# The Hidden Dangers of Chinese Economic — based on Real Estate

Yingbo Zhao *

Shangdong University of Finance and Economics, Shandong, China

* Corresponding Author Email: 15050240135@xs.hnit.edu.cn

**Abstract.** Chinese economy has ever developed rapidly. However, the economic development had tended to be slow in the past three years. Although the emergence of COVID-19 has hit the economic order of almost every country in the world, of course, China is one of them. However, the reason why China's economic development speed has become slow is mainly from the hidden dangers of own economy. Real estate is also a very important part of the hidden dangers of economic development. Because the real estate industry is an extremely important part of China's economy. Based on the connection between the real estate industry and the bubble economy, the population income and real estate, public policy and real estate, the problems and the development model of real estate, this paper shows that there are many hidden dangers in the development of real estate. Through research and analysis, these problems have fully affected the development of China's economy. By improving these problems, the economy will also recover and develop.

**Keywords:** Bubble economy; population income; public policy; the development model of real estate.

## 1. Introduction

The form of China's economic development in recent years is not clear. The data responded adequately that China's economic growth rate had suffered a setback. According to China's annual economic report, China's GDP grew by 6.1 percent in2019 [1]. But in 2022, according to the first half of the growth data, China's GDP grew by 2.5 percent year-on-year [2]. Though the COVID-19 epidemic which has lasted for three years, has hit all industries in China. It is merely the blasting fuses for the hidden dangers of all walks of life. In the process of China's rapid economic development, the real estate industry used to play its way out well. This also makes people ignore the many hidden dangers of development under the rapid development. The real estate industry as a whole shows a decling trend. This is clearly illustrated by using a 2022 data chart. Figure 1 shows that National real estate development and investment growth rate [3].

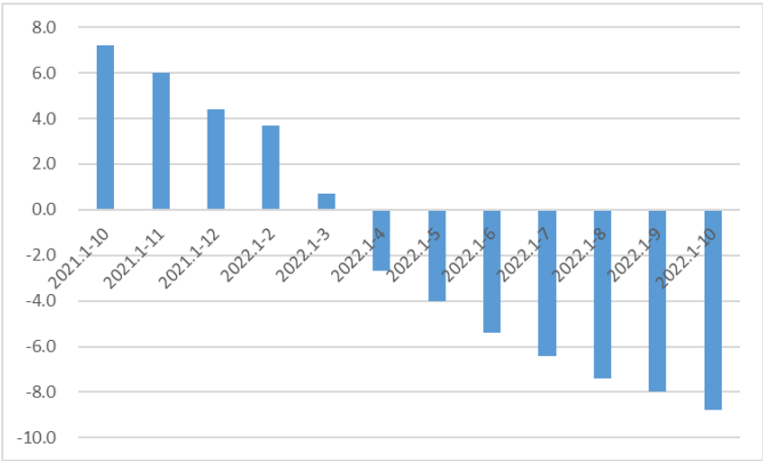



**Fig 1.** National real estate development and investment growth rate

By studying the hidden dangers of real estate, the research hopes to solve the problems in the real estate industry while solving some of the hidden dangers of China's economic development and put forward constructive suggestions on the development of the real estate industry and the Chinese economy.

## 2. The Status Quo of the Real Estate Industry and the Potential Dangers

### 2.1. Bubble Economy

It's not hard to think of Japan when it comes to the bubble. In popular terms, the bubble economy can be interpreted as a false prosperity. China's economic growth rate has slowed down in recent years, but housing prices in first-and second-tier cities, remain high. Despite the high price, many houses are in a state of price without market. The capacity for sustainable development is the most important factor in marcoeconomic development. And this is what the bubble economy lacks.

