Global Economic Policy Lab

China's Real Estate Crisis: Structural Challenges and Policy Limitations

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Key Messages

China’s real estate market remains deeply troubled. While falling home prices may appear to offer an attractive entry point for investors, the market suffers from underlying structural challenges and difficulties in recovery. Persistent oversupply, weak demand, and a heavily indebted development sector continue to exert downward pressure, making a sustained price rebound highly unlikely. For years, China’s property sector fueled economic expansion, but excessive reliance on debt and speculative investment created vulnerabilities that policy adjustments alone cannot resolve. This research note argues that without deeper reforms addressing debt sustainability, fiscal dependence on land sales, and homebuyer confidence, real estate prices may remain depressed for the foreseeable future.

The Anatomy of the Chinese Real Estate Crisis

China’s real estate sector, contributing approximately 30% of GDP, is in a severe downturn. Housing sales have plummeted (Figure 1), and an increasing number of developers are going bankrupt (Figure 2). The crisis has created systemic risks affecting financial institutions, local government revenues, and household wealth.

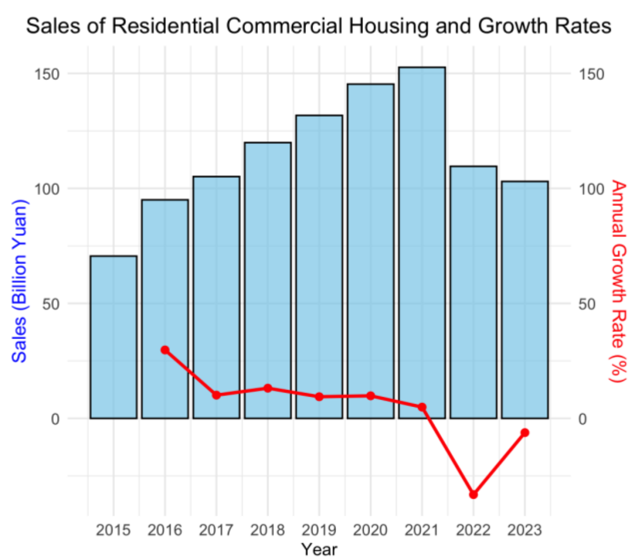

Figure 1 – Sales of Residential Commercial Housing and Growth Rates
Source: NBS

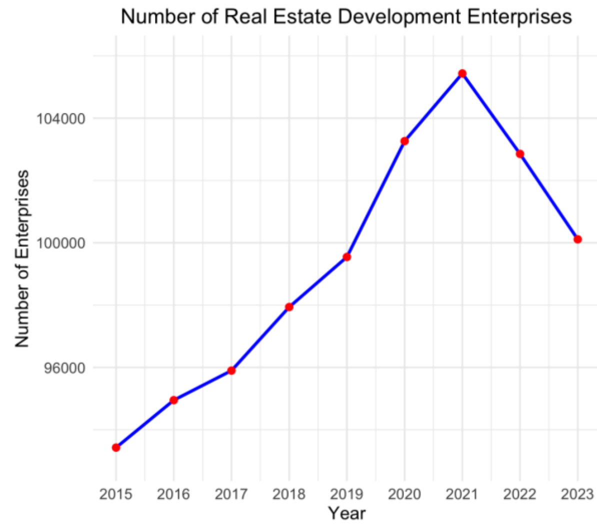

Figure 2 – Number of Real Estate Development Enterprises
Source: [NBS]

What Caused the Crisis?

The primary cause is the slowdown in urbanization (Figure 3). China has nearly exhausted its developable land after decades of rapid expansion, leading to a stagnation of the urbanization rate and declining housing demand.

