

# Housing and the Housing Market in China at the Turn of the Century

*GU Yun-chang*

Vice-chairman, China Real Estate Association  
People's Republic of China

## 1. Housing Development in China

### 1.1 Annual housing production of one square metre per capita

Housing construction in China has accelerated since the implementation of the reform and opening policy in 1979. The annual housing production in both urban and rural areas for the past two years has reached 1.1 to 1.2 billion square metres, or one square metre per capita. For 1998, a historic amount of 476 million square metres of new housing area has been developed in cities and towns across the nation (including some 660 cities and 18 000 towns). Residents of non-agricultural sectors have built 360 million square metres of housing.

For fifty years since the founding of the country, an additional 4.04 billion square metres of housing area have been developed in cities and towns (not including the figures of 1999), of which 3.51 billion square metres are developed in the two decades between 1979 and 1998, which is 6.6 times the production of the preceding twenty years. Over two thirds of the existing urban housing is developed after the founding of the People's Republic of China.

### 1.2 Per capita residential building area for the urban population close to 20 square metres

According to statistics, the average living area (net area of bedroom) of the urban population has increased from 3.6 square metres per capita in 1978 to 9.3 square metres at the end of 1998. In terms of per capita building area, the figure is 19 square metres at the end of 1998 and will reach 20 square metres by the end of this year. Incidentally, the per capita building area for the rural population is 25 square metres.

### 1.3 Seventy per cent of urban households live in self-contained flats

Urban flats (self-contained housing units with own kitchen and toilet facilities) account for 70 per cent of the current total housing production compared with 24 per cent in 1985. The average building area of such flat in 1985 is 56 square metres. **In recent years, most of such newly constructed housing units have an average building area of over 80 square metres.**

### 1.4 Over sixty per cent of urban households have their own homes

The home ownership rate in cities and towns in 1985 is less than 17 per cent. In the nineties, with the progress of the housing system reform in cities and towns, more and more residents chose to buy new housing units or the public rental units in which they have been living. The rate of home ownership has risen to over 60 per cent at the moment. A pluralistic housing market with self-ownership as the mainstay has thus evolved.

## 2. The Current Housing Market

### 2.1 Extensive housing investment and construction with 40 per cent of the total housing production for commercial purposes.

For both 1996 and 1997, the annual production of urban housing exceeds 300 million square metres. The figure for 1998 is some 360 million square metres, the largest total output in the world. China also ranks first in the percentage of her housing investment in the GDP and the number of flats produced per 1,000 persons per annum. For instance, the urban and rural housing investment in 1996 and 1997 amounts to over 7.5 per cent of the GDP (urban housing investment accounts for more than 4 per cent of the GDP). In other countries, the same is 3-6 per cent in general. The urban housing production is **13.5 housing units per 1 000 persons per annum** (calculated at an average building area of 80 square metres per unit). The figure is no more than 10 in other countries.

In 1997, 125 million square metres of commercial housing, or 40 per cent of the 312 million square metres of total housing output of the year, were built. Of the remainder, about 40 per cent were built by organizations and about 20 per cent were personal projects. This means that less than 40 per cent of the total output of new housing units can be available in the property market, with some commercial units belonging to commissioned projects and re-provisioning developments.

## **2.2 Commercial housing accounts for 80 per cent of the property market; while the overall supply of offices and commercial properties obviously exceeds demand.**

In 1997, 77.79 million square metres of commercial housing were put on sale, accounting for 84.8 per cent of the total 91.71 million square metres from all categories of commercial developments. The actual revenue derived from the sale of commercial housing was 141.7 billion RMB, or 76.6 per cent of the total sale of all commercial developments.

Since 1992, investment and the scale of construction in respect of offices and commercial properties have been augmented across the country. It is obvious that supply has exceeded demand in major coastal cities. For example, the nationwide vacancy in terms of area at the end of 1997 has increased by 50 per cent compared with the previous year. The area of unoccupied commercial and business premises has increased by 18 per cent for the same period.

## **2.3 The rate of commercial housing purchase by individuals increases each year.**

The rates of commercial housing purchase by individuals against the total sale area for 1996, 1997 and 1998 are 53 per cent, 64 per cent and 73.7 per cent respectively. Nevertheless, individual purchase of commercial housing is less than one-fourth of the total urban housing area built of the year (300 to 350 million square metres) is purchased by individuals.

## **2.4 Prices of commercial housing have been relatively stable in the last few years in spite of major geographical variances.**

Average prices of new urban commercial housing are 1,667 RMB per square metre in 1996, 1,822 RMB per square metre in 1997, and 2,002 RMB per square metre in 1998, representing a premium of 3.3 per cent, 9.3 per cent and 9.8 per cent than the previous year. Property prices in the first half of 1999 have a slight downturn compared with the same period a year before. The situation varies depending on the type of property. According to a survey, prices in Beijing have been relatively steady for ordinary accommodations, moving downward for apartments and upward for villas since the first quarter of 1997.