The Japan's economic crisis in the 1990s was a representative of the bubble economy. Japan's real estate market was too hot. At the end of 1990, the national market value of Japanese land was 2,356 trillion yen, about 5.5 times the norminal GDP of that year [4]. This trend inevitably presents the bubble economy. Japan enacted a tight monetary policy to save the situation. But the real economy had declined and the marked was full of speculators. The stock market collapsed, and the loss of money led to a lot of businesses failing. Then property prices fell rapidly. A series of ripple effects have reached all industries in Japan. All kinds of industries faced a recession. The negative effects of the economic crisis have yet to be resolved.

Introduce data to measure the relationship between real estate and the bubble economy. The ratio of the growth rate of housing prices to the growth rate of GDP represents the severity of the bubble economy. The data less than 1 represents the bubble economy within a reasonable range. The data greater than 1 and less than 2 represents the bubble economy with an early warning. The data more than 2 represents the bubble economy has emerged. Figure 2 shows that housing prcie growth rate/GDP growth rate.

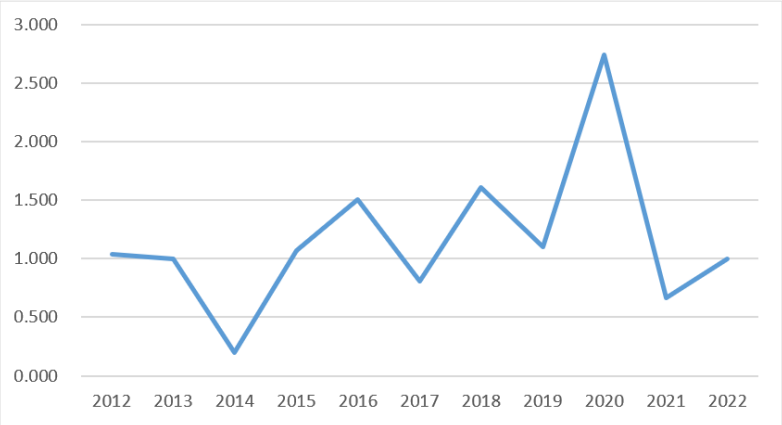



**Fig 2.** Housing price growth rate / GDP growth rate

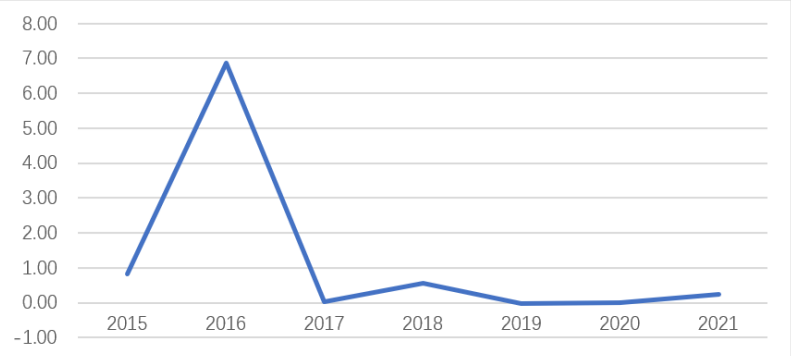



**Fig 3.** Beijing Housing price growth rate / GDP growth rate

It is not hard to see that most of the time China is in a state of bubble economic warming. Due to China's vast territory, there is a large gap between the development speed and speed of cities, and the real estate prices are mainly driven by first-tier cities, and GDP first-tier cities contribute more.

Contributing nation alone is not enough. Take the Beijing as the representative. Figure 3 shows that Beijing housing price growth rate/GDP growth rate.

Due to the balanced and rapid economic development of first-tier cities, the bubble economic is roughly in a reasonable state. Take Jinan as a representative of the second-tier cities. Figure 4 shows that Jinan Housing pricee growth rate/GDP growth rate.

