Dean&Francis

ISSN 2959-6130

Comparison of Risks for Real Estate Finance in Asian: Evidence from China, Japan and Korea

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Abstract:

As a matter of fact, China is currently facing a high leverage rate for residents facing housing loans, and a large number of bad real estate events have occurred in various regions recently. Local residents are dissatisfied with real estate developers due to these events, and researchers are exploring how to control the market and promote the healthy development of the real estate market. By exploring the practices of different countries in the real estate financial crisis and conducting comparative research, it is beneficial to control the risks of real estate finance. The country should strengthen its control over the market, require enterprises to increase transparency of information, strengthen connections with the international market, and other different means to promote China's development. This study helps to refer to how to face real estate financial risk crises, refer to various practices of different countries to solve the real estate financial crises they face, and provide several methods to prevent real estate financial risks.

Keywords: Risk in real estate; real estate finance; Asian economy.

1. Introduction

As a matter of fact, human beings have continuously promoted the goal of common prosperity and taken effective measures to improve people's livelihoods, providing Chinese inspiration for the international community to achieve poverty alleviation goals. At the same time, affected by the COVID-19, the Russia-Ukraine conflict and other factors, China's economic growth slowed down, and financial risks also increased. Residents are demanders of the real estate financial market and carriers of investment and financing risks. The degree of real estate financial risk in the residential sector of a region not only affects the risk of the financial system, but also directly affects regional stability and consumption markets. Resident consumption has been downgraded, and people's awareness of saving money has become stronger [1]. Wang pointed out that in 2020, data from the People's Bank of China showed that real estate assets accounted for 59.1% of total household assets in China, while in the United States, this proportion was only 30.6%. Real estate not only brings wealth accumulation to residents, but also has an important impact on income distribution. In addition, the real estate industry has close relationships with various industries, demonstrating strong economic correlation and playing an important role in the smooth operation of the national economic system; According to data released by the People's Bank of China, the proportion of RMB real estate loans in China to RMB loans in financial institutions has increased from 21.27% in 2014 to 29.01% in 2019. From 2021 to 2022, the balance of household loans in China has increased from 64.46 trillion yuan to 71.95 trillion yuan. This indicates a high degree of correlation between the real estate market and the financial industry, which may trigger higher risks. Among them, medium - and long-term consumer loans, mainly composed of housing loans, are the main component of China's household debt. In 2021, real estate companies such as Evergrande Real Estate frequently experienced „lightning strikes", which undermined the confidence of homebuyers in the market and also reflected the difficulty of sustained high leverage and high turnover profit models of real estate companies. In 2022, cities such as Zhengzhou in Henan Province and Jingdezhen in Jiangxi Province experienced outbreaks of „abandoned buildings" and „suspension of loans", which to some extent also triggered regional financial risks. In March 2021, Guo Shuqing, Chairman of the China Banking and Insurance Regulatory Commission, pointed out that „the core problem in China's real estate sector is still the strong tendency of financialization and foam". With the adjustment of housing prices and the continuous prevention and control of the COVID-19, „this momentum has been reversed". Based on the above background, how to promote the stable development of the real estate financial market, let the real estate return to the residential property, and how to reduce the real estate financial risk on the quality of life of residents has become the focus of attention of the current academic and industry. Therefore, one should pay more attention to the impact of real estate financial risks on the quality of life of residents

Li pointed out that a sudden real estate financial crisis swept across Asia at the end of the last century, involving most Asian countries including Southeast Asian countries, Hong Kong, Taiwan, South Korea, and Japan [2]. This real estate financial risk has led to a real estate foam financial crisis of different levels and degrees in all countries. In this crisis, countries have made different approaches to financial risks, and all countries have gained some experience, including: strengthening supervision and supervision of real estate finance; expanding daily channels of real estate; resolving non-performing bonds and avoiding risks in a timely manner; the government should conduct controlled protection and enhance risk awareness of financial institutions