According to statistics, the nationwide average price of commercial housing sold to individuals is 1,662.9 RMB per square metre in 1997 though it varies greatly at different locations. Shenzhen fetches the highest price at 5,234.1 RMB per square metre and is followed by Beijing (4,116.1 RMB per square metre), Shanghai (2,593.3 RMB per square metre), and Tianjin (2,087.8 RMB per square metre). Jiangxi asks for the lowest at 686.3 RMB per square metre while Guizhou, Anhui and Henan could do at the range of 860-880 RMB per square metre.

## **2.5 Vacant area of commercial housing increases each year**

Vacant area of commercial housing nationwide is 46.62 million square metres in 1996, 52.02 million square metres in 1997 and 61.46 million square metres in 1998. The average rate of vacancy over annual area output of commercial housing in these three years is 16 per cent. Incidentally, the rate of vacancy over total area of the current urban housing stock is at around 1 per cent.

The bulk of vacant premises are located around the coastal cities in the south. In 1998, the six provinces/cities, which include Guangdong, Shanghai, Jiangsu, Jiejiang, Hainan and Liaoning, claim over 60 per cent of the total vacant area of commercial housing in the country.

# **3. Greater Government Control over the Housing Market**

## **3.1 Central government's ambition to make housing development a new front of economic growth and consumption.**

China has managed to maintain an appropriate high rate of economic growth in the wake of the Asia financial turmoil by putting its emphasis on boosting internal demand and activating the domestic market. Housing construction can help boost the economy through investment and consumption. Moreover, with vast potential needs and an underlying force of a new business, the housing industry is evidently gaining importance and momentum in the national economy. Given the current slackened economic atmosphere in China, the development of the housing industry is particularly significant in the advancement and betterment of the consumption and property structures and in the growth of the economy.

How can housing construction be a new front of economic growth? The consensus is, first, further expansion of the scale of housing construction and push the economic growth by means of investment. Second, more technology in housing construction. To attract purchasers by quality and high class housing, to stimulate consumption by increasing the housing investment.

## **3.2 The greatest potential for more extensive scale of housing construction is found in**

### **cities and towns. The primary problem, however, is the ineffective housing demand.**

This can be analysed on three fronts:-

First, the demand and supply relationship. The current urban housing market is different from those in the 1970s and 1980s, or in 1992 and 1993, when supply fell behind demand. In a market economy, China faces with a high proportion of housing investment in GDP and the housing production per 1 000 persons, in addition to an aggravated overstock of commercial housing. How much more can the urban housing market of China accommodate?

Second, a problem of institution. A “welfare housing system” has been in practice in the cities and towns of China. The housing needs of residents and employees are met through allocation in kind by the government or working units of the enterprises. After twenty years of reform and opening, the government and working units have been exhausted in the development of housing. Both the Government and enterprises cannot do much financially in further investment in housing construction.

Third, affordability of an individual. From the foregoing analysis, it can be seen that to make housing construction a new front of economic growth, emphasis should be put on stimulating people’s housing investment and consumption. How about the power of purchase of our people? On the one hand, rents are extremely low under the welfare housing system. It makes more sense to rent than to buy. Conceptually people do not think that they have the “power” to purchase. On the another hand, property prices in the large and medium-sized cities are high. They are six or even ten times the income level. The general wage earners simply do not have the economic ability to buy.

### **3.3 The second problem of further development of urban housing is inadequate effective housing supply.**

In spite of the scale of housing construction, the housing quality in China (in terms of words, functions, environment and management) is low. The ranges and positioning of housing products also cannot meet people’s increasing housing demands, in particular the various “favours” of individual purchasers. As a result, the desire to buy a new house cannot be stimulated. The underlying issue is the poor quality of China’s housing industry. There is a serious problem of “three lows” : low productivity, low technology content and low marketing ability.

### **3.4 Key initiatives taken in the government macro-economic control.**

To address to problems of the lack of effective demand and supply in the urban housing market, the central government and the relevant departments have in the past one year taken a number of major policies and initiatives to regulate and influence the housing market with a “visible hand”. These key initiatives include :