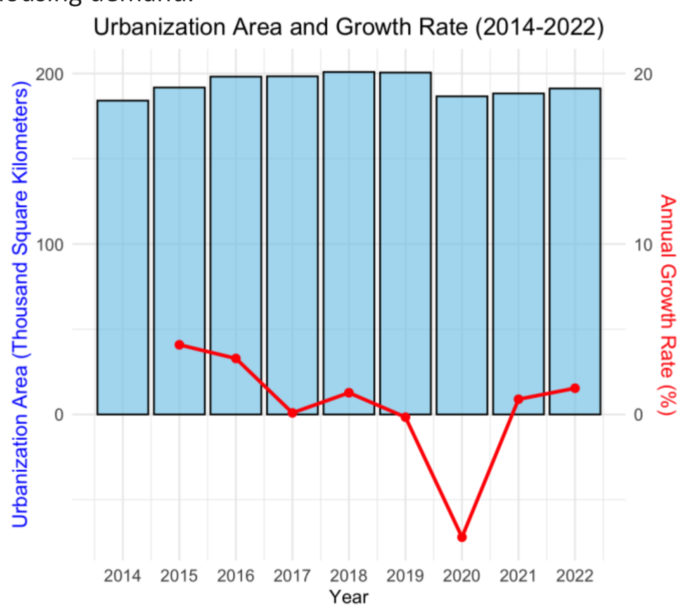

Figure 3 – Urbanization Area and Growth Rate (2014-2022)
Source: [NBS]

Under normal market conditions, supply should contract in response. However, China's pre-sale model prevents this adjustment. Developers sell housing units before construction is completed and rely on these proceeds to finance new projects. This model keeps developers highly leveraged and dependent on continuous growth. As demand weakened, liquidity constraints became severe. Many firms are under the pressure of financial distress.

In 2020, the government introduced the "Three Red Lines" policy to curb excessive debt in the sector. While intended to stabilize the market, the policy accelerated defaults, as many developers were already struggling with liquidity. This resulted in a wave of bankruptcies leaving numerous pre-sold housing projects unfinished. Mortgage holders who were required to continue payments on incomplete homes began to boycott repayments. This negative feedback loop has deepened the downturn with broad economic repercussions.

The Impact on Chinese Households

Since the beginning of the real estate crisis, house prices in China have shown a significant decline. Such asset depreciation leads to problems such as aggravation of homeowners' financial burden and collapse of consumer confidence, as for many Chinese households, real estate constitutes around 70% of their total assets.

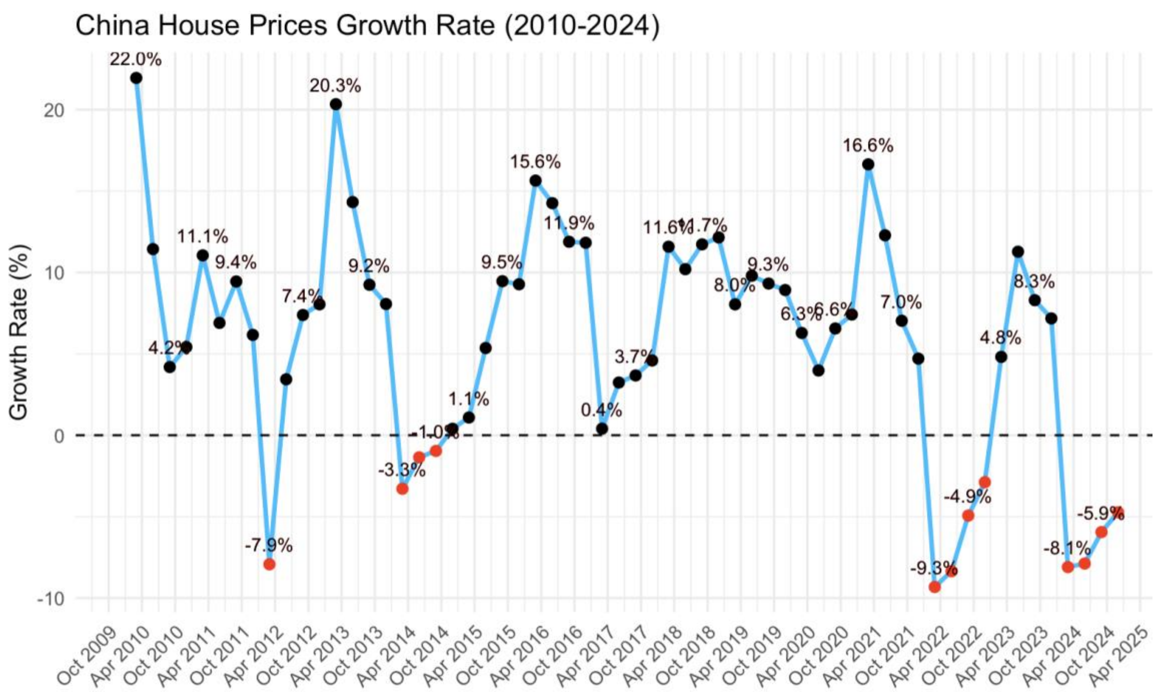

Figure 4 – China House Prices Growth Rate (2010-2024)
Source: CEIC Data

Part of the problem lies with China's pre-selling mortgage system, as buyers purchase units "off-plan" before completion, encouraging developers to overpromise and to take excessive risks. Since 2016, official policies have begun to encourage personal loans and mortgage lending and lower the threshold of minimum down payment for first-time homebuyers. At this point, approximately 60% of household debt in China is attributed to mortgages. As illustrated in the graphs, China's household debt as a percentage of GDP and its household leverage ratio both increased dramatically from 2015 to 2020, reaching around 60%-65%.