In summary, significant progress has been made in the study of the impact of real estate financial risks on the quality of life of residents, which has been validated in practical improvements. However, there are still many livelihood issues that need to be addressed, such as the balance between housing loans and consumption capacity among residents. To reduce the impact of real estate financial risks on quality of life, this article aims to summarize the basic situation of real estate financial risks, analyze how residents bear and avoid the risks of real estate finance at different times through the attitudes of real estate developers, different regulatory behaviors of the country, and consumption behaviors of residents. This includes a comprehensive analysis and evaluation of the above papers. Through sorting out the relevant papers, summarize the research results and shortcomings. It propose future research directions to promote the progress and development of stabilizing real estate financial risks and improving the quality of life of residents

2. Overview of Real Estate Financial Risks

Theoretical analysis of real estate financial risk refers to the possibility that banks may suffer economic losses due to various unforeseeable (i.e., uncertain) factors that may cause a deviation between their actual and expected returns in the financial services activities of raising, financing, and clearing funds for the real estate industry.

The process of real estate finance is complex, and when considering its real estate financial risks, it is not possible to cover all aspects, among which contemporary scholars have different opinions. Liu believes that the social environment, economic environment, and unexpected land conditions, financing risks, real estate status, and timing of real estate development during the business process are important factors for constructing a risk system from these aspects [3]; Sun believes that a risk system should be constructed from four aspects: the development trend of national real estate, the demand of residents for real estate, the coordination between real estate and economic development, and the development of real estate finance [4]; Zhou believes that risk estimation should be carried out on all aspects of the real estate development process, such as land selection, financing process, influencing factors in real estate development, and risks in real estate marketing process, in order to construct a risk system [5]; Wang chooses to construct a real estate financial risk system based on factors such as the potential of real estate, the ratio of total investment in real estate development to GDP, and the ratio of construction area to completed area of buildings [6]. According to the analysis, there is relatively little research on regional real estate financial risks in China. The above-mentioned scholars have universality in selecting real estate financial risk indicators, which is a large-scale selection. However, China‘s real estate market has strong regionalism, with a vast territory and significant differences in the development situation of the real estate market and economic development level among different cities. Therefore, it is best to choose local data for research on real estate financial risks in China according to local conditions

3. Analysis and Comparison

3.1 China

China is facing the same problems as Japan in the past. Although the demand for leveraged residents to purchase houses is still increasing, compared to Japan in the past, China’s real estate industry still has real housing demand as support. As of 2023, the urbanization rate of China’s permanent population is about 66.2%, which is equivalent to Japan’s level in 1963. There is still 10 percentage points of room for improvement from the turning point of Japan’s urbanization process from fast to slow in 1975. Moreover, by 2022, the urbanization rate of China’s registered residence population is still less than 50%, 17.5 percentage points lower than that of China’s permanent population. As long as the reform of the registered residence system continues, the improvement space of the urbanization rate of China’s registered residence population will also be the potential demand of the real estate market. A typical result is shown in Fig. 1. Secondly, the difference lies in leverage. The average leverage for Chinese residents to purchase houses is not high. As mentioned in the 2018 China Financial Stability Report by the central bank, the average down payment ratio for Chinese residents to purchase houses is over 34%. Therefore, even when buying a house at the highest point of housing prices, it still needs to drop by an average of more than one-third to make the property a negative asset. The rapid rise in housing prices began from 2015 to 2016, and many people did not buy houses at their peak. Therefore, even if the decline in housing prices leads to a reduction in wealth effects, the proportion of houses becoming negative assets may not be high. The low leverage for purchasing a house means that the decline in housing prices may not be too rapid.

