



**OBSERVATORY
GROUP_{LLC}**

The Role of Central Bank Policy in China's Housing Development

--Discussion about the Paper on China's Shantytown Renovation
by Zhiguo He, Zehao Liu, Yang Su and Kunru Zou

June 2024

Discussion Overview

- I. **Definition of Shantytown Renovation Program (SRP) and its links to the central bank policies in China**
- II. **The paper's contributions to China's housing policy analysis**
- III. **Thoughts on further research and policy discussions**

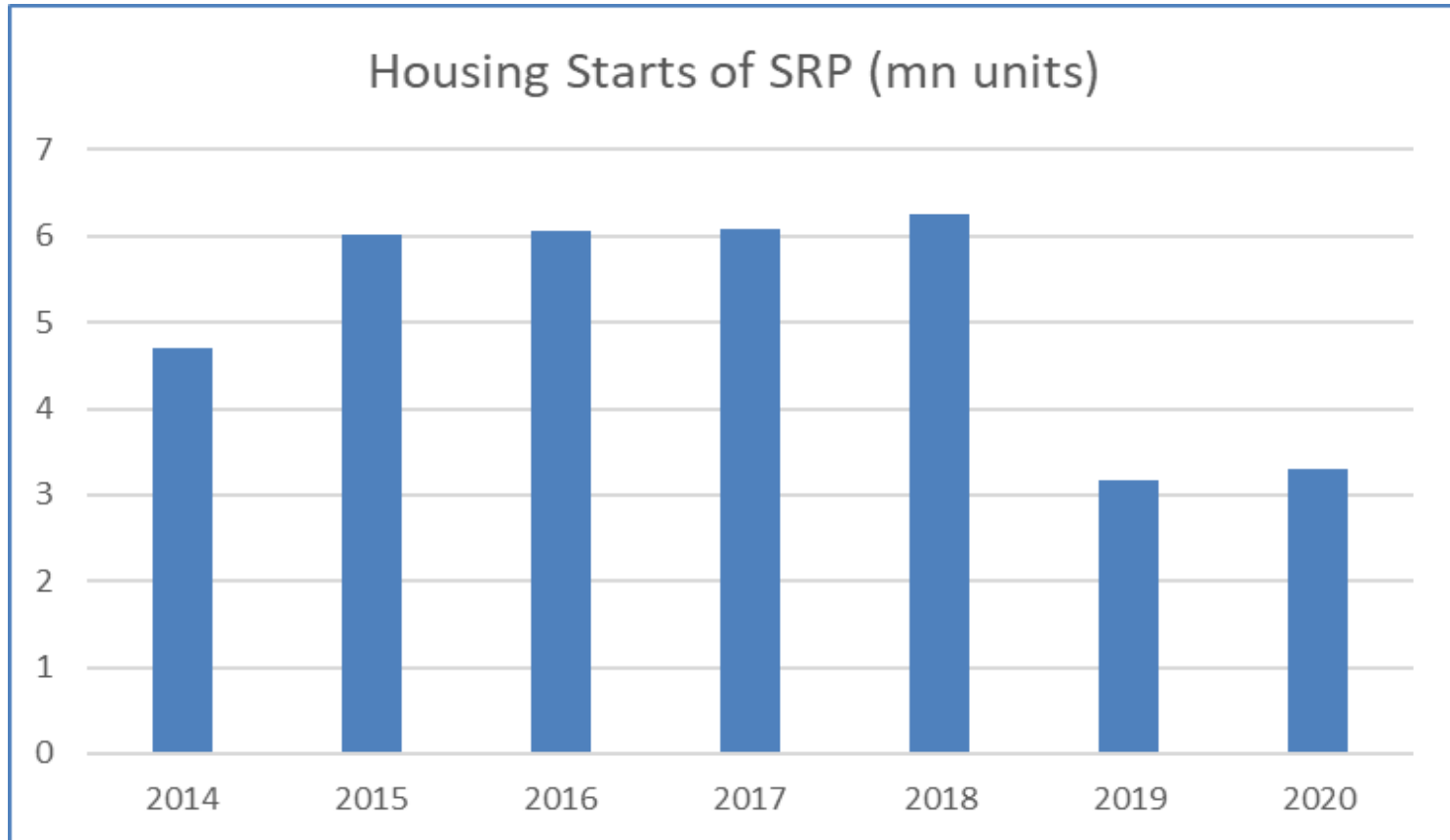
I. What's Shantytown Renovation Program

Urban redevelopment program led by Chinese government

- **Definition:** SRP is a large-scale government-led urban redevelopment program in China, which started in 2008 but accelerated in 2014-2018.
- **Goals:** Initially, SRP aimed to upgrade urban slums and improve low-income people's living conditions (welfare-oriented), but eventually was used to support local housing market and to reduce home inventories (efficiency-oriented).
- **Size:** total housing starts of more than 29 mn units in 2014-2018.
- **Resettlement Approaches:** In-kind resettlement vs. cash resettlement

