

Special Comment

Pilot program for property tax reform has limited impact on rigid demand, but may adversely affect property sales

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Hong Kong, 5 November 2021 — China Chengxin (Asia Pacific) Credit Ratings Co., Ltd. (“CCXAP”) believes that the pilot program for property tax reform has limited impact on rigid demand, but may adversely affect property sales in the near term. In the long run, we should pay more attention to the credit quality of property developers that have poor regional layout.

On 23 October 2021, the Standing Committee of the National People's Congress decided to authorize the State Council to pilot property tax reforms in some regions. Property tax should be levied on all types of residential and non-residential property in pilot areas, while lawfully-owned rural homesteads and houses built on them are excluded; taxpayers are the holders of land-use rights and house owners. The State Council will decide on specific approaches, while the local governments of the pilot areas will decide on the specific procedures for tax collection. The date of start of the five-year pilot program will be determined by the State Council.

The pilot program aims to (1) establish a long-term regulatory mechanism for property market, and facilitate its steady and sound development; (2) regulate income distribution, which help achieve social justice and narrow the gap between the rich and the poor; (3) broaden the tax income sources of local governments, and alleviate their reliance on land transfer income.

We expect that the influences of the property tax reform on property market include (1) reduction on investment-oriented housing demand, but limited impact on rigid demand; (2) increasing divergency of the property markets in different regions driven by rigid demand; (3) increasing liquidity pressure of some property developers with high debt burden and poor cash collection.

Reduction on investment-oriented housing demand, but limited impact on rigid demand

We believe that the launch of property tax has limited impact on rigid demand. On one hand, certain preferential policies for homebuyers with rigid demand may be introduced. On the other hand, the rigid housing demand is more related to the income level of residents and the concept of housing consumption, and it is relatively less sensitive to rising costs caused by taxation. As tax costs rise and investment attribute of property market weakens, the investment-oriented demand of house purchase will be reduced. However, if the policy is implemented too quickly that the scope of pilot area and the strength of the taxation exceed market expectations, it may also have a certain negative impact on the rigid demand of house purchase.

Increasing divergency of the property markets in different regions driven by rigid demand

Since the main purpose of introducing property tax is to guide the rational housing consumption, with the combined effect of various property regulatory policies, the future house purchase demand will be more related to factors such as regional economic development and population size. The degree of differentiation of property market in different regions may be increased. The inventory pressure of cities with high land supply, slow or even negative population growth may further increase.

Increasing liquidity pressure of some property developers with high debt burden and poor cash collection

Since the second half of 2021, the national sales of commercial housing have cooled down. Sales amount and area has been declining on YoY basis since July 2021. The decline of investment-oriented housing demand may increase the sales pressure of real estate enterprises, and the liquidity pressure of some property developers with high debt pressure and poor cash collection. In the rigid demand dominated property market, the sales performance of property developers will also be more closely related to the regional layout. We should pay more attention to the credit quality of property developers that have more layout in areas with low population and economic growth.

In conclusion, CCXAP believes that the pilot program aims to facilitate the steady and sound development of China's property market, regulate income distribution, broaden the tax income sources of local governments and alleviate their reliance on land transfer income. As the real estate industry still plays an important role in China's economy, we expect that the progress and intensity of property tax reform will be largely in line with market expectations, under the current policy goal of "stabilizing land prices, stabilizing housing prices, and stabilizing expectations". We expect that the launch of property tax could reduce investment-oriented demand of house purchase, but has limited impact on rigid demand. Therefore, with the reduction on investment-oriented demand and the delay of some rigid demand, house purchase demand may be suppressed in the short term, which will further increase the sales pressure of property developers and the liquidity pressure of some property developers with high debt pressure and poor cash collection. In the long run, since the main purpose of introducing property tax is to guide the rational housing consumption, with the combined effect of various property regulatory policies, the future house purchase demand will be more related to factors such as regional economic development and population size. The degree of differentiation of property market in different regions may be increased. We should pay more attention to the credit quality of property developers that have more layout in areas with low population and economic growth.



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