THE CHINESE GOVERNMENT'S NEW HOUSING MARKET INITIATIVES

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Executive Summary

1. China's Central Bank and Banking Regulatory Commission announced the easing of credit rules on 30 September 2014, thereby relaxing credit restrictions (限贷) on the housing market initiated by the previous Hu-Wen leadership in 2011.

2. The easing of credit rules is to stimulate the currently depressed housing market, ease the fiscal status of local governments, liquidise the banks' mortgage assets, broaden capital sources for the real estate sector and ultimately reinvigorate economic growth.

3. However, neither the easing of credit rules nor the removal of purchase restrictions in the summer of 2014 was it able to reverse the housing downturn. The capital shortage in the banking system and the real estate sector, the real estate registration system, the expected property tax levy, the anti-corruption campaign, and the housing glut, have greatly restrained housing market recovery.

4. The easing of credit rules and the removal of purchase restrictions show a divergence from the previous leadership's administrative measures and monetary expanding to market-oriented measures for sustainable housing development.

5. While the down payment ratio and interest rate for mortgages have been trimmed and attracting strong attention, the essential change is the introduction of Mortgage-Backed Security (MBS, 住房抵押贷款支持证券). It is expected to broaden capital sources for the real estate sector and significantly change the banks' balance sheets.

6. The operation of MBS will face huge challenges in China's relatively under-developed financial market as the relevant institutions for a secondary mortgage market have yet to be established.

7. The MBS could increase the level of risks to the banking sector if the deals are not carefully scrutinised. The leadership is expected to deal with this risky MBS

business with extra caution and keep its development at a manageable and gradual pace. Consequently, MBS development in China is thus likely to be slow in the near future.