate companies are classified into four categories based on three red lines: a liability-to-asset ratio of less than 70%, a net gearing ratio of less than 100%, and a cash-to-short-term debt ratio of more than 100%. The debt level of each company is restricted based on this classification. Red companies that breached all three red lines will not be allowed to increase their interest-bearing debt. Orange companies that breached two red lines will be managed and supervised so that their interest-bearing debt will increase by no more than 5% per year. The pace of increase in interest-bearing debt will be limited to within 10% per year for yellow companies that breached one red line, and within 15% per year for green companies that did not breach any of the three red lines. As a result of this measure, land area acquired by real estate companies has decreased significantly, and some real estate companies are facing the risk of bankruptcy due to difficult cash flow conditions, with attention now being paid on whether their corporate bonds will default.

The government is expected to continue to take measures to rein in the real estate market. A guideline for improving order in the real estate market announced in July 2021 indicated that China's authorities would strictly regulate violations of the government's policy in the four areas including real estate development, brokerage, rental housing, and related services over the next three years or so. In addition to the fact that the tightened regulations will cover a long period of time, over three years, it is noteworthy that more government agencies (eight government departments) are now responsible for the real estate market.

The move is likely to further slow the pace of investment in real estate development going forward. Housing sales are expected to remain below the levels seen in the second half of 2020 for the time being.

■ Serious market adjustments are expected to be avoided for the time being

Some say that the Chinese government's restraint will cause the real estate bubble to burst. However, it is judged that there will be no serious market adjustments such as a sharp drop in real estate prices and a rapid decline in investment in real estate development based on the following three points. First, on the whole, there is no significant gap between real estate prices and income growth. If real estate prices rise sharply, far outpacing income growth, they could plunge due to hitting a number of triggers. With the government controlling the real estate market both on the demand side and on the supply side, new house prices in 70 major cities increased by an annual average of 7.3% between 2015 and 2020. On the other hand, nominal disposable income in urban areas increased by an annual average of 7.0% over the same period. This indicates that the growth of housing prices is at a pace comparable to that of income. Monetary easing in response to the COVID-19 pandemic has been small, and housing prices have not risen in China as much as in the United States.

Second, the share of investment in real estate development in the overall economy has been controlled at a relatively flat level. During the period between 2008 when the financial crisis occurred following the Lehman Brothers collapse and around 2014, funds continued to flow into the real estate market and the ratio of investment in real estate development to GDP continued to rise. Amid this situation, there were concerns that in reaction, investment in real estate development could plummet at some point. However, since 2014, investment in real estate development has been controlled to a level commensurate with economic growth, and the real estate market is making a soft landing. This is largely due to the introduction in 2013 of a series of measures to curb demand, such as restrictions on housing purchases and a tax increase on capital gains, as well as supply constraints, such as curbing fundraising by real estate companies through the control of shadow banking. In recent years, the size of shadow banking, such as wealth management products (WMPs) issued by banks and trust loans as an alternative to conventional bank loans, has been shrinking, while the dependence of real estate companies on shadow banking for fundraising has also been decreasing.

Third, urbanization and higher housing quality in line with rising incomes are expected to underpin steady growth in housing demand. In recent years, the population inflow from rural areas to urban areas has been continuing at a scale exceeding 10 million people every year, but the urbanization rate in 2020 was only 64%, so a great deal of room remains for further increases. There is also great potential demand for relocation due to rising income levels. People are gradually moving from aging apartments to new ones.

■ Some issues remain to be solved for sustainable growth

On the other hand, from a medium- to long-term perspective, China's real estate market faces various challenges. First, the number of births is decreasing at a faster pace than expected by the government, and it is highly likely that the timing of the population's decline will be brought forward. In order for the Chinese real estate market to achieve long-term growth, it is essential to implement policies that take demographic trends into account, such as comprehensive child-rearing support.