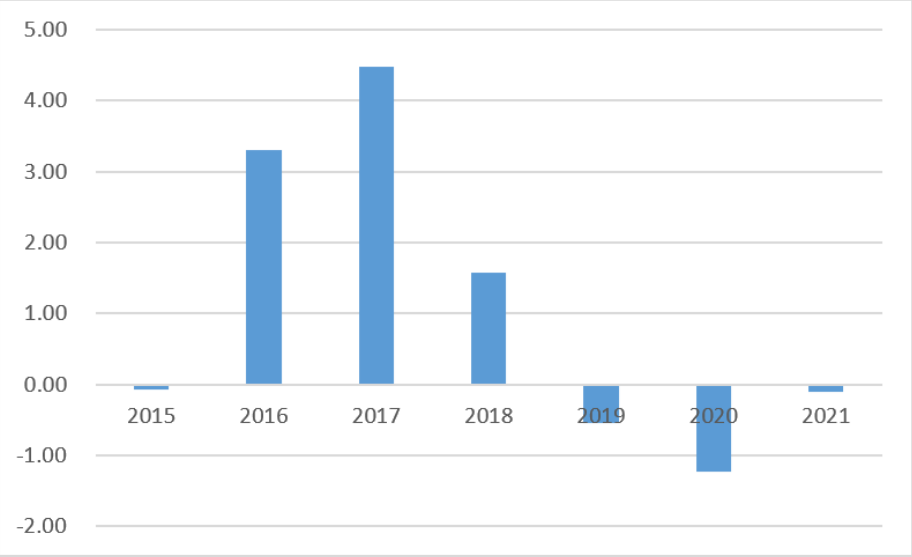



**Fig 4.** Jinan Housing price growth rate / GDP growth rate

This set of data variances is large. It is easy to understand that the epidemic has caused lower incomes. This particular period has caused a decline in housing prices. The data from 2016-2018 are more telling. Second-teir cities are the hardest hit by the bubble economy.

The easing of China's bubble economy in recent years is closely related to the decline in housing prices caused by epidemic. After China lifted the epidemic prevention and control, the government will certainly try to stimulate the economy. House prices will bottom out and rebound. Preventing the bubble economy is very important. Once the housing price rises too violently, the brought economic hidden danger is very destructive.

### 2.2. Population Income

The mismatch between high housing price and income is a hidden danger for the development of the real estate industry, and also one of the hidden dangers for economic development and social stability.

China's real estate development has a historical origin. China's real estate industry has made an indelible contribution during the period of rapid economic development. There are many reasons for this. First of all, real estate market is an important means to stimulate domestic demand. The development of real estate is not simply the development of its own industry. Its radiation surface is very wide. The real estate industry is very large. It can drive both the furniture industry and the construction industry at the same time. It is able to increase government taxes. Through the construction of shops to drive consumer demand. Second, real estate plays an important role in stimulating the financial industry. The real estate industry is leveraged. That makes real-estate developers happy to use it. This financial leverage combined to GDP, the effect of pushing the GDP is incomparable.

The government attaches great important to the development of real estate. Property prices are constantly rising. To show with intuitive data. Figure 5 shows that housing price growth rate.

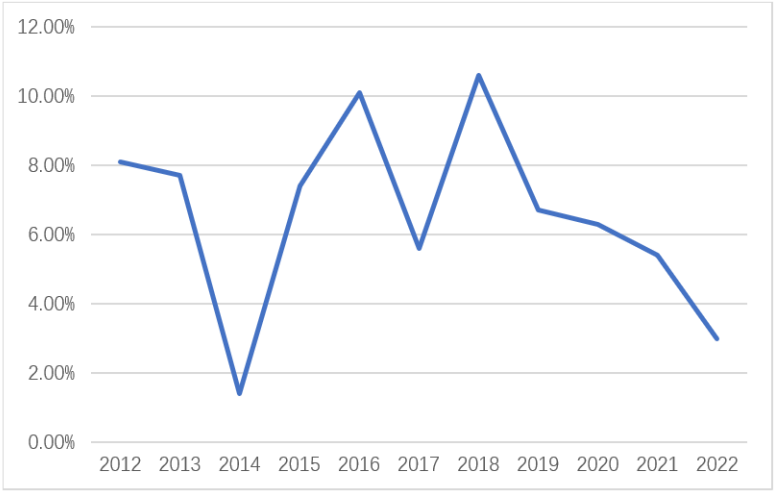



**Fig 5.** Housing price growth rate

There has been no negative growth in the past few years. The relationship between housing price and income can be quantified by the ratio of house price to income. The World Bank proposed this data is normal between 1.8 and 5.5 in developed countries and between 3 and 6 in developing countries. Look at China's housing-price-to-income ratio data. Figure 6 and Figure 7 shows that National house-price-to-income ratio and Beijing house-price-to-income ratio.

