



Beyond Headlines



EDITION 4

CHINA'S GIANT HOUSING BUBBLE

FINANCE AND INVESTMENT CELL
SHRI RAM COLLEGE OF COMMERCE



THE FAILING MARKET

Excess urbanization, high debts, unfavorable demographics & Covid-19 led to slowing demand & oversupply.

3 RED LINES

Harsh debt control policy adopted in August 2020 put highly leveraged developers in distress, triggering a crisis.

THE FAULTY MODEL

Credit-fueled growth model post 1998 with high leverage, speculation & pre-sales created a house pricing bubble.

CHINA'S REAL ESTATE CRISIS

THE BUBBLE BURST

Home sales, property prices, real estate investment - all crashed. \$18 Trillion of household wealth wiped out, widespread mortgage defaults and unfinished projects

DEVELOPERS' DOWNFALL

Major developers faced heavy losses and falling stock prices. Many went bankrupt after drowning in debt, leaving behind unfinished projects

THE SYSTEM COLLAPSE

Banks and Financial sector suffered from rising NPLs. Local government revenues declined and debts rose. Consumer confidence plummeted

HOW DID IT HAPPEN?



Developers took huge loans and sold properties before their completion



The pre-sale model failed due to declining demand, depleting developers' liquidity



Three Red Lines policy put severe financial burden on developers with huge debts, causing defaults

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EXECUTIVE SUMMARY

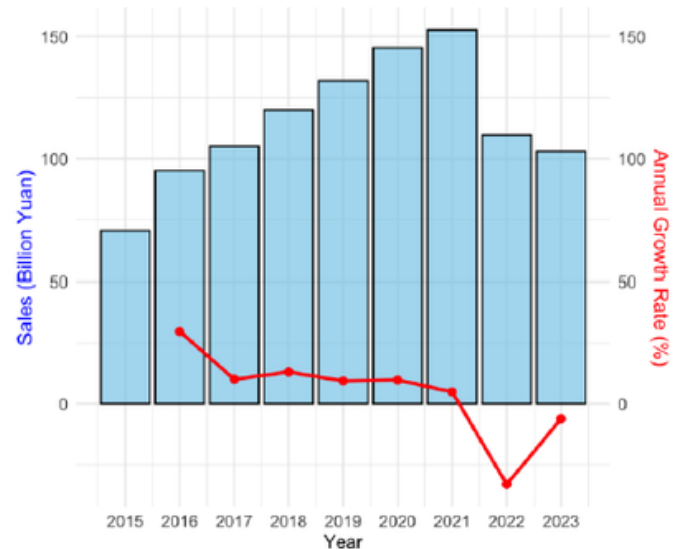
China's real estate sector, which played a major role in driving its economic expansion for decades, has been in crisis since 2020. The contemporary housing crisis is a result of a multitude of structural issues with the sector like the speculative pre-sale model, inefficiency of Local Government financing, excessive debt within the sector and China's demographic trends. It was triggered by the Three Red Lines policy of 2020, and was amplified due to the ongoing COVID-19 pandemic. The country has since seen a fall in property demand, plummeting housing prices, financially distressed developers and widespread defaults by homeowners and firms, affecting both the domestic and global economy.

INTRODUCTION

Over the last few decades, China has become an economic Superpower - the main driver of global growth as the world's 2nd largest economy, with the real estate sector being an indispensable pillar of this success story. This can be quantified from the fact that Real Estate has historically accounted for over 30% of the country's GDP, compared to other developed nations where it contributes 15-20%. With Chinese homeownership exceeding 80% of households and roughly 70% household wealth concentrated in real estate assets, it is evident that any damage to this sector is highly detrimental to the country's economy. Post 2020, the real estate market in China has experienced a significant crisis- plummeting property sales and house

prices, developers going bankrupt and growth slowing down. A troubled housing market not only impacts buyers and developers, but also creates systemic risks for the world economy at large.

Figure 1 shows Sales of Residential Commercial Housing and Growth Rates



This report focuses on analyzing the causes and impacts of China's Real Estate Industry Crisis.

TIMELINE

Phase 1: The Trigger - Three Red Lines Policy (2020)

August 2020: The Chinese government enacted the "Three Red Lines" policy, establishing guidelines for property companies taking on extra debt.