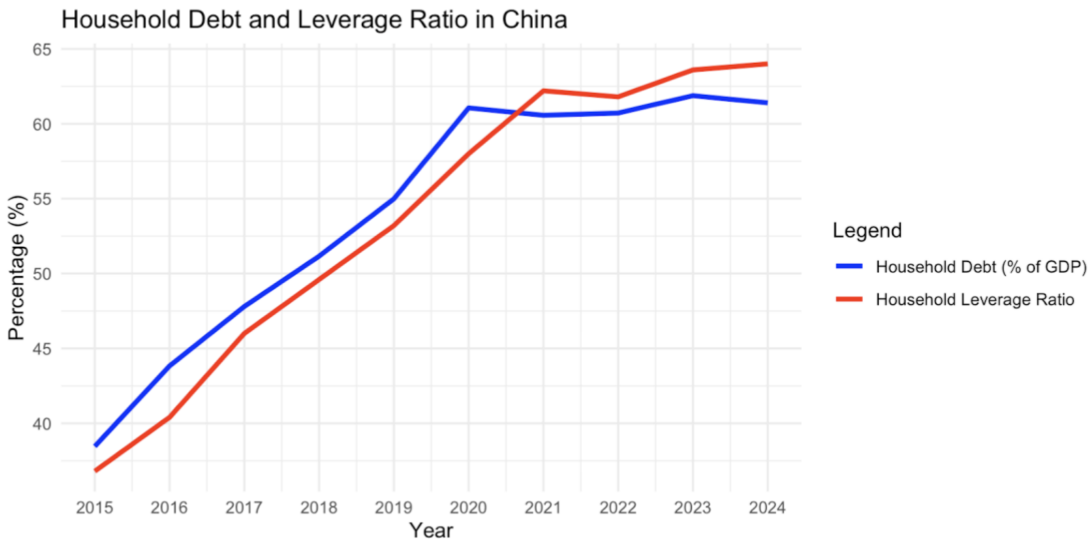

Figure 5 – Household Debt and Leverage Ratio in China
Source: [CEIC Data]

Faced with an economic slowdown, real estate downturn, and an uncertain job market, highly leveraged homeowners may struggle to service their loans, leading to negative equity and defaults. In China, in the absence of a US-style bankruptcy regime, if a household defaults on its mortgage payments, it faces severe financial consequences that result in foreclosures.

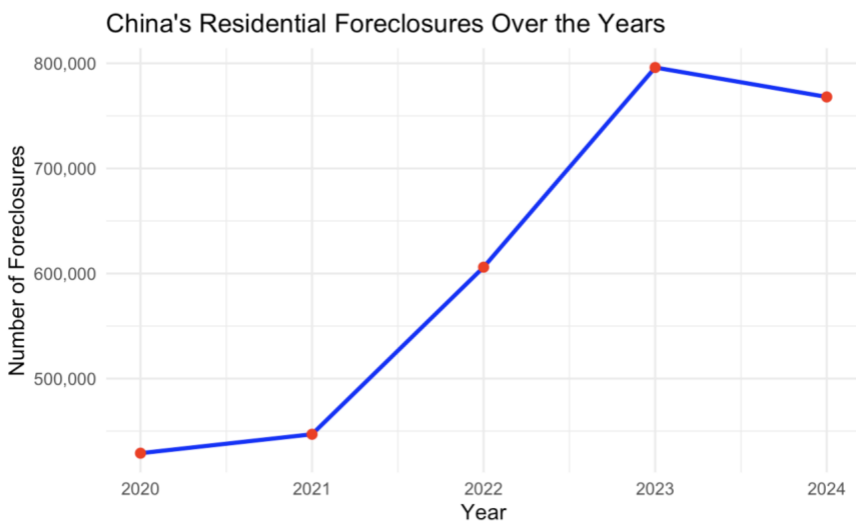

Figure 6 – China's Residential Foreclosures
Source: Reuters; The China Project

The trend of rising defaults is corroborated by the surge in the number of China's residential foreclosures since 2020. In addition to the circumstance of being unable to repay the mortgage, some frustrated Chinese buyers have temporarily halted or boycotted mortgage payments in protest against delayed construction by property developers under the pre-sale model. As a result, money shortages of real estate companies have deteriorated and banks risk accumulating bad loans.