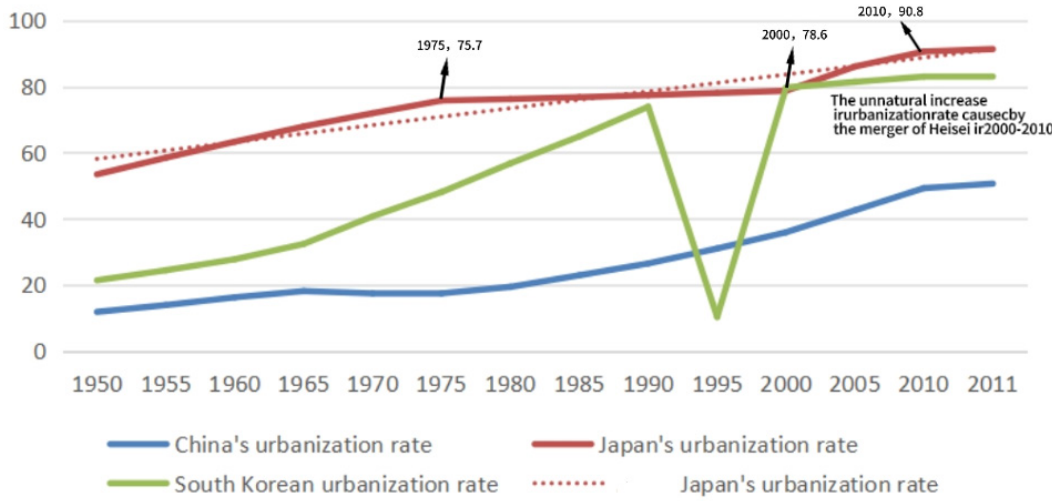

Fig. 1 Urbanization rates in China, Japan and Korea.

3.2 Japan

There are two real estate financial risks in Japan, one in the 1970s and the other in the early 21st century. Before the outbreak of the first crisis, Japan's real estate industry was highly financialized for two reasons: firstly, under the main banking system, the Japanese financial system (especially banks) was deeply bound to physical enterprises, which promoted speculative risks for enterprises and increased the fragility of the financial system. Secondly, the long-term prosperity of real estate has encouraged residents and businesses to engage in leveraged speculation, leading to an increase in residents' willingness to purchase houses. Especially when enterprises invest heavily in land and commercial housing, systemic financial risks arise; Under this speculative upsurge, Japan's housing price foam expanded rapidly, causing crisis in Japan's real estate industry.

After the crisis, Japan issued the Plaza Agreement in 1985. The combination of extremely loose monetary policy, lack of investment opportunities for entities, financial liberalization and other factors gave birth to foam in the stock market, real estate and other fields. On the one hand, the leverage ratio of residents and enterprises has significantly increased. Enterprises and residents borrow heavily to purchase land and property. On the other hand, enterprises, especially small and medium-sized enterprises, make a large number of speculative purchases of real estate. During the six-year period from 1985 to 1991, although housing prices in Japan only increased by 48.9% nationwide, housing prices in Tokyo increased by about 106.3% in just five years. As monetary policy was tightened suddenly from extreme easing, coupled with land financing policy control, the asset foam was directly punctured. In another decade, Japanese real estate prices have fallen by nearly 80%, reaching levels in the 1980s. At this point, economic development has finally resumed; The second real estate financial risk is that Japan's regulatory policies have shifted from tightening to loosening, and legislation has been established to accelerate the disposal of non-performing assets. Japan has established specialized non-performing asset disposal companies and sorting and recovery banks to dispose of non-performing assets. In the first real estate financial risk, due to the possibility of speculation, the willingness of residents to purchase a house increased, and then the government's regulation reduced the willingness of residents to purchase a house to achieve economic stability;

3.3 Korea

The last real estate financial risk in South Korea was around 1997. In 1997, due to the country's external debt problem, it led to a national bankruptcy crisis. After being forced to accept the harsh conditions of the international organization IMF and undergo a bone scraping reform of the financial system, the South Korean economy quickly recovered and repaid the IMF's last loan ahead of schedule in 2001. However, the price of IMF "rescue" is the rise of foreign capital's shareholding in Korean financial, electronics and other important industries, especially in the banking industry, which once reached 66%, greatly weakening the Korean government's ability to control the domestic financial industry, leading to its lack of response to the subsequent real estate foam, and residents' leverage almost out of control.