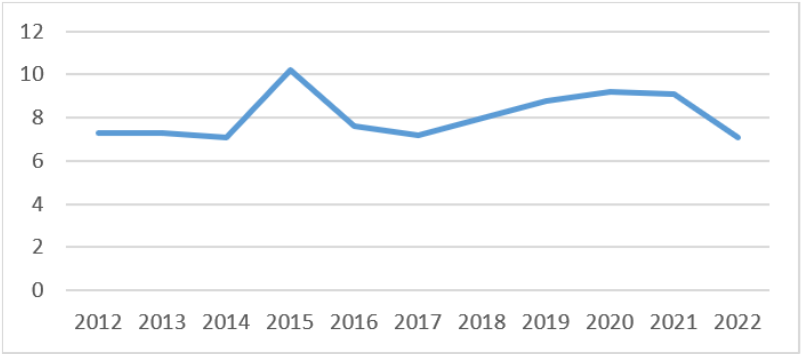



**Fig 6.** National house-price-to-income

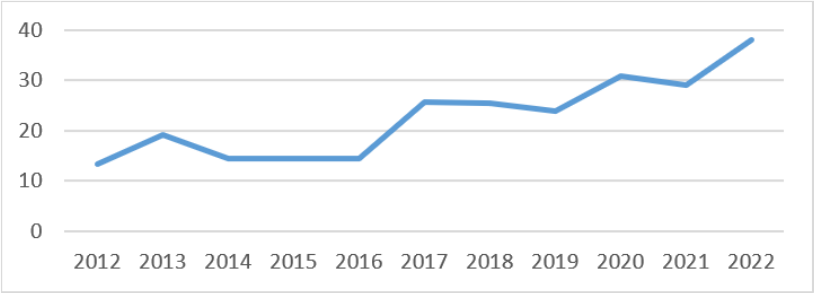



**Fig 7.** Beijing house-price-to-income

This data is not difficult to see that China's value is very high. This means that a significant number of people can't afford a house. In such a situation, the young people will be under a lot of pressure. One senario is that people will carry huge mortgages for long times. The expansion of long-term debt may rationally not have that much impact on consumption. Even in some ways, it can stimulate the consumption of daily necessities. But from reality it is not consistent with reason. In second-tier cities, taking Jinan as a example, the average price of real estate is 15889 yuan per square meter. At the same time, the per capita housing area in Jinan is 39.3 square meters [5].The per capita income in the same year was 114596 yuan. Let's say that if a family has three people, both the couple and one child accumulate the housing area, and the couple pays the average salary as the average house price of the house. They need to pay 1873313, 1 yuan. That's about eight years of their salary. Spending due to

living injuries. They have huge mortagage loans of more than a decade. This is only a reasonable estimate. Young people have a house purchase demand. However, many young people do not earn more than the average income. More than half of urban areas are also higher than average. The reality will be trickier. More young people will tend to become risk-averse people. Investors who are risk adverse reject investment portfolios that are fair games or worse. Risk-averse investors consider only risk-free or speculative prospects with positive risk premiums [6]. People are more inclined to rent house. This is a purely expenditure act. It is less good for stimulating the economy and investing than buying house. At the same time, savings decline because of huge mortgages. Downward pressure on the economy continues to increase. Meanwhile, the employment pressure caused by the epidemic is great, this undoubtedly adds to the situation. House price growth is slowed but not stalled. People's incomes have never matched their value with house prices. This is laying the hidden danger for the real estate market crash. And the huge debt will add to the pessimism about markets and economic development. It is a hidden danger for China's economic depression as well.