In some areas, unbalanced growth can be seen, and the real estate bubble is becoming larger. Anjuke, a Chinese real estate information provider, listed areas where the real estate market is overheating. For example, in August, the price of a second-hand house in Nanjing West Road in Shanghai was 132,129 yuan (about 2.25 million yen) per square meter, up 27.4% from the same month last year. On the other hand, a second-hand house in Roppongi, Minato Ward, Tokyo, is priced at 1.34 million yen per square meter (according to a survey by MANSION MARKET Inc.) Given this, we cannot rule out the possibility that major price adjustments will occur in these areas. It is necessary to stabilize housing prices in these areas and aim for balanced growth.

Third, attention should be paid to the uneven distribution of real estate assets. According to the "China Housing Stock Report 2021" compiled by Ren Zeping, Chief Economist at Soochow Securities, the top 10% of households with the highest income levels in 2015 use 19.6% of total urban residential floor space. On the other hand, the bottom 20% of households with the lowest income levels use only 7.2% of the total. Rectifying this disparity through the introduction of property taxes and inheritance taxes is a long-term task. As described above, the Chinese real estate market is expected to enter a period of adjustment and move toward a soft landing, but various issues must be resolved in order to achieve sustained and balanced growth going forward.

(Shinichi Seki)

Topics What is India's aim in introducing e-RUPI?

In August 2021, the Indian government announced the introduction of e-RUPI, a new electronic payment system. The main purpose of the system is to provide fast and reliable subsidies to people in distress due to the COVID-19 pandemic.

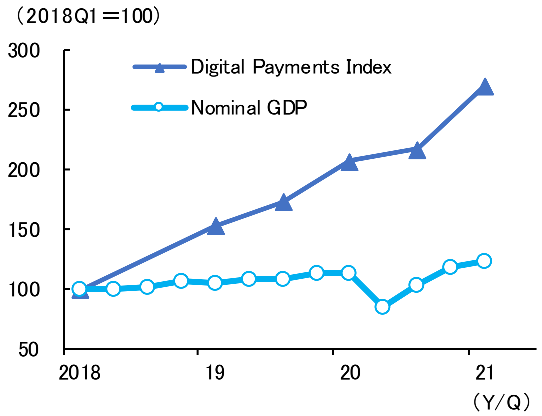
■ India is digitizing its financial services

Since the inauguration of the Modi administration in 2014, the Indian government has been making various efforts to digitize financial services. Behind this endeavor is the high social cost of cash settlements. Specifically, in addition to the costs involved in the production, distribution, and storage of cash, there are problems such as illicit accumulation of wealth, tax evasion, and counterfeit banknotes. Another problem has been the lack of adequate cash transfers for low-income earners due to inefficient administration and corruption. In order to overcome these challenges, the government is promoting the digitalization of financial services from two aspects: 1) improving access to banking services by low-income earners; and 2) strengthening regulations on cash use.

With regard to the former, in August 2014, the government announced Pradhan Mantri Jan Dhan Yojana (PMJDY). This is a campaign to promote the opening of special accounts with waived account maintenance fees and free benefits such as non-life insurance and life insurance. By introducing Aadhaar, a new national ID using biometric technology, financial transactions became enabled for people who had difficulty opening bank accounts due to a lack of literacy and official identification documents. As a result, more than 400 million new accounts have been opened to date. When PMJDY was first launched, there was criticism that the increase in the account ownership ratio did not lead to the improvement of economic efficiency through financial intermediation or a reduction in poverty because financial transactions after opening accounts were limited. However, when subsidies for low-income earners were switched from cash transfers to direct bank deposits, financial transactions became active, leading to reductions in administrative costs as well as corruption. As these moves increased opportunities for commercial banks to obtain deposits and profits, they aggressively launched account opening campaigns.

Next, regarding regulations on cash use, in 2016, when purchasing jewelry with a value exceeding a certain amount, it was necessary to present a Permanent Account Number (PAN). In addition, in November of the same year, 500-rupee and 1,000-rupee notes, which had accounted for more than 80% of the cash in circulation, were suddenly abolished. The delay in the supply of new notes temporarily caused great confusion in the Indian economy and society, but on the other hand, it also triggered expansion of the use of mobile banking and other digital services. The introduction of regulations on cash transactions totaling 300,000 rupees or more in 2017 also prompted the digitalization of financial services. In addition, restrictions on activities in the wake of the COVID-19 pandemic have accelerated the digitalization of financial services through the expansion of online transactions. While India's economy declined sharply due to the severe lockdowns imposed through the first half of 2020, the Digital Payment Index, which measures the state of digitalization of financial services in a comprehensive and quantitative manner, has been rising (see the figure on the right).