- A national conference on housing reform was held in June 1998, which led to the release of a document entitled “Further Deepening the Reform of the Urban and Rural Housing Systems and Speeding up the Housing Construction” in July 1998. The document set forth a guiding principle to make the housing industry a new front of economic growth, and at the same time put forward key points to deepen the reform.
- The Ministry of Construction held a national conference on housing development in November 1998. A main concern of the conference is to speed up the modernization of the housing industry and to improve housing quality. To this end, the document entitled “Views on the Promotion of Housing Industrialization and Improvement of Housing Quality” was released.
- The implementation of the Affordable Housing Scheme. Three batches of housing projects would be carried out under the Affordable Housing Scheme in 1998. The scale of the overall construction is 212 million square metres, and the total investment is 170.3 billion RMB. The construction and investment project under the Affordable Housing Scheme 1999 involves a total area of 244 million square metres (with 109 million square metres carried forward from the previous year) and an investment of 190.1 billion RMB by the end of the year.
- In May 1998, the People’s Bank of China released the “Guidelines on the Management of Personal Housing Mortgage Loans”. In April 1999, the State Council promulgated the “Housing Contribution Fund Management Ordinance”. The main purposes are to define the management and use of housing contribution funds to enable a more speedy development of the nation’s housing finances and to make housing construction a new front of economic growth.
- In July 1999, documents on the development of a secondary housing market and the adjustment of taxation policies with respect to the housing market were issued by the Ministry of Finance and the Ministry of Construction to activate the property market.

### 3.5 Letting people buy their own houses.

Over the year, a series of policies have been implemented on housing construction and the housing market, which can be summarised as enhancement of effective demand, improvement of effective supply and activation of housing flow. In a nutshell, it is to : “Let people buy their own houses.” (a remark by Premier Zhu Rongji at a press conference during the 1998 National People’s Conference.) The first point is to appeal to people to “buy houses on their own” instead of following the practice of relying on their working units to buy or build the houses and then allocate to them. The second point is to “let most of the people” but not just a handful of wealthy minority to buy their own houses.

How to “let most of the people buy their own houses”? This can be answered in the four focus points in the new initiatives:

**First, reform of the housing allocation system.** Allocation of housing is terminated and replaced with financial assistance. Housing allocation in kind has been terminated in the cities and towns since the end of 1998. Units are no longer allowed to buy or build houses and allocate them to residents or employees. The latter have to pay for their own houses instead. In cities and towns where property prices are four times above the wage level, units will pay housing subsidy to employees who do not have their houses or are in need of housing.

**Second, establishment of a new housing supply system.** Appropriate housing supply policies are adopted for families of different income levels with stress on the development of affordable housing. Families of the lowest income level are to be provided with low rental housing either by the government or relevant units. Low and middle income families should buy affordable housing. High income families should buy or rent commercial housing in the open market. Affordable housing is a kind of commercial housing developed with government assistance under a policy of land grant and profit control. An important purpose of such stress on the development of affordable housing is to curb high property prices so as to make housing more affordable to the general wages earners.

**Third, rationalization of the housing market system.** The emphasis is on opening up and regulating the housing secondary market. Residents are allowed and encouraged to sell their public or affordable housing units in the market. Concessionary tax duties (such as transaction tax waivers and 50 per cent reduction in stamp duties) can help flat owners trade in their properties for bigger or newer ones. This will boost housing consumption and investment.

**Fourth, development of housing finances.** The emphasis is on developing loan packages by combining the strategic housing provident funds and the commercial mortgages of banking institutions. With lower interest rates, longer lending periods and improved housing mortgage services, residents can realise their dreams of owning their houses by making use of future money.

## 4. Analysis of the Prospects of the Housing Market

### 4.1 The housing industry of China is faced with great changes at the turn of the century.

We have observed hitherto that apart from a responsibility to provide sufficient housing for the society, the housing industry of China is given the onus to spearhead economic growth. Meanwhile, unprecedented changes are taking place in the industry. Specifically, there are three categories of changes.

**First, system change. The urban housing system is changing from allocation in kind towards allocation in money.** This is a historic change that signals the demise of the “Welfare housing system” that has been in existence for half a century in China. The establishment of a new system of urban housing will have profound impact on the country’s development of housing in the next century.

**Second, orientation change. The housing market is changing from a sellers’ market to a buyers’ market.** In other words, the state of demand exceeding supply in the past has given way to a state of equilibrium or of supply exceeding demand. Consumers/consumptions have taken the place of developers/investments as the determining force of the market. Buyers’ market took shape in the coastal regions such as Guangdong and Shanghai around 1996. The same occurred in inland cities in the last few years. Such orientation change is of paramount importance to the development of the housing industry.

**Third, structural change. The urban housing of China is no longer in scarcity. The prevalent of settlement type of housing products has given way to comfort.** During the 80s, the requirement housing had been “livable and partitionable” and the average size of housing unit was 50-55 square metres. Currently, the requirements have become “convenient, comfortable, and with good environment”. The most popular housing units in the market are two-bedroom units of around 80 square metres and three-bedroom units of around 120 square metres. Moreover, people are increasingly paying more

attention to internal facilities and outdoor environment.