### 2.3. Public Policy

There is currently no bubble economy in China, but the warming is already in place. The mismatch between per capita income and housing prices also needs resolving. So the government has introduced a lot of policies to prevent and solve problems. It's hard to predict that a policy is good or not before its appearance. Some policies have backfired, and even add new hidden dangers for the development of the real estate industry.

First of all, it should not be ignored that many people regard real estate as a mean of speculation. Property speculation phenomenon has largely driven up housing prices. This will increase the income of a price in the entire housing market. Most people don't have their income increase as a result. But it faces even higher housing prices. The purchase restriction policy is one of the means to adjust this phenomenon. This policy limits the number of homes people can buy. Most of its policies are based in family units. In the short term, it works to limit housing prices. But the unit measurement of this policy is problematic. This ignores people's subjective initiative. People can split up their family units by divorce. Property developers can also weaken policy by controlling the amount of housing supply. Meanwhile, for different cities, the effect of the policies is also completely different. The purchase restriction policy plays a significant role in the housing price and income in second tier cities, but has the opposite effect in third-tier cities [7]. This policy has great limitations, resulting in the gray industry is also unavoidable.

The second option is renting. Renting houses can save a lot of money rather than making direct purchases. But this is only a superficial and rational expectation. Specifically, many aspects are still not ideal. First the added value of buying house is much greater than that of renting a house. Buying a home represents not just the ownership of the home, but also linked to settlement policy and children's education. In the long run, most people will not necessarily choose to rent. According to the data, only 10 percent of the young people do not choose to buy house [8].It can be explained that renting instead of buying is only a short-term policy, in the long term, people are more inclined to buy a house.

From the macro level, China's policy regulation is not all reasonable. The main goal of government policy is to control prices. The rules of the market itself are ignored many times. The real estate industry is highly bound to the domestic economic development. The value of real estate assets is high and stable. This determines that the real estate industry can be used as a tool for credit expansion. At the same time, most real estate companies rely on bank loans. Most policies have a huge impact on companies. Moreover the policy focus on the demand side reform, and the supply-side structural reform has always been not deep enough. The real estate industry developed too fast in the early stage, and the social public policies did not follow up in the late stage in time. Listed companies take advantage of the early hot market to circle money and get high debt. The market is in a state of deformity. Government policy should not be about controlling prices merely, the establishment of a healthy operation market and improve the supply side structure is the focus. And stick to the reality,

government should solve the problems of construction quality and low-income people. Many of the current policies in operation are not only difficult to solve long-term problems, but also will leave hidden dangers for future development.

### 2.4. The Development Model of Real Estate

Real estate is a leveraged industry. To some extent, the leverage ratio can promote the capital operation and economic development. The development of real estate in China is heavily dependent on banks. High leverage is inevitable. Such a running model is at high risk.

Financial leverage and the capital structure are interactive. The behavior of enterprises in financing through financial leverage will expand their leverage coefficient. When this value exceeds a certain amount, the financial risk will change and increase. When the financial leverage coefficient is greater than 1,it indicates that the financial risk is greater. And most of the domestic real estate enterprises the financial leverage coefficient is greater than 1.

Leverage is not only in the real estate development but also in the overall economic development. Linkage with the housing price growth modelm is the household leverage ratio. Due to the high house prices, mortage loan is an important part of residential loans. The growth of the housing prices is the most important means to increase the household leverage ratio. This can be seen in the high housing prices in China and the increase in them, the household leverage ratio is at a relatively high level. The data can also be clearly illustrated. Figure 8 shows that Residential leverage ratio.