The Impact on Banking Sector

Rapid growth in real estate loans typically signals a booming economy, as property development and home purchases drive economic activity. While this was previously the case in China, real total balance of estate loan growth has slowed significantly since 2016 as shown in figure 7, with a sharp contraction in 2023 when growth fell below zero. The drop in personal housing loans further underscores declining confidence in the real estate sector, exacerbated by lower purchasing power amid a sluggish economy. Additionally, stricter lending policies have curbed real estate borrowing by imposing tighter debt controls on developers. As shown in figure 7, banks have also become more reluctant to lend following high-profile defaults such as Evergrande's financial crisis, further constraining real estate financing.

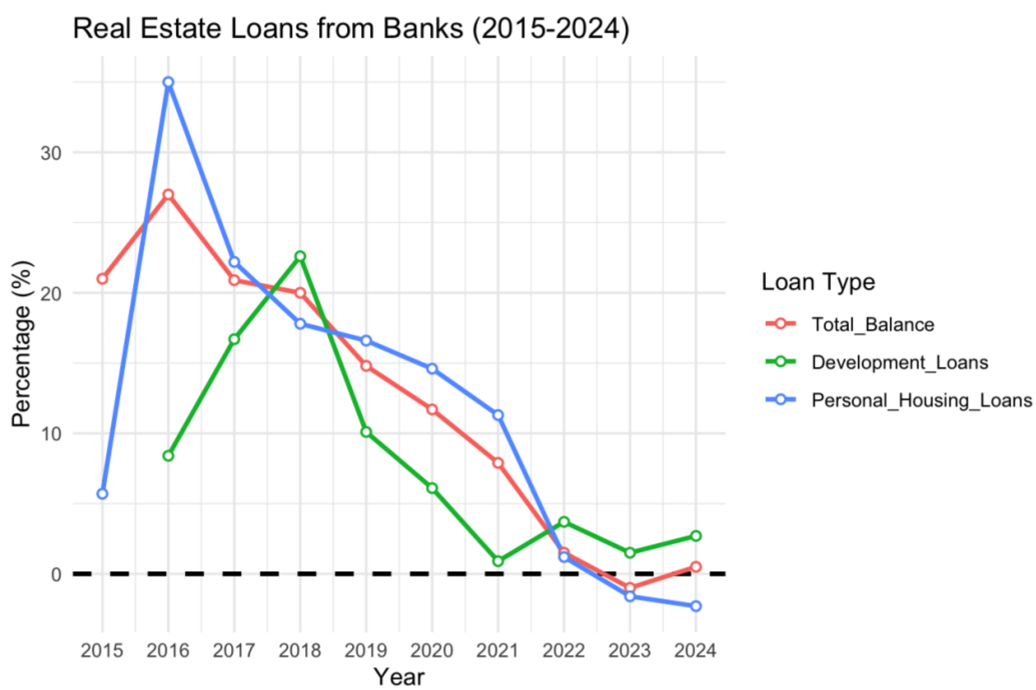

Figure 7 – Real Estate Loans from Banks (2015-2024)
Source: [The People's Bank of China]

Despite high-profile developer defaults, China's **Non-performing Loan** (NPL) ratio has remained below 2% from 2015 to 2024, which suggests good credit quality and low default risk. The **Provision Coverage Ratio (PCR)** reflects the funds a bank allocates to cover potential losses from unhealthy debts. In this case, a high PCR indicates that the Chinese financial system is well-prepared to absorb any potential bad debts that incurs. One explanation of these values is that real estate development loans account for less than a quarter of total real estate loans, while personal housing loans make up nearly three-quarters, spreading the risk. Additionally, in September 2023, the National Administration of Financial Regulation (NAFR) allowed banks to cut rates on existing mortgages, easing pressure on borrowers and keeping NPLs low. However, loans to Local Government Financing Vehicles (LGFVs) and private developers are being restructured with government support, delaying their recognition as NPLs. However, if these restructured loans fail to be repaid, the impact could be significant in the future.

