



ASIA INSIGHT

Real estate slowdown shakes Asia's economic foundations

Weak markets spell trouble for investors, consumers and retailers

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SINGAPORE/HONG KONG/TOKYO -- The economic downturn in China and the darkening global outlook have reversed the momentum in Asia's property markets, giving homebuyers painful whiplash and raising fears of spillover effects on consumer spending.

Eason Shao is one condo buyer caught by the sudden shift. For about six months last year, he repeatedly signed up for "housing lotteries" in the eastern Chinese city of Hangzhou, determined to purchase an apartment where he could start a family. Developers had introduced the lotteries in big cities in late 2017, as the number of buyers had far exceeded the available units during a three-year property frenzy.

Shao, who works for an internet finance company, would get up at 6 a.m. and join long lines of hopefuls outside a local bank. The prospective buyers would transfer tens of thousands of dollars each to the developers just to be included in the draw. For the most popular developments, Shao said, the odds of being chosen were as low as 1%.

The eighth time was the charm for Shao. His number was finally called in October.

Then, only a few months later, the rush died down. Shao heard that people were buying more attractive homes in better locations without going through a lottery at all. "Of course I'm a bit disappointed," he said. "But I made the best decision I could manage back then."

Shao's experience is just a snapshot of the Chinese real estate roller coaster ride, as the trade dispute with the U.S. and the broader economic slowdown hit homebuyers' confidence in the world's No. 2 economy. Since last year, China's largest developers have slashed prices by up to 30% to speed up sales, and analysts and economists expect a further 10% price drop this year.

The cooling market is worrisome for China's policymakers. For years, the sector has played a pivotal role in creating jobs, driving investment and generating cash for local governments. Roughly 25% of the country's gross domestic product comes from property-related industries.



Applicants look at condo models in Hong Kong, where homes are increasingly being sold at a loss. © Getty Images

In Hong Kong, one of the world's most expensive housing markets, owners are grudgingly adjusting to a cruel reality in which homes are increasingly being sold at a loss. Prices peaked last July and declines are accelerating. In November, prices of existing homes fell 3.5%, the territory's largest single-month fall since the global financial crisis in 2008.

Analysts are predicting a correction as deep as 15%, as Hong Kong faces a triple whammy of the trade war, the slowdown on the mainland and higher real interest rates.

"Hong Kong's almost 10-year housing market bull run looks like it is coming to an end," said Joseph Tsang, executive director at Jones Lang LaSalle in the city.

A huge influx of mainland capital was one reason Hong Kong's residential prices more than tripled after 2009. The authorities imposed a series of restrictions on non-local buyers and prolific investors to try to stem the surge. They largely failed, but now the U.S.-China friction and other external turmoil are doing the job for them.

The headwinds are not confined to China.

In Japan, housing prices in some Tokyo suburbs are falling sharply as buyers become pickier. In early January, the price of a condo in the Eravio Todoroki development just 30 minutes from the central Tokyo Station business district was cut by 13%, to 59.8 million yen (\$550,000).

"It takes more than 10 minutes to walk from the station to the building, which is a little long for customers who prioritize convenience," said a manager with developer Dynacel.



China's real estate sector plays a pivotal role in creating jobs and driving economic growth. © Getty Images

"We started to sell this apartment a year and a half ago, but it was taking too long," the official said. "We wanted to sell out all the units to avoid additional operating costs."

Real estate companies are increasingly wary of that predicament.

"Developers tend to select locations more carefully of late," said Tadashi Matsuda, a chief researcher at Japan's Real Estate Economic Institute. "If condos are far from a station, sales depend more on prices."

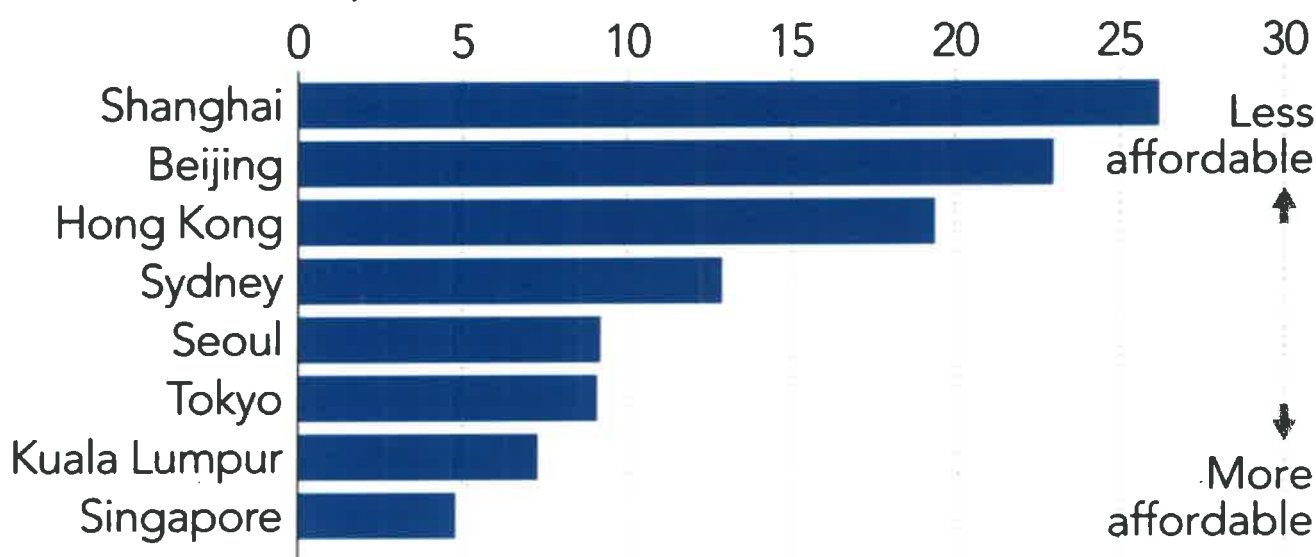
Data from the institute shows that the monthly contract ratio for new condos in the capital area -- the ratio of new units sold to fresh supply -- was under 70% for most of last year. Anything under that threshold is considered unfavorable. The figure for December, announced on Tuesday, was 49.4%, down 23.1 points from the previous year.