The new policy effectively prevented developers from over-borrowing from banks, which instantly resulted in a severe cash crunch for the industry.

Phase 2: Zero-Covid and Demand Destruction (2020 - 2022)

Effect of Lockdowns: The government's

zero-Covid policy caused property values to drop, leading to diminished demand and a general loss of confidence in the real estate market. Lockdowns also kept prospective buyers from inspecting homes, which affected consumer spending.

Phase 3: The Fiscal Blow and Systemic Strain (Early 2022 - Early 2023)

This phase highlights the impact of the crisis moving beyond developers to local governments and the construction supply chain, confirming the end of the old growth model.

Decline of Land Finance: Land transfer revenue had historically accounted for 91% of local governments' total income. Land revenues considerably dropped.

Supply Chain Contraction: Transfers from developers to engineering and construction firms significantly decreased.

Phase 4: Major Collapse and Aggravation (2023)

Economists downgraded forecasts for Chinese economic growth in 2023 to just 5%. Major developers were in financial distress with heavy losses and high debts.

Country Garden's sales fell by 60% in July 2023, and it reported a massive loss of \$7.6 billion in the first six months of the year. Later in August 2023, China Evergrande formally filed for U.S. bankruptcy.

Phase 5: The Inflection Point and Stabilization Efforts (2024 - Present)

The government pumped liquidity into the economy to reverse the downturn, and is anticipated to provide substantial additional financial assistance, potentially injecting up to \$1 trillion.

Stabilization Goals: it is expected to provide resources necessary to reduce saleable

inventory, clear the construction backlog, and restructure debt.

BACKGROUND

Before its housing market reforms, China had followed a state-controlled welfare housing system.

After this system was abolished in 1998 and a market-oriented model was adopted, the real estate sector saw rapid growth spanning decades. China's Real Estate Development Model has 2 such defining characteristics that acted as structural causes behind today's crisis:

Role of Local Governments: The primary source of revenue for Local Governments was land sales. Local Government Financing Vehicles (LGFVs) borrowed heavily against future land revenues to fund infrastructure projects.

Since local governments needed higher land prices to fund more debt, this created an incentive for a pricing bubble to form.

Pre-Sale Model: Major private developers adopted a high-risk model, relying heavily on financial leverage to expand.

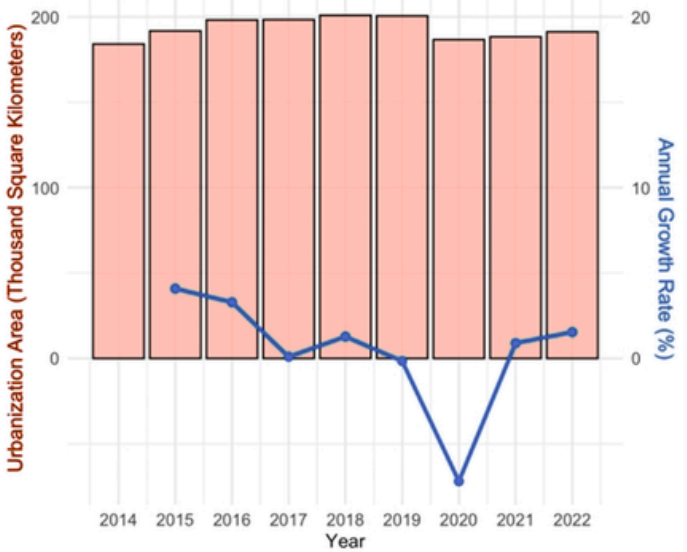
Homes would be sold before construction was completed, allowing them to use homeowners' upfront payments to finance further waves of land purchases and construction. It is based on the presumption that demand would always be on the rise and new customers would keep buying in. As a result, the market was fueled by heavy borrowing and speculation.

CAUSES

Having understood the structural reasons, the specific causes behind the crisis were:

Urbanization: Rapid expansion over the last few decades led to an exhaustion of developable land. This caused the urbanization rate to stagnate and demand for housing to decline. In regular market conditions, supply would have reacted by contracting. However, because of the pre-sale model, developers who were highly dependent on growing demand and regular sales faced financial distress.

