Beijing's Remedy For The Great Property Crisis Is Doomed To Fail.

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Unfinished apartment complex in Shanghai, China.. (Photo by In Pictures Ltd./Corbis via Getty ... [+] CORBIS VIA GETTY IMAGES

Beijing has taken its boldest step yet to address China's stubborn property crisis and clean up the financial fallout from it. The new policies aim to lift the burden on China's financial system and economy imposed by a massive 3.2 trillion yuan ($446 billion) funding gap among the nation's property developers. Compared to

the tentative nature of Beijing's behavior previously, the latest effort looks forceful, but it will short of the need.

According to reliable press reports coming out of China, this latest initiative has three basic elements. Beijing is urging the nation's banks to boost their financing for property developers. Since most banks are state-owned, they will doubtless respond. This is something of a complete reversal from Beijing's efforts in 2020-21 to starve property developers of financing, which itself was a radical reversal from Beijing's former and long-held policy of promoting property development with easy financing terms. That sudden reversal three years ago was, more than anything else, responsible for the crisis in the first place. Now China's leadership has come full circle. (So much for the wisdom and stability of a government directed economy.)

A second part of Beijing's effort is to permit banks to advance un-secured, short-term loans to developers. Until this latest policy initiative, development financing has always been secured by the property in question. Beijing hopes that the availability of un-secured loans will enable troubled developers to repay the older loans that stand at the center of the crisis for which they lack the resources to discharge.

The third element in the new program will secure for the nation's leadership a hand in choosing which developers will get this help. The government will provide lenders a so-called "white list" of 50 eligible developers. Here the inevitable political connections will enter the policy equation. The complete list is not yet available, but it seems that the giant developer Country Garden is on it as is the state-backed China Vanke.

The most constructive part of the new policy initiative is how this new flow of credit will enable developers to complete an estimated

20 million apartments for which homebuyers had pre-paid before the crisis broke. If buyers can take possession of these units, China will have relieved itself of considerable social unrest. Completing these units should also relieve a fair amount of strain on China's banks and its financial system generally. These buyers had taken out mortgages in order to pre-pay on the apartments but to date have understandably refused to make payments until the apartments materialize. Presumably, once these people take possession, they will begin to pay on these mortgages, lifting from the banks what today looks like a large tranche of bad loans.

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Besides this welcome effect, Beijing's actions will only kick the can of financial troubles down the road. The developer receiving the new flow of credit may complete the units for which it contracted, but otherwise it has little prospect of a new business cash flow. The units were pre-paid and so that money has long-since changed hands. And the Chinese economy today offers little prospect of further development that will offer these firms sufficient revenues to pay off their debts, old and under Beijing's new program. China's banks will as a consequence continue to face the prospects of huge losses on these credits. The new financial flows are little more, it seems, than a variation on the old and cynical banking saw: "extend and pretend" in which lenders, facing a failure on a loan, will extend its maturity in the vain hope that somehow at a future date the failing borrower will secure the resources to make good on the loan.

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Beijing must address this still existing financing gap in ways that go beyond the proposal's offer of new loans to cover old ones. Without more substantive action, the financial crisis will resume at that future date when developers announce that they still cannot pay what they owe. Because Chinese bankers can see that they still face an overhang of bad debt, circumstance will continue limit Chinese finance's ability to support other presumably more promising projects, such as Beijing's latest decision to increase infrastructure spending.

Beijing deserves credit for taking bolder steps than previously to address this festering and burdensome crisis. Praiseworthy as the latest action may be in this respect, it nonetheless will fail to meet China's needs. Neither Chinese finance nor the Chinese economy are out of the woods on this critical matter. Nor, as a consequence, is China's leadership. A resolution will require more and bolder action out of Beijing. Sadly for China, it is not apparent that leadership is up to the challenge.

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