＜Digital Payments Index and Nominal GDP＞



Source:Reserve Bank of India,Ministry of Statistics and Programme Implementation

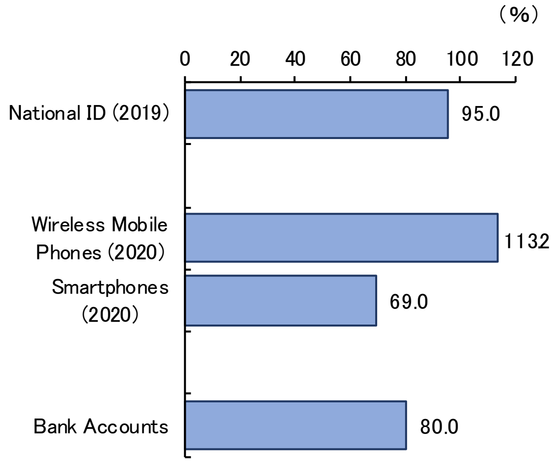
■ Why is the Indian government introducing e-RUPI?

Amid these circumstances, the Indian government announced in August 2021 that it would soon introduce e-RUPI, a new electronic payment system. The government plans to use the electronic payment system provided by National Payments Corporation of India (NPCI) to provide electronic coupons for social welfare services through QR codes and SMS.

As for the key features of the system, compared to conventional subsidy payments, receiving and using e-RUPI does not require a bank account. Beneficiaries receive goods and services by presenting electronic coupons sent to their mobile phones, and providers of goods and services receive compensation from the government through financial institutions.

One reason the government wants to switch from transferring subsidies into bank accounts to providing electronic coupons to mobile phones is that mobile phones are more widespread than bank accounts. The Indian government is promoting JAM trinity, which links bank accounts (Jan Dhan Yojana), national ID (Aadhaar), and mobile phones, in order to improve the efficiency of administrative services. However, in reality, a significant number of people who have national IDs and mobile phones do not have bank accounts. According to a World Bank study, the percentage of people aged 15 and older with bank accounts increased from 53% in 2014 to 80% in 2017, mainly due to the opening of bank accounts by low-income earners as a result of PMJDY (see the figure on the right). The bank account ownership rate has been on an upward trend since then, but it is estimated that around 10% still do not have bank accounts. On the other hand, with regard to mobile phones, while the penetration rate of smartphones is about 70%, which is lower than that of bank accounts, the number of wireless mobile phone subscriptions, including feature phones (so-called "Galapagos phones" which had been popular before the widespread use of smartphones), is approximately 1.2 billion, exceeding the population of people aged 15 years and over (approximately 1 billion people), and it is possible to offer coupons through e-RUPI by sending SMS to a wide range of users. Therefore, by introducing e-RUPI, the government aims to provide subsidies quickly and reliably to people in distress due to the COVID-19 pandemic, while controlling the risk of virus spread. The introduction of e-RUPI is also believed to be aimed at ensuring the minimum standard of living for low-income earners by limiting spending on luxury goods and gambling through the distribution of electronic coupons.

＜Penetration of National ID, Mobile Phones and Bank Accounts＞



Source:JRI based on State of Aadhaar "State of Aadhaar 2019"、World Bank "Global Findex"、Counterpoint "India Monthly Smartphone Market Analysis, September 2020"、Telecom Regulatory Authority of India、United Nations "World Population Prospects 2019"

Finally, let’s look at the relationship between Central Bank Digital Currencies (CBDC), which has attracted attention from other countries, and e-RUPI. e-RUPI, which has limited use and cannot be transferred to others, does not fall under the category of CBDC, which functions like cash. While the government may expand the provision and use of e-RUPI for further digitalization of the economy and society in the future, e-RUPI will not replace India’s existing currency unless financial functions such as deposits, remittances and borrowing are incorporated into it. This means that it is important to continue efforts to improve the existing financial infrastructure, even as the use of e-RUPI increases going forward.

(Shotaro Kumagai)