I. What's Shantytown Renovation Program

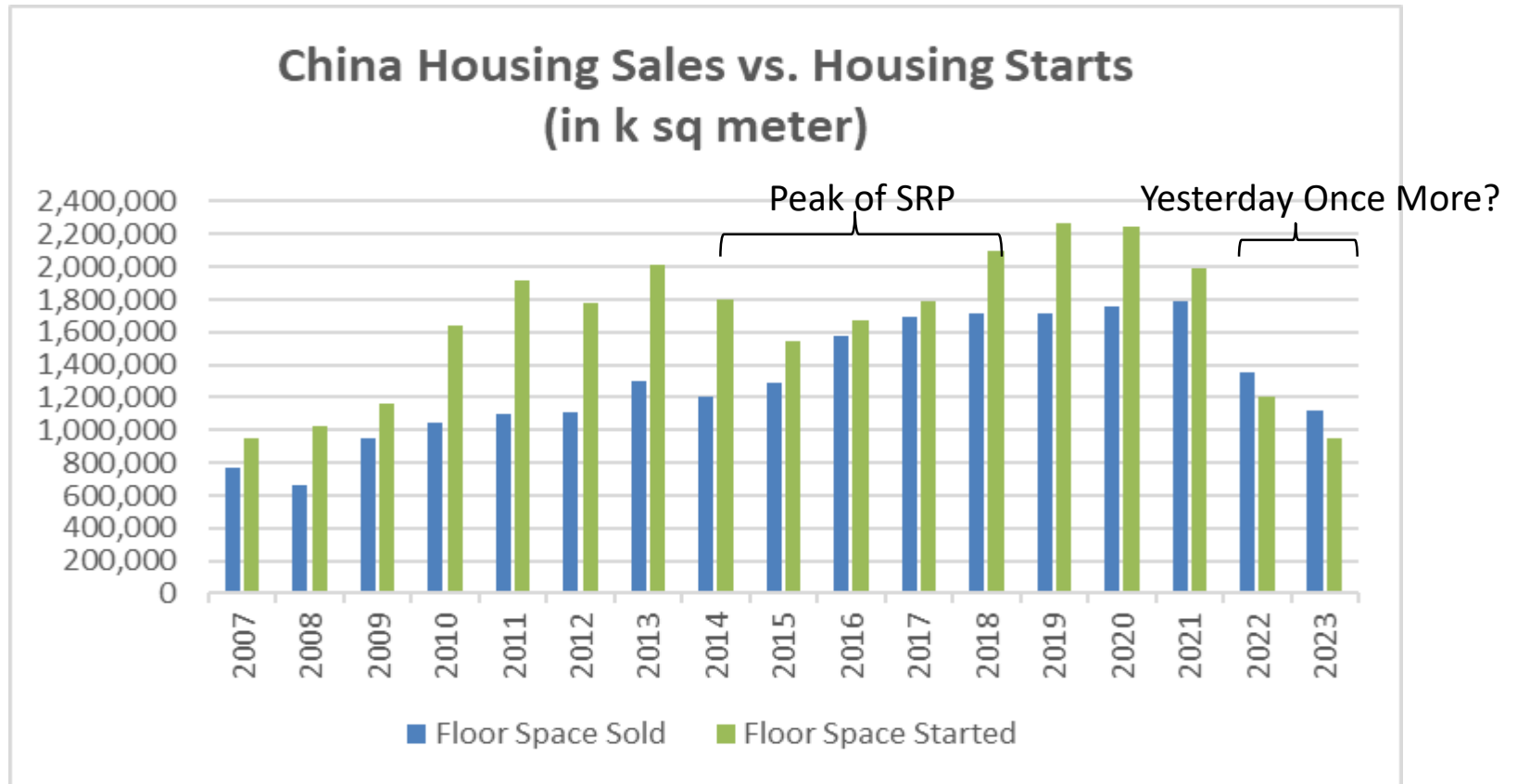
Urban redevelopment program led by Chinese government