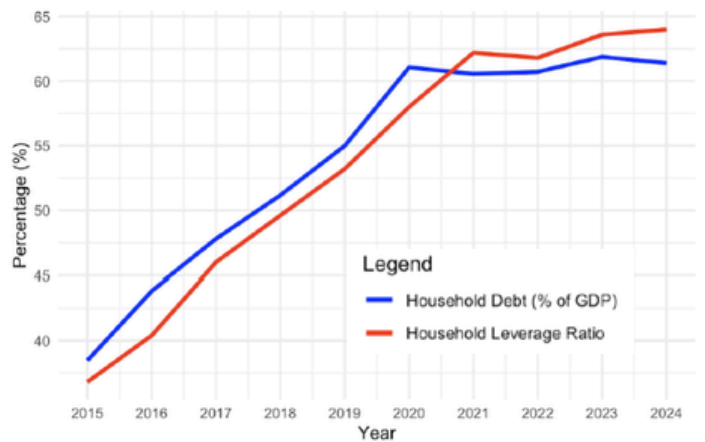
Figure 2 shows the Urbanization Area and Growth Rate from 2014-2022.



Demography: China's real estate boom was fueled by growing incomes and favourable demographics. However, with an aging population and low birth rates, demand for housing started declining and the speculative assumption of ever-growing demand was broken. This created a situation of excess supply, with vacancy rates as high as 15-20%.

Excessive Debt: The rapid credit-fueled growth model led to a surge in household and corporate debt. The average debt-to-asset ratio for real estate developers exceeded 80% by 2020. In 2021, RMB 52 Trillion of loans were directed to real estate - an 18x increase from 2005. Huge borrowings coupled with a pricing bubble meant a debt crisis was imminent.

Figure 3 shows Household Debt and Leverage Ratio in China.



Capital Misallocation: The Land Finance model led to excess construction in hundreds of tier 3, 4 and 5 cities. These cities face slower growth and population exodus, creating a lack of demand.

COVID-19: The lockdowns and zero-COVID policy caused workers to be laid off and consumer spending to decline. With buyers in need of liquidity, demand for housing plummeted.

THE TRIGGER: THREE RED LINES POLICY

The "Three Red Lines" policy, introduced in August 2020 by the People's Bank of China, was explicitly designed to curb excessive borrowing and reduce systemic risk. It targeted highly leveraged developers by imposing 3 strict criteria to control credit:

- Liabilities to asset ratio must be less than 70%

- Net gearing ratio must be less than 100%
- Cash to short-term debt ratio must be at least 1

Developers, who had for long relied on continuous high credit supply, were now required to adhere to strict debt reduction targets. This resulted in large scale defaults by developers who were already struggling with liquidity due to deficient demand and declining sales. This resulted in a wave of bankruptcies, unfinished projects and mortgage defaults from protesting buyers.

EVERGRANDE - A CASE STUDY

Evergrande Group, founded in 1996, has over 1,300 projects in more than 280 cities in China. Entering the market during the boom period, it quickly grew into China's second largest property developer. Its use of heavy borrowing to finance land acquisitions and development projects led to it becoming the world's most indebted developer with nearly \$330 Billion in liabilities. Its problems started after the introduction of the Three Red Lines policy in 2020. Facing a cash crunch due to the ongoing liquidity crisis, its shares started plummeting in 2021. It defaulted on an offshore bond payment in December 2021. After facing continued financial distress, it filed for bankruptcy in the US in 2023. In January 2024, a Hong Kong court ordered its liquidation due to its failure to present a viable debt restructuring plan. In August 2025, it got delisted from the Hong Kong stock exchange.

Figure 4 depicts Evergrande's Stock and Bond prices.