	2022	2023	2024
Non-performing Loan Ratio (%)*	1.63	1.59	1.56
Provision Coverage Ratio (%)	205.85	205.14	209.48

Source: National Financial Regulatory Administration (NFRA)

The **Loan Loss Reserve Ratio (LLR)**, which measures how much banks set aside for potential defaults, has remained above 3% from 2015 to 2024 and has been increasing. This suggests a more cautious banking approach, likely in anticipation of rising defaults. It may also signal growing credit risk, with more borrowers struggling to repay loans. The **Net Interest Margin (NIM)** measures a bank’s profitability from lending activities, calculated as the difference between interest earned on loans and interest paid on deposits. As shown in figure 9, NIM has been declining, signaling weaker profitability and lower loan demand due to economic uncertainty and reduced household borrowing. Given the Chinese banking system’s relatively low NPL rate and high PCR, a financial crisis is unlikely, however, concerns remain regarding a more cautious banking approach, individuals' ability to repay housing loans, and the overall profitability of Chinese banks.

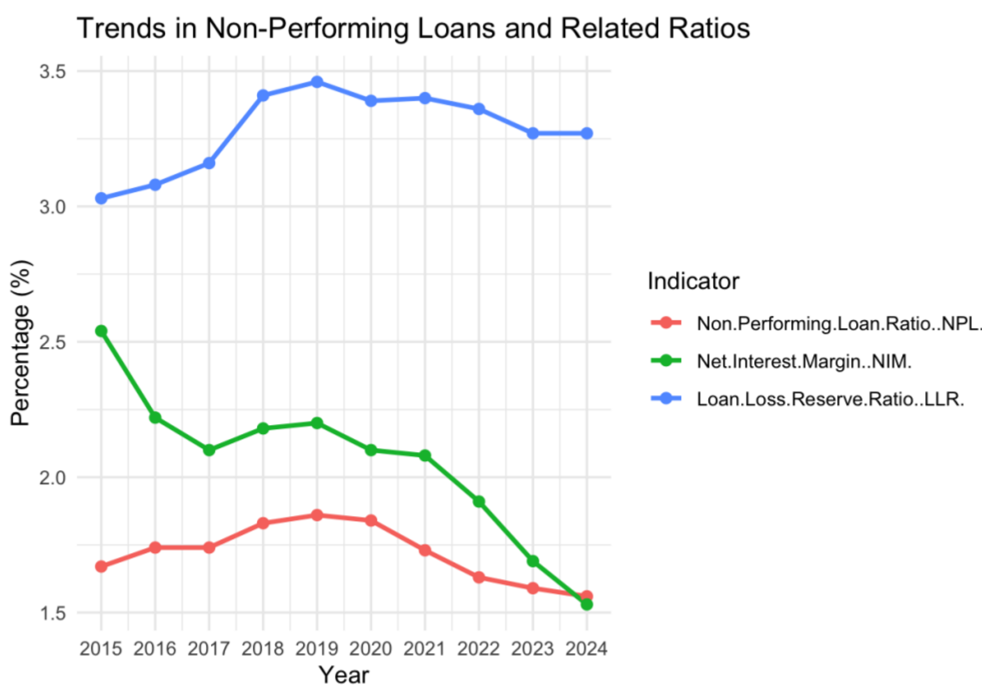

Figure 9 – Real Estate Loans from Banks (2015-2024)
Source: The People’s Bank of China

The Impact on Local Governments

A significant part of the funding for the local governments in China comes from land transfer revenues, meaning the sale of state-owned land-use rights to developers. However, the real estate downturn led to a substantial decline in these revenues, subsequently affecting the local government budget. Official data shows a persistent drop in land sales income since 2021 and decreases in land transfer revenues since. This decline has prompted many regions to revise their budgets and reconsider infrastructure investments. Dependence on land-related income is a structural issue, but as property developers face difficulties and land sales slow, local governments rely more on debt financing. If this trend continues, it could further strain local governments' ability to service existing debt, necessitating stronger central government intervention to maintain financial stability. Unsurprisingly, China's local government debt has grown significantly, the debt balance rose from 2.76 trillion USD in 2018 to 6.11 trillion USD in 2023. This trend suggests growing fiscal pressure on local governments, reinforcing concerns about debt sustainability.