Source: China's Ministry of Housing and Urban & Rural Development

I. What's Shantytown Renovation Program

Urban redevelopment program led by Chinese government



Source: CEIC

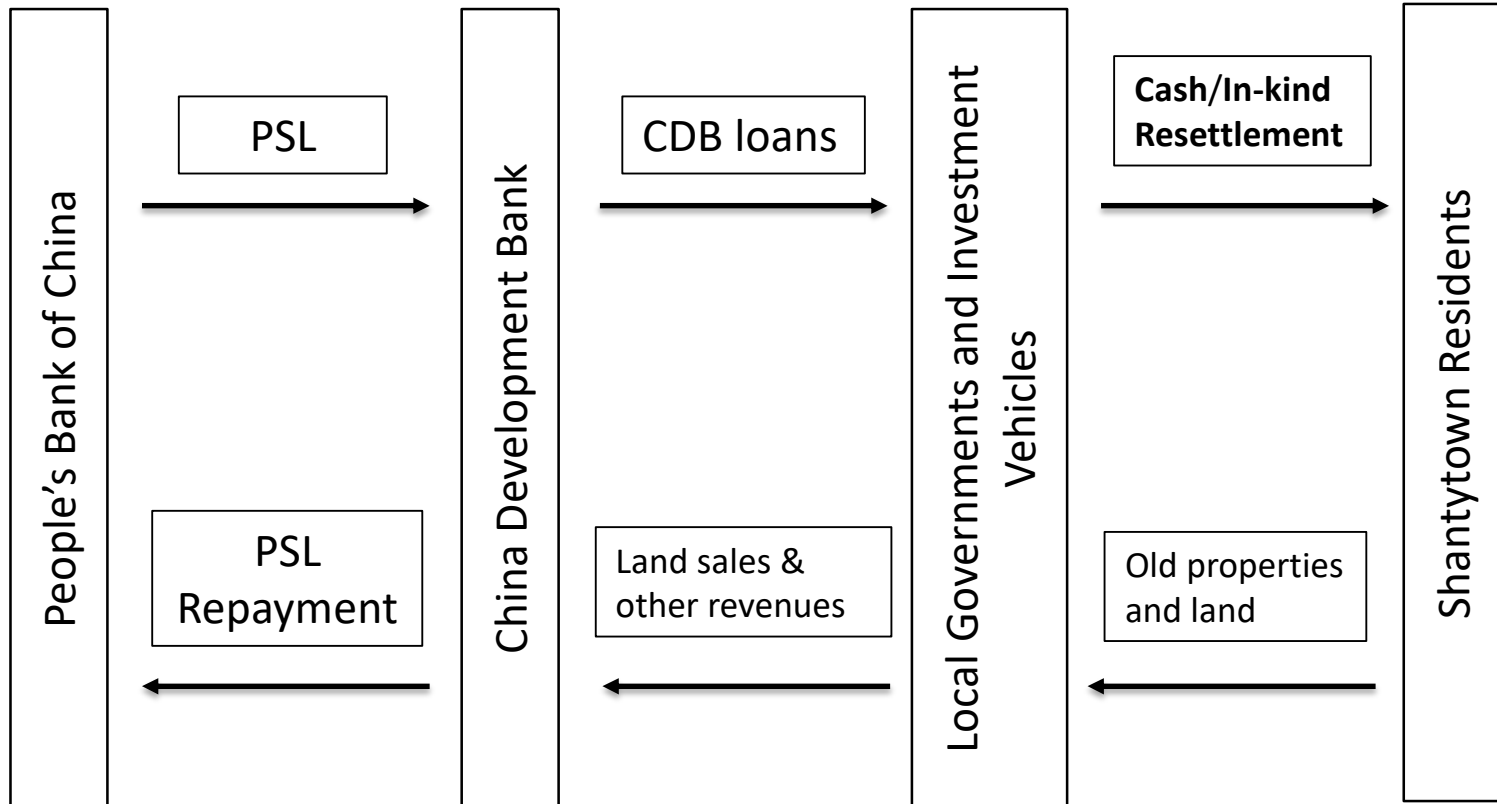
I. What's Shantytown Renovation Program

Urban redevelopment program financed by the central bank

- **Pledged Supplementary Lending (PSL):** a structural monetary policy Instrument of the PBoC that provides funding support to SPR and some public infrastructure programs. It is a targeted lending program that directly expands the central bank's balance sheet and is often labelled (inaccurately) as the PBoC's QE program.