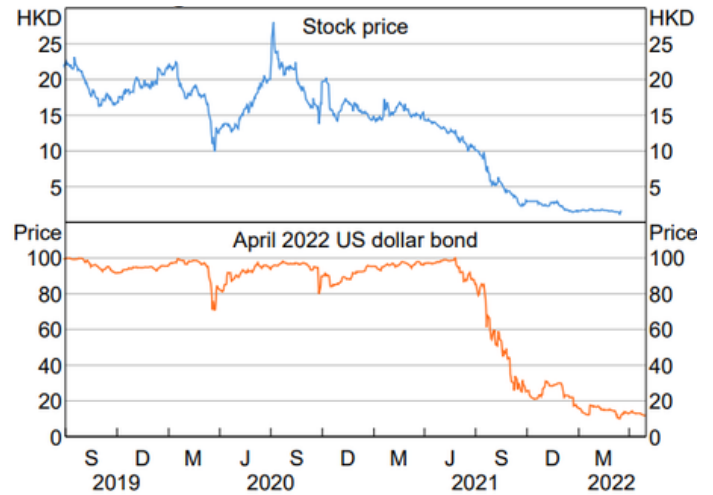
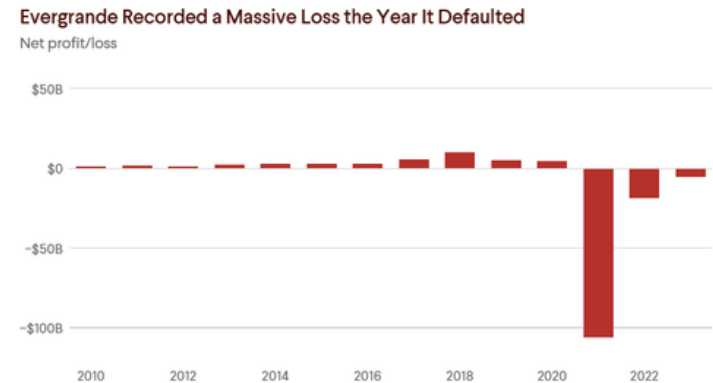


Figure 5 depicts Evergrande's Net Profits/Losses from 2010-2023.



IMPACTS

Impact on Chinese Households

The bursting of the pricing bubble resulted in property values tanking. Since real estate constitutes over 70% of households' total assets, this decline in prices wiped out an estimated \$18 Trillion in household wealth. With roughly 60% of household debt being held in mortgages, those who held mortgages on unfinished projects also suffered from developers shutting down operations.

The Real Estate Market Meltdown

The Chinese property market that once

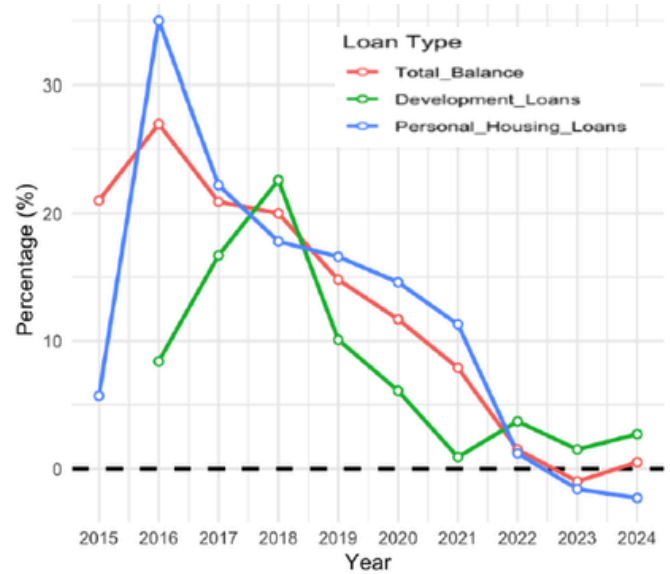
surged is rapidly shrinking. Major developers (such as Evergrande, Sunac, Country Garden etc.) and small firms suffered losses, financial distress and bankruptcies. More than 50 developers have defaulted on debt payments and bond holders have lost over 90% on offshore bonds issued by China's largest developers. Real estate investment fell by 10.6% year on year in 2024, and an additional 11.2% in the first half of 2025. Housing starts fell more than 60% relative to pre-pandemic levels. Residential sales decreased 15-20% in both value and volume. Figure 6 graphs year-on-year changes in Real Estate Investment, Home starts and Sales in China (2012-2023).



Impact on banks

Chinese banks have a large concentration of real estate as most real estate development has relied on credit and leverage for many years. The housing crisis has led to an increase in the non-performing loans (NPLs) in Chinese banks, which have been a drag on bank balance sheets. The risk of non repayment resulted in a steep decline in loans to developers and homebuyers. Total aggregate real estate exposure decreased from 32.3% of total loans in 2020 to 25.9% in 2023.