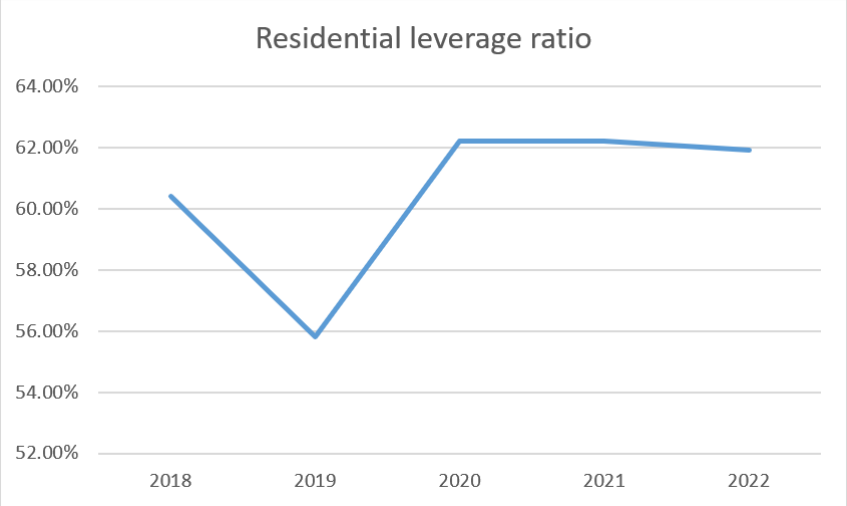



**Fig 8.** Residential leverage ratio

Over the last five years of data, resident pole rate is very high. Whether it is the financial pole ratio or the resident leverage ratio, both levels are above the risk line. China's debt levels are risky. While using the real estate industry as catalyst for economic development, it has failed to effectively control the disadvantages brought about by the rapid development.

### 2.5. Result

According to the above way to cut into the problem, China's real estate has great hidden dangers. The problem is mainly concentrated with high housing prices. So most of the solutions to the problem are biased to control prices. Suppose that prices are controlled with policies, whether the real estate can be developed reasonably. From the current policy and the actual housing prices, the role of price control can be said to be a drop in the bucket. Solving the hidden dangers of real dangers is related to solving the hidden dangers of China's economy. It needs to consider from many aspects rather than simply control the price.

## 3. Discussion

Through the above methods of analysis, they can clearly reflect the development of real estate hidden dangers. And China is facing such hidden dangers, it should not trace it back to the source but also prevent and solve.

### 3.1. The Root Cause of the Rapid Real Estate Development

In the late 1980s and early 1990s, China's economic situation was not clear. China began its tax-sharing reform in 1994.Under this system, the central government's ability to absorb its finance is enhanced. National tax revenues have increased dramatically. This policy increases the power of local governments and weaken their financial power. The government seeks development through a large increase in revenue.

Under this system, state power is easier to concentrate. But local governments are in a relatively tight state. The 1994 reform made all the land use transfer fees transferred by the central government to local governments and shared with other local governments [9]. Land finance was born. There are two modes of local government using land. One is the industrial land used to attract investment. The other part is the conmmercial land sold to real estate developers. The functions of two lands are different. Industrial land is sold at low price which is used to attract talents and stimulate empolyment. When a city had more capital more people who had more income, people will have a need to buy houses. At this time, commercial land was sold at high prices for real estate development. High land prices mean high housing prices. and mean the government will have more revenue. The government uses the high income to complete the infrastructure construction and optimized tax policies to attract more investment and more talents. House prices in this model cycle, step by step increased.

The revenue and economic growth form this development model are not enough. Land is a natural credit tool. Land is great collateral. Local governments use land mortgages to get capital. That takes advantage of the high leverage of property. And the ownership of the land essentially belongs to the state. The yuan is issued by the state. Use the land of the country to borrow its money, this establishes the relationship between the land price and the currency price. It also gives the real estate industry greater economic significance in China. The uses of financial leverage itself is the use of the future to develop the current behavior. Although this makes the country develop rapidly, housing prices will inevitably rise significantly.