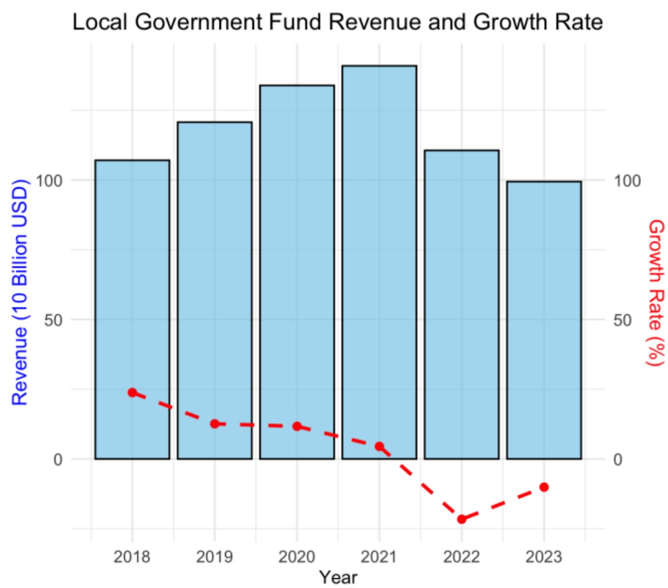

Figure 10 – Local Government Fund Revenue and Growth Rate
Source: [Ministry of Finance of the People's Republic of China]

A Tale of Two Crises: Comparing the 2007 U.S. Real Estate Bubble Burst and China's Current Real Estate Crisis

Differences in Financial Structure and Decision-Making Process

The 2007–08 U.S. financial crisis was triggered by excessively loose credit policies, which led to a surge in subprime mortgage lending to high-risk borrowers. These high-risk mortgages were bundled into complex financial instruments , which were heavily leveraged and traded by financial institutions. As housing prices declined and mortgage default rates soared, the value of these securities plummeted, leading to widespread financial losses, the bankruptcy of large financial firms, and a collapse in global financial markets.

While financial risks exist in China's real estate market, they are relatively simpler compared to the U.S. subprime mortgage crisis: China's real estate sector primarily relies on direct bank lending rather than complex financial instruments in the U.S. which led to the cascading financial sector collapse. Overall we therefore expect the real estate crisis to have a depressing effect on economic activity, but not to pose a fundamental challenge to the stability of the Chinese financial system.

Differences in Mortgage Structures and Risk Bearers

A key distinction between the U.S. and Chinese real estate markets lies in the fundamental nature of mortgage loans. In China, mortgages are recourse loans, meaning that if property values decline and a homeowner defaults, banks can recover losses by auctioning off the property. If the auction proceeds are insufficient to cover the remaining loan balance, the borrower is still personally liable for the outstanding debt. In addition, mortgage default results in a negative record on an individual's credit report and may lead to their inclusion on the "List of Dishonest Persons subject to Enforcement." In contrast, U.S. mortgages in some states are non-recourse loans, which means that in the event of default, the bank can only seize the property but cannot pursue the borrower for any remaining debt if the borrowers declare bankruptcy. This structural difference significantly affects risk distribution. In China, homebuyers bear a greater financial burden during market downturns, whereas in the U.S., banks absorb more risk from repayment defaults, concentrating the impact within the financial system rather than on homeowners.

Impact on the Domestic and International Economy

The U.S. real estate crisis led to widespread economic recession, including significant job losses and structural adjustments across various industries. Sectors directly linked to housing experienced severe declines, while other industries, such as technology,å saw employment growth as the economy restructured. The crisis had a broad and lasting impact on the national and global economy, contributing to a deep recession. In contrast, China's real estate crisis has had a more concentrated impact limited to the housing sector. Unlike the 2008 U.S. crisis, which triggered a deep recession, China's housing crisis has resulted in a gradual economic slowdown rather than an outright collapse.

Policies Are Not Enough

In response to the crisis, the Chinese government has introduced policy tools such as urban village redevelopment, government purchases of unsold properties, and monetary easing to address the housing crisis. However, these policies are unlikely to provide long-term efficacy of three recent policy measures, as they do not address the deeper structural problems of the crisis.