Figure 7 shows the amount of Real Estate Loans given by Chinese Banks (2015-2024).



Consumer Confidence and Spending

As property values declined and the risk of unfinished projects increased, many potential homebuyers became hesitant to invest in real estate which is reflected in the sharp drop in property sales and the increase in defaults on mortgages. The cautiousness of the consumers is further compounded by broader economic uncertainties like rising unemployment and stagnant wage growth.

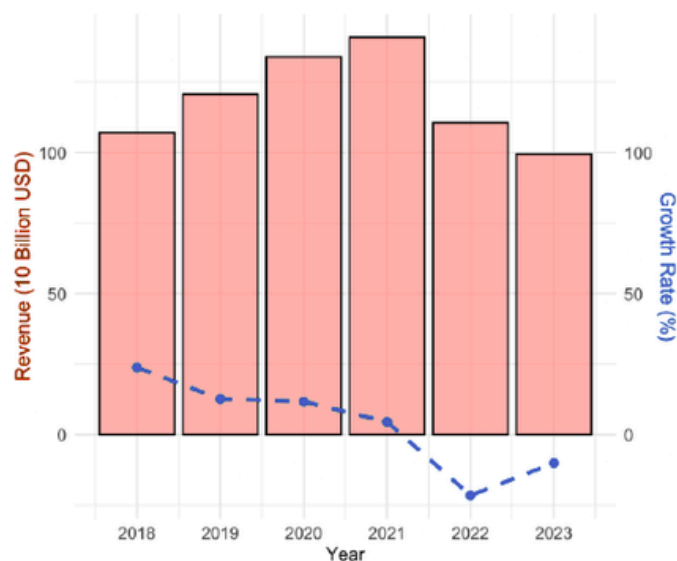
Figure 8 is China's Real Estate Consumer Confidence Index from 2015-2024.



The Impact on Local Governments

The drop in share of land sales in Local Government own revenue from 38% in 2019 to 27% in 2023 compelled many local governments to adjust their budgets, thus analyzing and assessing infrastructure investments. Local government debt in China has continued to increase to significant levels, the debt balance grew from USD 2.76 trillion in 2018 to USD 6.11 trillion in 2023. The trend towards debt financing that occurred in China shows the high level of fiscal pressure local governments were operating under, which again suggests concerns about debt sustainability.

Figure 9 depicts Chinese Local Government Fund Revenue and Growth Rate.



Global Financial Implications

Financial markets are particularly sensitive to developments in China due to the size of its economy and the scale of its banking sector. Chinese banks are among the largest in the world by assets, and a crisis within this sector can trigger global financial instability. Moreover, the banking and real estate crises could result in increased risk aversion among global investors, leading to capital outflows from emerging markets and tightening of global financial conditions. This

shift in investor sentiment can potentially slow down global economic recovery.

CONCLUSION

China's banking and real estate sectors are currently dealing with crises due to significant amounts of debt taken on by the country's property developers, leading to developments like the failure of Evergrande. Regulatory crackdowns were warranted but have increased nonperforming loans and strained liquidity. The fall off in property sales has halted construction on projects and reduced consumer confidence, leading to economic slowdown. The crises at home also present potential challenges to global markets and trade.

Looking ahead, the future of China's banking and real estate sectors will largely depend on the effectiveness of the steps taken by the Chinese government such as financial interventions and regulatory adjustments, to stabilize the situation. The shift towards a more consumption driven economy will be crucial for sustainable growth.

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APPENDIX

- ◆ [Boom to Bust: The Implications of China's Real-Estate Crisis](#)
- ◆ [The Transition of China's Economic Model from Real Estate to Consumption and Manufacturing - CKGSB Knowledge](#)
- ◆ [China's property slump could extend into 2027 with further price drops: Goldman Sachs | South China Morning Post](#)
- ◆ [Has China's property market reached the bottom? | Goldman Sachs](#)
- ◆ [The History of China's Real Estate Market and The Risks It Faces](#)
- ◆ [China's Economic Slowdown: The Property Crisis as a Drag on Growth](#)