- **China Development Bank (CDB):** China's largest policy bank that facilitate functions of both fiscal and monetary polices, sometimes dubbed as China's second Ministry of Finance (MoF).
- **Coordination between PBoC and CDB:** China's Central Banking Law prohibits direct lending of the PBoC to non-bank institutions. To some extent, it uses CDB as a "conduit" to provide funding to SRP through PSL program. But CDB's role is more than a "conduit", as it provides collateral and takes credit risk onto its balance sheet.

I. What's Shantytown Renovation Program

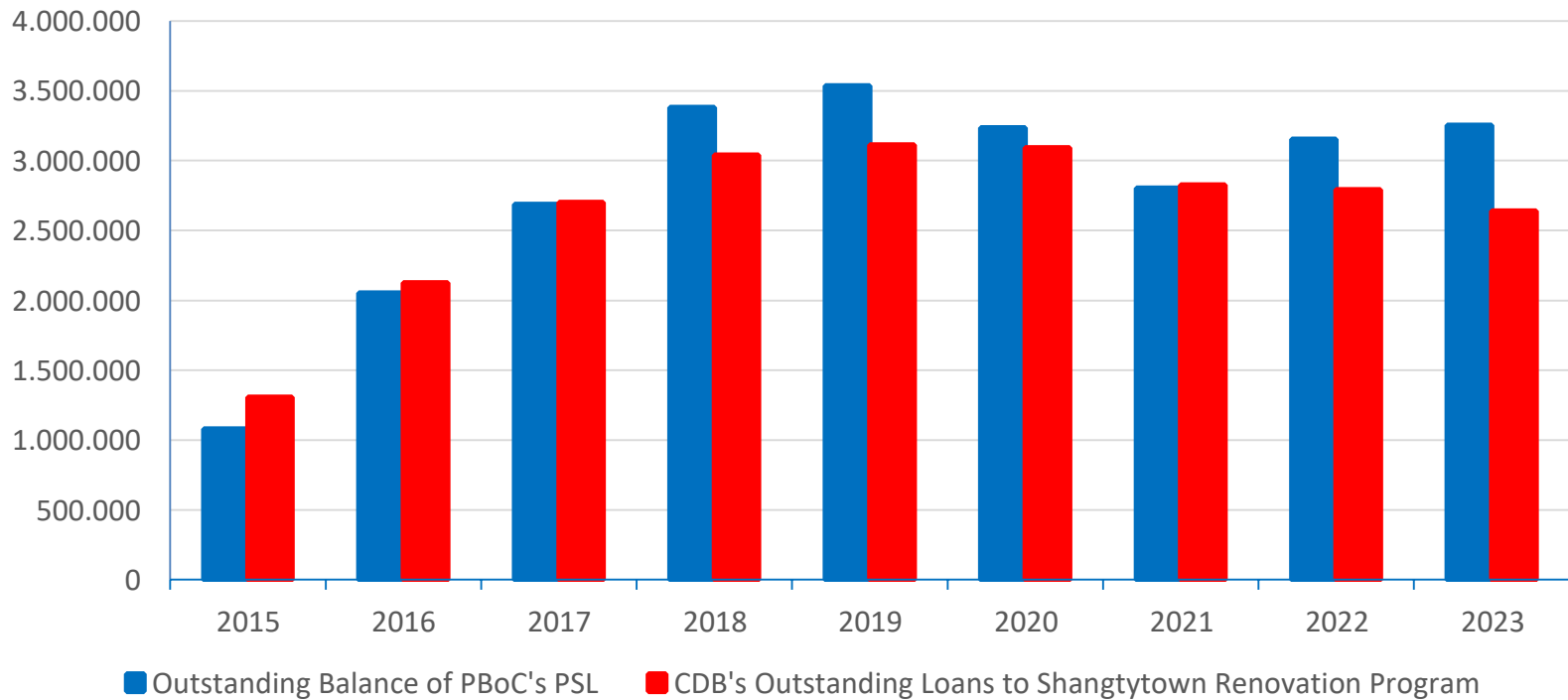
Urban redevelopment program financed by the central bank