Among them, the real estate foam problem in South Korea can be largely attributed to the financial control ability of the "weak government" in South Korea after 1997. Since the Asian real estate crisis mentioned by the two countries above, South Korea has started to marketize its housing finance, with housing prices rising by 14% and 26% respectively from 2004 to 2006 and 2020 to 2022. South Korea's implementation of the full rental housing system has boosted housing prices and leveraged residents. In this mode, tenants prepay a deposit of 50% -80% of the market value of the property, without the need to pay any other rent during this period. This is equivalent to the landlord borrowing leverage from tenants. The scale of full rental housing deposits in South Korea is huge, roughly equivalent to the scale of household mortgage loans. If we consider the full rental deposit, the leverage ratio of South Korean residents will reach 156%, ranking first in the world. The real estate risks at this time will affect South Korea for the next two decades. Last year, Bank of Korea Governor Lee Chang Yong stated that the overdue rate of real estate loans in South Korea is increasing. He believes that the government should seek to gradually implement a medium - to long-term plan to deleverage household debt. Typical results are listed in Table 1.

Table 1. Foreign shares for different bank.

	Foreign shares
Kookmin Bank	85.8%
ShinHan Bank	64.0%
Hana Bank	76.6%
Woori Finance oldings	11.7%
korea first bank	100%
Korea Exchange Bank	74.3%
Citibank Korea	100%

4. Implications and Suggestions

According to the analysis, the implications and suggestions are proposed. Firstly, the country should strengthen the supervision of real estate enterprises to avoid financial risks caused by their own reasons. Secondly, direct financing through excessive real estate financing methods should be used to reduce indirect financing through property finance, and the leverage of residents should be lowered within a reasonable range. In addition, reasonable leverage can promote economic development. There is still room for accommodating the leverage of residents in China, which is currently not enough to seriously affect the real estate economy and lead to a real estate financial crisis. It is also necessary to strengthen information disclosure and transparency: during the financial crisis, the problem of information asymmetry becomes more prominent. Governments and financial institutions should strengthen information disclosure, improve market transparency, and enable investors to fully understand market conditions and make wise investment decisions. One also needs to strengthen international cooperation: the financial crisis has had a profound impact on the global economy, and it is necessary to strengthen international cooperation and communication. Governments and financial institutions of various countries should strengthen information sharing, jointly respond to the challenges brought by the financial crisis, and jointly promote the stable development of the global economy

It is suggested that the country should continue to pay attention to the leverage ratio of residents, intervene in the market economy before reaching the critical value, support the market economy, and achieve the goal of promoting national development and protecting market growth through the market [7-10]. One also needs to pay attention to local emergencies and crack down on bad real estate developers to promote healthy competition in the real estate market. Remind real estate developers to promptly handle non-performing bonds to avoid affecting subsequent development. Strengthening the risk awareness of real estate merchants and providing guarantees for the market and their own development. Strengthening international connections, continuously promoting their own internationalization, requiring real estate developers to further disclose their information, facilitating further investment choices for the public, and effectively avoiding large amounts of capital from investing in enterprises and ultimately sinking into the ocean. Therefore, market supervision should be increased.

5. Conclusion

To sum up, this study elaborates and compares the current situation of real estate financial risks in several different countries and past examples of real estate risks. It summarizes that the main factors of real estate financial risks come from the high leverage of residents‘ lives, and points out some methods that are conducive to avoiding real estate risks to a certain extent. However, this study did not provide detailed methods for various regions and found relatively few methods for avoiding real estate financial risks. In the future, more detailed and in-depth exploration can be conducted through this article. The research in this article can help people better avoid real estate financial risks and reduce economic losses caused by adverse factors and operations

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