This is the first time the ratio has dropped below 50% since August 1991.

And there is a clear divergence between central Tokyo and its periphery. "Sales of condos in the suburbs of Tokyo were in very bad shape in 2018, in contrast to the top form of high-rise buildings in central districts," said Tatsuhiko Hisamitsu, president of consulting company Totalbrain.

Housing affordability in Asian cities

Ratio of housing prices to household incomes (in times)



Source: ADB, Citi Research

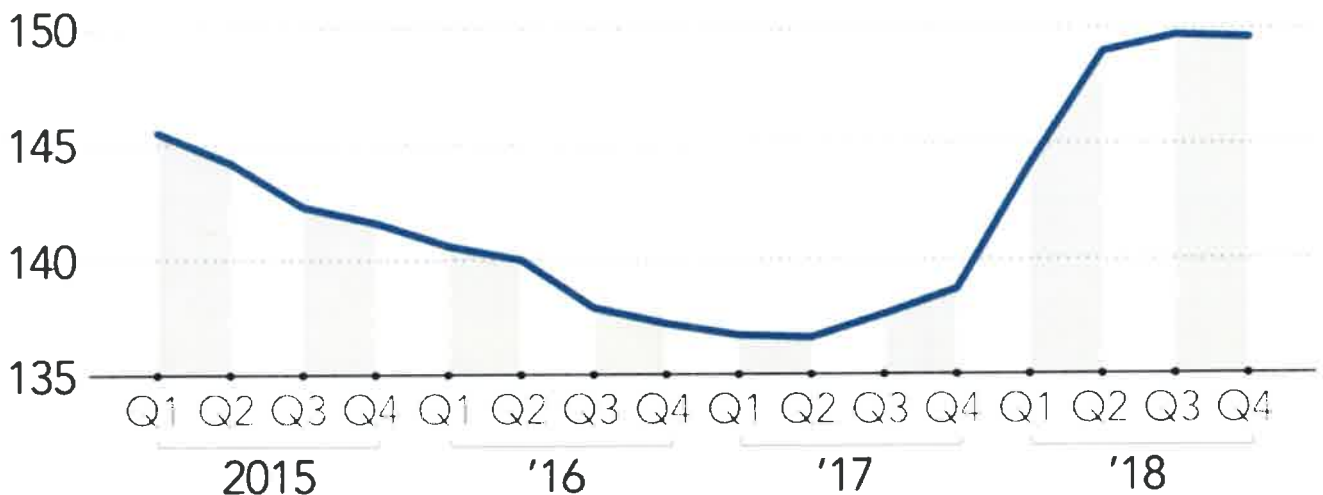
Home prices are determined by a range of factors -- the economic outlook, supply and demand, and interest rates, to name a few.

Prices in many parts of Asia have risen in recent years, with steady economic growth and relatively low interest rates pulling in investment. A study by the Asian Development Bank and Citigroup recently found that home prices were 26 times the median household income in Shanghai, 23 times in Beijing and 19 times in Hong Kong -- an imbalance that raises the risk of a major shock when the market declines.

Some governments have sought to avoid that risk by lowering the market temperature. Singapore stepped in last July with measures including a 5-percentage-point increase on the buyer's stamp duty rate when purchasing a second and subsequent property. This came after the residential property price index rose 9% in the year through last June.

"The sharp increase in prices, if left unchecked, could run ahead of economic fundamentals and raise the risk of a destabilizing correction later, especially with rising interest rates and the strong pipeline of housing supply," the Singaporean government explained.

Singapore's residential price index drops for first time in six quarters



January-March 2009=100

Source: Urban Redevelopment Authority, Singapore

Singapore's intervention led to the first drop in the home price index in six quarters -- a 0.1% fall in the October-December term. "Property prices could have increased by more than 10% in 2018 if not for the July cooling measures, which have been effective in curbing market exuberance," said Christine Li, senior director and head of research at Cushman & Wakefield.