I. What's Shantytown Renovation Program

Urban redevelopment program financed by the central bank

PSL and CDB's Shantytown Renovation Loans (in mn RMB)

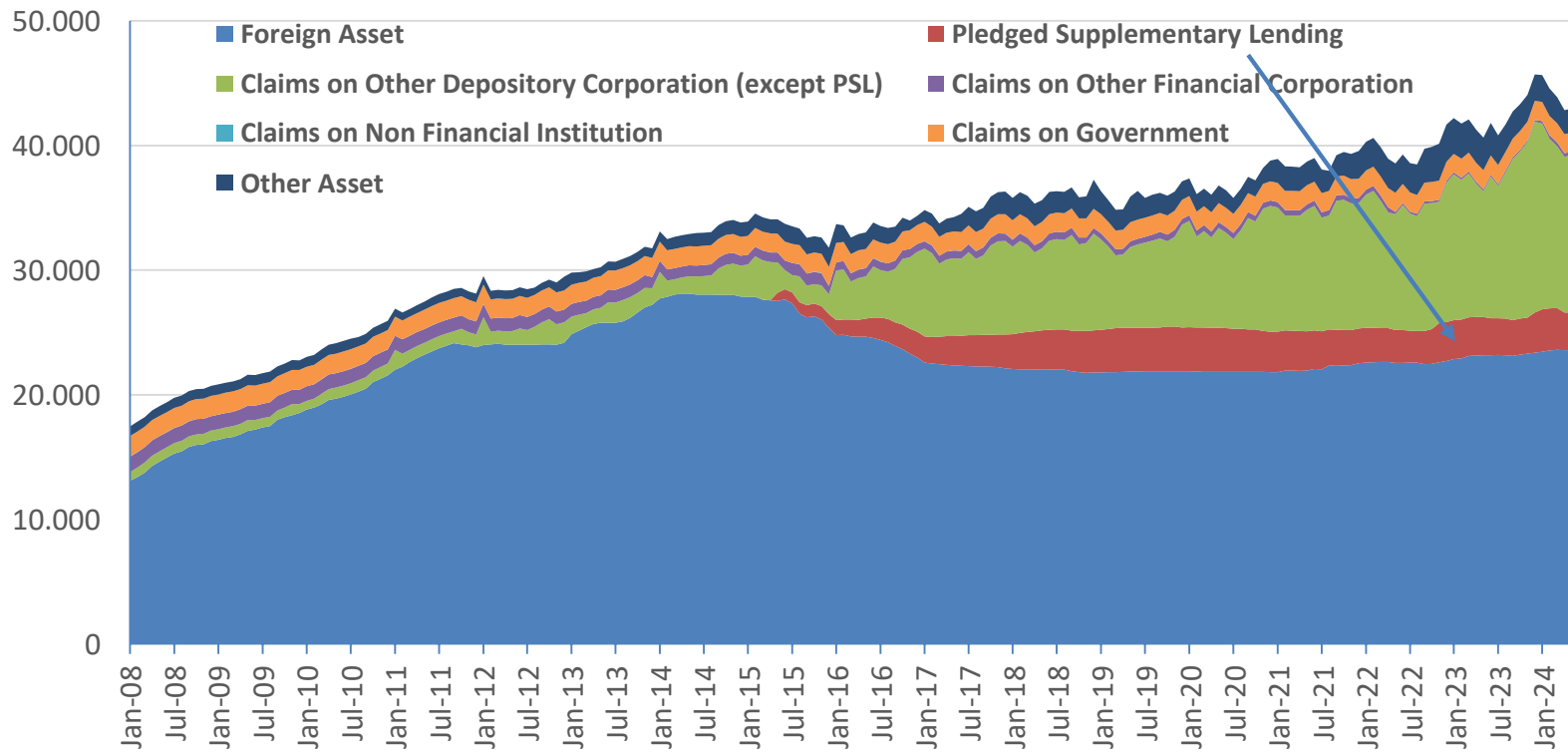


Source: PBoC, CDB

I. What's Shantytown Renovation Program

Urban redevelopment program financed by the central bank

PBoC's Balance Sheet (Assets: in bn RMB)



Source: PBoC

II. The paper' contributions to China's housing policy analysis

The first In-depth quantitative analysis to SRP

- **Originality and uniqueness:** There has been no other in-depth research that focuses on quantitative analysis on the policy effects of SRP by any government or research institutions up to date.
- **Data:** three sets of data (CDB loan data; migration data from China's national census, and housing data from both official publication and private sector) and comprehensive data treatment.
- **Methodology:** difference-in-difference (DID) and panel data analysis.
- **Timing:** The paper provides a timely reference for the ongoing practice of China's housing policy.