Urban village redevelopment involves upgrading underutilized or dilapidated residential areas to provide new housing while modernizing infrastructure and public services. This initiative will be extended to 300 cities, potentially generating millions of jobs and bolstering construction and infrastructure sectors. Despite these promises, this approach struggles against slowing population growth, an aging demographic, and limited demand beyond select urban centers. Moreover, the high cost of large-scale reconstruction can burden local governments already contending with significant debt, raising concerns about the sustainability of these initiatives.

Besides, in an effort to reduce excess inventory and stabilize prices, local governments are encouraged to purchase unsold housing units from developers burdened by sluggish sales and liquidity constraints. These properties are then repurposed for affordable housing or other social programs. However, many municipalities are already grappling with high debt levels, making large-scale acquisitions fiscally risky. Meanwhile, by artificially supporting housing prices, these measures may interfere with natural market adjustments, prolonging structural imbalances in supply and demand. Over time, the financial costs of maintaining and managing these housing stocks could outweigh any short-term gains, especially if fundamental demand remains weak.

Mortgage interest rate cuts and lengthening repayment periods aim to stimulate property purchases by increasing affordability. Although these measures can temporarily boost market sentiment, their efficacy hinges on robust consumer confidence and stable income growth—both of which are currently in doubt. Moreover, banks extending longer mortgage terms risk accumulating higher credit exposure if the broader market continues its downward trajectory. In this environment, merely easing financing conditions cannot offset the deeper issues of demographic stagnation, slowing urbanization, and local government fiscal constraints.

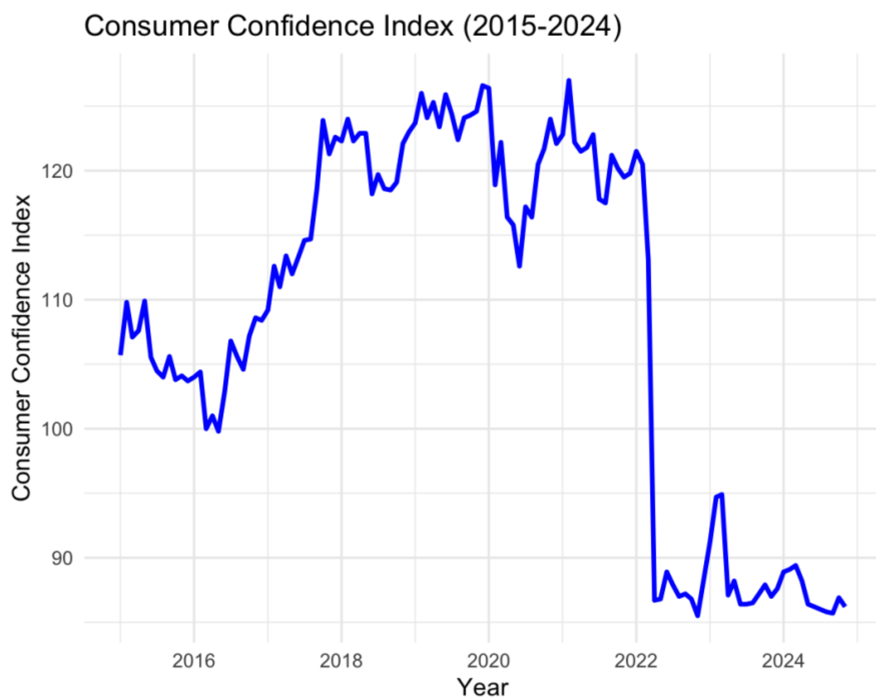

Figure 11 – Consumer Confidence Index (2015-1014)
Source: [CEIC Data]

Conclusion: Unresolved Structural Problems

China’s real estate crisis is not just a cyclical downturn but reflects structural issues in the country’s economic and fiscal framework. The Chinese local governments’ fiscal dependence on land sales, coupled with excessive leverage in property development and an overbuilt housing market, creates a feedback loop that is highly resistant to policy interventions. The oversupply is not easily corrected because it is built into the local governments’ revenue models and the real estate companies’ revenue strategies. In addition, the weak demand in the real estate market is a significant microcosm of China’s overall insufficient domestic demand. If housing demand is to be simulated, more concrete measures will be needed to restore consumer confidence. Structurally, China is also facing demographic challenges, naturally leading to declining demand. Without structural reforms that reestablish consumer confidence, address demographic shifts, and rebalance local government financing, current policy efforts will be insufficient to resolve the crisis.