Chinese households’ concentration of wealth in real estate is magnifying the danger to the world’s second-largest economy of any property bust, as the nation grapples with the consequences of its record credit surge.

Some 66.1 percent of family assets were in housing in 2013, a national survey of about 28,000 households shows. Mortgage debt as a share of disposable income rose to 30 percent from 18 percent in 2008, according to estimates by Nicholas Lardy at the Peterson Institute for International Economics in Washington.

The buildup raises the stakes for any slide in property prices amid China’s efforts to head off defaults by local governments and developers that propelled a run-up in borrowing that now amounts to more than double the size of the economy, according to Goldman Sachs Group Inc. A hit to household wealth could impair consumer spending, rebuffing policy maker efforts to rebalance the economy toward domestic demand.

“A fall in housing prices could have significant knock-on effects on private consumption,” said Eswar Prasad, a former chief of the International Monetary Fund’s China division and now an economics professor at Cornell University in Ithaca, New York. “Such a hit to private consumption could pose significant macroeconomic risks, both to headline growth and the process of rebalancing growth.”

China’s households piled into real estate in recent years as they sought returns beyond the regulated caps on savings deposits. With the nation’s stock market failing to keep pace with economic growth, property offered an alternative, along with trusts that channeled credit to borrowers outside the official banking system.

Values Rose

Among urban households that own apartments, 75.5 percent of their assets are in real estate, according to Gan Li, director of the Survey and Research Center for China Household Finance in
Chengdu, a body set up by the Southwestern University of Finance and Economics. The center’s 2013 national survey showed that households’ assets rose by 20 percent from 2011, while the value of their residential property holdings increased 26.8 percent.

A bursting housing bubble would cause a “substantial hit to Chinese household wealth” with long-term consequences for consumption, said Gan.

For now, there may be little sign of danger. Home prices in December had the biggest year-on-year gain in 2013, increasing 12 percent, according to SouFun Holdings Ltd., China’s biggest real-estate website owner. At the same time, some cite concern that developers have built more than the economy needs -- with Centaline Property Agency Ltd., China’s biggest real-estate brokerage, detecting oversupply last year in cities other than the nation’s four biggest.

**Looming Risk**

Liu Li-Gang, chief Greater China economist at Australia & New Zealand Banking Group Ltd., said today that risks may mount in coming years as China opens its capital account, giving property owners in major cities such as Beijing the opportunity to “rush to the exit,” shifting their money overseas if they think prices aren’t sustainable. He spoke to Bloomberg Television in Hong Kong.

The survey by Gan’s center indicated that about 90 percent of households in the world’s most populous nation already own homes.

A separate survey of 30 developers in second-tier and third-tier cities conducted by Standard Chartered Plc showed that while the group anticipated continued land-price gains in coming months, they are finding it harder to get financing. “A record-high 12 respondents said they had heard of cases of developers having problems paying for land,” the bank, which began the surveys in 2010, said in a Jan. 27 report.

**Swelling Debt**

China’s policy makers have attempted to rein in the unprecedented credit boom they unleashed in 2008-2009 amid the global financial crisis, as risk mounted that some of the loans would go bad. Goldman Sachs analysts estimated in a July report that the nation’s total debt-to-gross domestic product ratio jumped almost 60 percentage points since the crisis, to almost 210 percent.

Whether triggered by a cut-off in financing or a collapse in demand, any bust in the housing market would have an economic effect that’s difficult to calculate, given China hasn’t been through such a crisis in recent history.
“A decline in home prices will definitely have a negative impact on consumption -- but since we’ve never had a sustained home-price decline in China, any estimate is quite judgmental,” said Ding Shuang, senior China economist at Citigroup Inc. in Hong Kong.

**Cash Buffer**

Higher down payments for homes -- typically 30 percent of the purchase price -- and the lack of mortgage securitization reduce risks of the kind of financial panic and recession that the U.S. experienced last decade. About 30 percent of Chinese buyers pay all cash, estimates Liu Yuan, a Shanghai-based researcher at Centaline.

Hong Kong’s experience may be an example for China, said Zhu Haibin, chief China economist at JPMorgan Chase & Co. Mortgage defaults failed to exceed 3 percent even as the city’s home prices dropped 70 percent from 1997 to 2004, Zhu said.

“There is no question that housing is the most important part of Chinese household assets,” said Zhu, who’s based in Hong Kong. Even so, Chinese household debt is still “relatively low” he said.

**‘Wealth Effect’**

One potential channel for affecting the economy is through the “wealth effect,” where households tighten their budgets after seeing a decline in their net assets due to a slide in the value of property they hold.

“A sharp decline in house prices would have a perceptible negative effect on household private consumption expenditure, even if it did not lead to substantial stress in the financial sector,” said Washington-based Lardy, who has studied China’s economy for more than three decades.

Any hit to consumption would impair efforts by President Xi Jinping and Premier Li Keqiang to step up the role of spending in the domestic economy and reduce reliance on exports. Li said in an October speech that expanding domestic demand is the “most important” key to adjusting the structure of the world’s second-largest economy.

A tradition of borrowing from family and friends could exacerbate strains, according to Gan, with interest rates ranging as high as 36 percent and 40 percent of Chinese households engaged in informal borrowing or loans.

“You can’t sell your house to pay back -- that’s going to create not only economic problems but also social problems as well,” Gan said. “Friends become enemies.”

To contact Bloomberg News staff for this story: Xiaoqing Pi in Beijing at xpi1@bloomberg.net