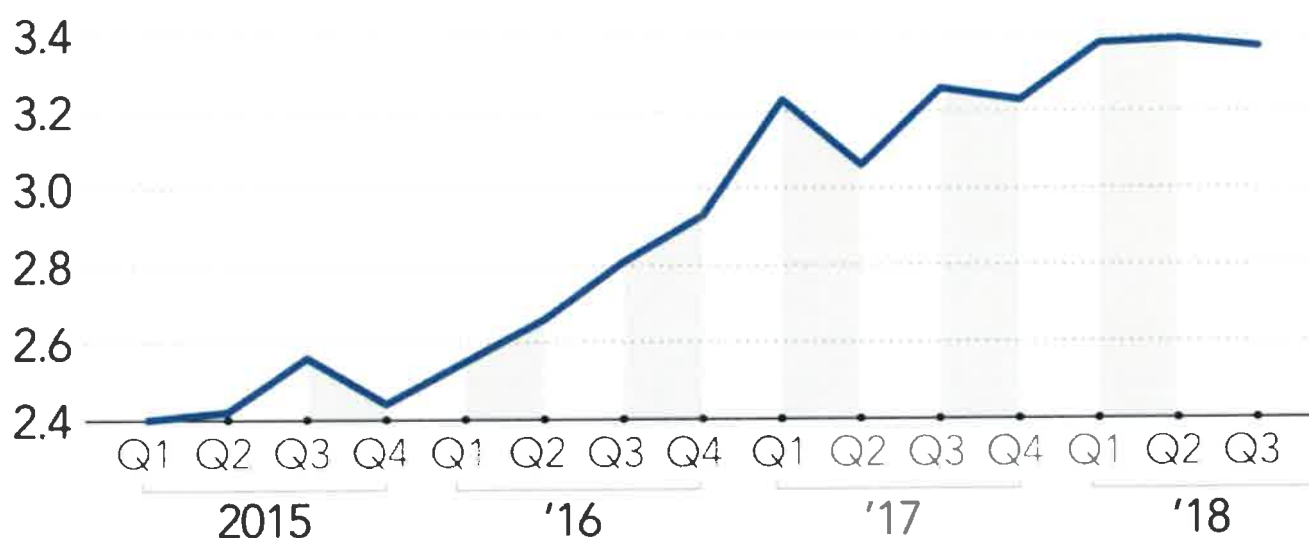
But governments also run the risk of scaring off investors en masse.

"Investors for high-end homes are expected to adopt a wait-and-see approach, as uncertainties in the global financial market have dampened the sentiment somewhat," Li said. "Recent cooling measures have also made it less attractive for foreigners to invest in Singapore residential in the near term."

Nevertheless, Thailand is also tightening its lending criteria for housing loans this year, aiming to rein in household debt.

The country is concerned about the rising ratio of nonperforming housing loans, which stood at 3.37% at the end of September, according to the Bank of Thailand.

Thailand's ratio of nonperforming housing loans has surged *(in percent)*



Source: Bank of Thailand

The central bank governor, Veerathai Santiprabhob, cited the nonperforming loan ratio as a danger to domestic financial stability, noting that such loans have continued to rise "especially among second- and third- home buyers."

Under the new rules, anyone buying a second home will have to make a down payment of at least 20% of the value to qualify for a mortgage exceeding 10 million baht (\$310,000).

What trajectory will Asia's markets take now?

"One key area to watch this year is the pace of interest rate hikes, which will likely weigh on home buying interest should they escalate sharply," said Tricia Song, head of research for Singapore at Colliers International.

Chinese fiscal stimulus is another factor to monitor. Praveen Choudhary, property analyst at Morgan Stanley, predicts prices in Hong Kong will drop more than 10% in the next six months but stage a modest recovery in the second half of the year, as Beijing stabilizes its economy and Washington pauses its hikes.

Capital Economics analyst Chang Liu is more pessimistic about Hong Kong, warning that a declining property market could impact other sectors in the territory of 7 million people. The analyst foresees a 30% decline in Hong Kong property prices over the next five years, leading to a 3% to 6% contraction in consumption and a 0.5-percentage-point reduction in annual gross domestic product growth.



China's softening property market has made consumers and travelers less inclined to splurge on luxury brands. © AP

An Asiawide housing slump would take a toll at the best of times, and these are not the best of times. The U.S.-China trade war threatens to destabilize the world economy, and for now the uptrend in U.S. interest rates has begun to suck money out of emerging countries.

Banks, developers and homeowners would be the first to suffer, but the ripples would fan out from there.

"We think weaker housing markets will impact economic activity," Citigroup analysts noted in a recent report, citing "implications on household consumption," including hits to wealth and confidence, as well as construction- and housing-related employment. They also expect detrimental effects on real estate investment activity.

"We find that the impact [of] housing prices [on] consumption is particularly high and statistically significant in more developed Asian economies -- New Zealand, Korea, Japan, Australia (and a tad bit in Hong Kong) -- but is surprisingly also disproportionately high ... for the Philippines," the analysts added.

China has already seen how a real estate slump, coupled with a stock downturn, can **dampen consumption**. While retail sales grew 9% on the year in 2018, the figure was down from 10.2% in 2017.

Now, as the real estate warning signs spread, it's buyer beware in Asia.