II. The paper's contributions to China's housing policy analysis

Findings are counterintuitive and contrary to the prior analysis

- The authors constructively separate Chinese cities into two groups based on flows of CDB loans:
 - In originating cities: housing price ↓, housing supply ↑, inventory ↑;
 - In destination cities: housing price ↑, housing supply ~, inventory ↓;
- **Answer to the puzzle of “more treated but less responses”:** intercity money flow has facilitated household migration from originating cities (usually small and in-land cities) to destination cities (usually provincial capitals and big coastal cities).
- **Dilemma of cash resettlement:** It generates more housing activities (investment and housing starts) in originating cities, but outflow of money facilitates emigration demand. (housing supply ↑; housing demand ↓)

II. The paper's contributions to China's housing policy analysis

Its conclusion may have important policy implications.

- **PSL and CBD loans:** It has been proved as an effective model to boost housing development (and to facilitate intercity migration as an unexpected by-product). But its long-term sustainability is questionable, as this model has caused a fiscal transfer from lower to top-tier cities (from poor to rich).
- **Voucher resettlement vs. cash resettlement:** While the latter was a powerful tool to unlock households from illiquid housing market, the former offers more targeted effects at local housing market, and reduce the spatial variation among cities.
- **Rebalancing welfare-oriented policies vs. efficiency-oriented policies:** Chinese government has launched a new round of housing stimulus measures including expansion of PBoC's PSL and other lending programs, to develop public housing and to reduce excess inventory of commercialized homes. Can it hit two birds with one stone?

III. Thoughts on further research and policy discussions

Evaluation of structural monetary policy (SMP) instruments

- **Aggregate or structural?** By nature, PSL is an instrument of structural monetary policy (SMP) with a macroeconomic impact.
 - As of end of Q1'24, the total outstanding balance of the PBoC's SMP instruments reached RMB 7.54tn, or 17.2% of the PBoC's balance sheet. Among these SMP instruments, PSL is the largest one (7.7% of the PBoC's total assets).

- **Emergency or routine?** Started as emergency lending programs in the Global Financial Crisis and the European Debt Crisis, SMP has become a routine practice of major central banks.
 - Fed: TALF, PDCF, CPFF, MMLF, PMCCF, SMCCF, MSLP, etc.
 - ECB: TLTRO I, II, III, etc.
 - PBoC: PSL and other sector-specific lending facilities

III. Thoughts on further research and policy discussions

But DSL is the PBoC's only meaningful Housing-Related SMP Programs

	Purpose	Borrowers	Total (RMB bn)	Balance as of Q1'24 (RMB bn)	Change over past 6 months (RMB bn)	Interest rate
Pledged Supplementary Lending (PSL)	Shantytown renovation and other public housing	Policy banks (CDB, ADBC and EXIM Bank)	Open-ended	3,370	468	2.25%
Special Lending Program for Developer Relief	M&A of developers	Five asset management companies (AMC)	80	20.9	20.9	1.75%
Rental Housing Loan Program	Purchase of existing homes as rental housing	Big commercial banks	100	2	2	1.75%
Guaranteed Home Delivery Loan Program	Completion of unfinished homes	Big commercial banks	200	8.6	3	0.00%
Re-lending Loan Program for Public Housing	Purchase of existing homes as public housing for rental or sale	Big commercial banks	300	-	-	1.75%

Source: PBoC

III. Thoughts on further research and policy discussions

Why is PSL more effective than other SMP instruments?

Two important factors:

a) The Shantytown program was implemented in an expansionary stage of China's housing cycle, whereas the new programs are adopted during a housing downturn.

b) In both PSL and those new housing-related SMP programs, the PBoC plays the role of "the lender of the last resort (LOLR)". However, the CDB's role is also critical, as it is "the risk-taker of the last resort (RTLRL)" in the Shantytown program, but the same role is missing in the new housing policy programs.

Conclusion: In the downturn of a credit cycle, emergency SMP programs should be structured differently from routine SMP programs; in this case, the role of RTLRL is indispensable for the success of SMP programs. (Example: combination of TALF and TARP in 2007-2009 GFC).

Many Thanks!