### 3.2. Disadvantages of Development

On a personal level, it's still income problem. When people's income is slow to meet the demand for housing, people will have pessimistic expectations of economic development. Meanwhile, the rapid rise in housing prices is widening the gap between the rich and the poor. The people who buy a house first because of the continous appreciation of the property, and the capital gap between those who did not buy a house is widen.

At a marco level, the local government debt problem is quite serious. Because of too much use of real estate to develop the economy, the economic danger has emerged. Develop with a high leverage ratio, local government is in a state of high debt ratio, and residents are in a state of high debt. Because the old development model depends on the growth of house prices, looking at lowering house prices could hit the economy hard. Therefore, it is impossible to quickly unbind the real estate and economic development. And the social benefits brought by infrastructure construction cannot be realized in the short term. So, it is difficult to control real estate prices. Local governments rely on debt to contribute to the rapid development of infustrializetion fot a certain period of time. One study showed that, real personal income per capita is significantly and positively associated with debt levels of local governments and debt levels of all state and local governments taken together [10]. But too much reliance makes it difficult to transform the economy, it is too difficult to solve.

## 4. Suggestions

The above content fully illustrates the complexity of the real estate problems. It also fully shows that solving the problems should not only consider controlling the price. As the former driver of economic development, it is absolutely impossible for real estate industry to be directly separated from the economic development.

But in the current Chinese society, problems are forcing the real estate industry to change.

First of all, China needs an economic transformation. Although China's industrial system is perfect the driving force for innovation is insufficient. Industrial brand influence is insufficient. The second is the decrease of China's available land area, and the urbanization is approaching saturation. In the long term, the aging is also urging the real estate to change.

The transition will go through the pain period. But the transition is necessary. In a sense, the development of real estate combined with finance is the full use of debt leverage. In the long run, the bubble economy will gradually emerge. The development of the real estate industry is ostensibly a real industry. The core of promoting development is actually finance.

This article does not believe that the real estate industry will decline and exit the historical stage. Simply addressing bubble economies is also inefficient. It should start with the high-tech industry. Attach importance to the development of new energe and other industries. Reduce the resources occupied by the real estate industry through macro-control. The driving force of economic development gradually becomes diversified. The government's thinking on economic development should also gradually change. Don't just pursue development speed. The negative effects of the pain of economic development are more acceptable than the economic collapse caused by a bubble economy. With the self-strenthening of market expectations the real estate price soon divorced from reality, when the hyped capital chain is unsustainable, the bubble is like a nuclear bomb explosion, cause a chain reaction [11].The generation of bubble economy is destructive to the national economic security. At present, Chinese young people have a serious pessimistic attitude towards economic development. High housing prices are a big reason. Meeting the employment needs is not enough. It need to make the housing price hierarchy more clear, enabling young people to temporarily buy houses that may not be good enough but belong to their own. Seeking economic development requires not only rational consideration but also a full consideration of human spiritual needs.

Three years of the epidemic made the real estate industry ushered in a cold winter. China's economy is also in urgent need of a recovery. Despite economic difficulties, it is also an opportunity. If once again focus on using real estate to restore the economy, then the economic pattern will be difficult to change.

## 5. Conclusion

According to the study, there are hidden dangers in the real estate industry in bubble economy, population income, public policy, the development model of real estate. And take these hidden dangers as the breakthrough point, the research to solve the problems of the real estate industry. The government can not only control the price, should consider many issues. The real estate industry plays an important role in China's economic development. The problems existing in the real estate industry also represent the hidden dangers of China's economic development. China's economic recovery and development cannot rely solely on the leverage of debt. Respect the objective economic law while developing industry and encourage the development of private industry. China should establish a reasonable economic development driving structure and pursue high-quality development, rather than just focusing on the speed of development.

This research is devoted to discovering the hidden dangers of real estate development and the root causes of the hidden dangers, and putting forward reasonable suggestions. Due to the variety of data calculation methods some data may be different from the real situation. More practical research should be done.

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