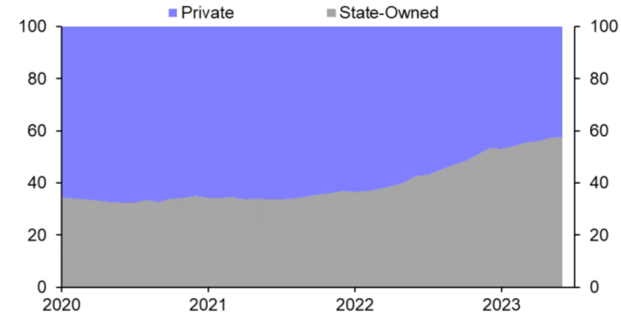
CHINA ECONOMICS UPDATE

China's property sector is increasingly state-led

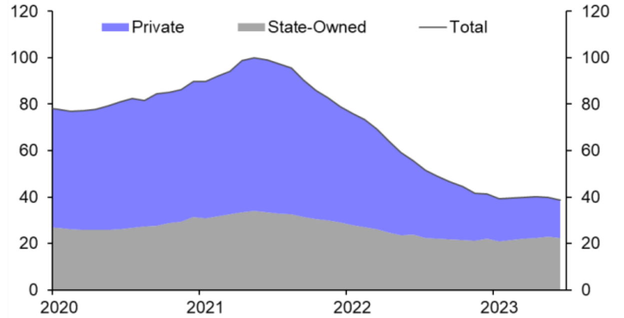
- **The property downturn has left state-owned developers the dominant players in a previously privately-led sector. The state is likely to continue playing a larger role as consolidation continues around more financially-secure firms.**
- Based on a sample of 50 major developers, we estimate that **privately-owned developers have historically generated around two-thirds of property sales. That share has fallen over the past couple of years to under half.** (See Chart 1.) In 2022, seven of the 10 developers with the largest sales were state-owned.
- **This shift in relative standing is the result of a slump in private developer sales; sales by states firms have stayed relatively resilient.** (See Chart 2.) For example, sales by major private developers like Evergrande, Sunac and Shimao Group have collapsed 90% since mid-2021. In contrast, sales by state-owned juggernauts Poly Real Estate and China Overseas Land and Investment have fallen only around 25%.
- **In turn, this divergence is the result of the more favourable regulatory and financial circumstances of state firms which have led to buyers of new property trusting them over more distressed private firms.**
- First, the "Three Red Lines" disproportionately constrained private developers since they had been more aggressive and taken on more leverage over the previous decade.
- Second, at any degree of leverage, state firms have continued to find it easier to access financing, whether from banks or the bond markets. State firms have always had preferential access to the onshore bond market, which hasn't experienced a major sell-off. Private firms always relied far more – both for reasons of access and convenience – on the offshore market, where investor interest and prices have collapsed.
- **This dynamic has become self-reinforcing: both homebuyers and creditors want to limit their exposure to more stressed private firms, which has only made these firms' situation worse.** State firms are perceived to benefit from state-backing and so seen as more credit-worthy all round.
- A final driver of the market restructuring has been the push by local and central governments to have state developers merge with distressed counterparts or to buy their projects as an alternative to government bailouts of developers (although it appears that state developers have not responded as enthusiastically as officials might have hoped).
- All of these factors are likely to continue to constrain private developers and help state-owned competitors further raise their market share. **The sector that emerges from the crisis will be one in which the state is dominant**. This will improve developer access to cheap funding and provide a backstop to public confidence. But state-owned developers are typically less responsive to market signals around design, build quality and location, and more likely to respond to political pressure about where projects should be built. **A state-led housing sector should be less prone to debt-fuelled overexuberance but may be more prone to wasteful, misallocated investment.**

Chart 1: Property Sales by Developer*
(% of total area sold, 12m rolling average)



*Based on data from 50 major developers

Chart 2: Property Sales by Developer*
(area, May 2021 total = 100, 12m rolling average)



Sources: Wind, Capital Economics

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