#### **4.2 Enormous opportunities, potential and room for development in the market**

The prominent characteristics of residential property include substantial market demand and high relevance that attract investment, stimulate consumption and boost employment. At a time when the economy slows down under the macro-economic control, residential property is urged to develop at a quicker pace. The central government has introduced a series of incentives and concessionary measures to stimulate housing investment and consumption, **thus providing an unprecedented opportunity for the development of the housing market in China.**

“Potential”, on the one hand, implies that the housing levels of urban dwellers in China are far lower than their counterparts in the developed and the developing countries. The objective of self-contained housing for each household has not yet been completely achieved, not to mention a room for each family member. The consumption pattern of urban dwellers indicates that the percentage of food consumption in overall expenditure has decreased from 52.9 per cent in 1992 to 46.4 per cent in 1997. They are now **in a dramatic upgrade period to satisfy their “housing” and “transportation” needs.** During this period, they would spend 60 per cent of their saved household expenditure on “clothing”, “food” and “consumption” on housing. As such, it is possible that their enormous potential housing demand may turn into actual need. On the other hand, it also means that **China is in the process of accelerated urbanization.**

In 1998, 30 per cent of China’s population lived in towns and cities. Currently, 70 to 80 millions of peasants have become a “mobility force”, as either investors or workers. Most of them do not have proper urban accommodation. If urbanization advances at a yearly rate of 1 per cent, there would be an addition of 120 million city dwellers a year. They will constitute a considerable source of demand in the future housing market.

“Enormous room for development” means that the “young” housing market in China not only has much room for development at the primary market level, but its existing housing stock also allows the formation and further development of a secondary market. Moreover, the market of agency service is at its start and the heyday of the property management market is yet to arrive.

#### **4.3 The speed of housing development hinges on the progress of system innovation.**

System innovation refers to the reform and improvement of the housing system. Under the old system, the main buyers in the housing market were corporations (various administration and work units). Take Beijing as an example. Before 1997, 90 per cent of the commercial housing in the market were bought by corporations. In 1998, it was 80 per cent. In Guangzhou and Shanghai, pioneers of the housing reform, corporation purchase only accounted for 20 per cent or less in the last two years. Over 80 per cent of the properties were purchased by individuals. Under the new system, residents in big and medium cities who are not adequately housed usually can receive housing allowance from their relevant units. Low and middle income families can buy affordable housing of passable quality at a reasonable price. Through the open housing secondary market, people can trade up their small and old flats for larger and newer ones. Employee purchasers not only can draw on their accumulated housing contribution funds; they can also apply for mortgage loans provided by the contribution fund management centre and banks. One major purpose of establishing the new housing system is to help maintain the original amount of investment in housing budgeted by the government and the relevant units, and at the same time explore the potential housing consumption of individuals. In a word, **housing development finds its strength in mobilizing the positiveness of the government, various units and individuals, in particular the positiveness of the residents in housing consumption.**

That system innovation can bring about housing development is illustrated by the condition of Shanghai. Real estate transactions in Shanghai register an exceedingly high increase in the first half of 1999. Volume of advance sale rises by 64 per cent in comparison with the same period a year before and is 7.9 times of the 1996 figure. The volume of rise by 84 per cent over the year before, and is 5.5 times of the 1996 figure. In Changdu (Sichuen), Qingdao (Shandong), and Nantong (Jiangsu), where the housing reform is carried out at a quicker pace and housing secondary market is developed at an early time, housing transactions also register a drastic increase.

#### **4.4 The development and share of market depend on the intensity of technology innovation.**

Housing development in China has moved from quantity-oriented to attaching importance to both quantity and quality. People’s ever-developing requirements on housing quality demand that new breeds of housing products be designed. Those small housing units built in the 80s are found to be quite contrived in functional layout. Their kitchenettes and small living rooms are especially out of place in modern living. To encourage spending on housing, there is also a need to develop new housing products to stimulate purchase. New generations of housing products have to be supported by new technology.

**Innovative technology to achieve housing product upgrade, to develop reasonably priced, marketable quality products and to secure future market share.** Quality products and brand names are emerging in the housing market of China, though not many.

Real estate enterprises in China are growing in number. In 1986, there were only 1 704 such enterprises. In 1995, the number rose to 33 428. The transition now is towards excellence, which is to be achieved through fierce market competition, natural selection of the elite, and merging and taking-over of enterprises. Enterprises are the focal points of technological innovation. In the future, only those who are powerful in technological innovation can take the lion share of the market. Those who do not will be edged out.

#### **4.5 The housing industry in China will enjoy a heyday of a further two to three decades.**

The housing industry of China has experienced 20 years' rapid development since the country's reform and opening up. With fast economic growth at a suitable pace, the reform of the urban housing system, the accelerated urbanization and the ever-increasing housing needs of urban population, it can be expected that the housing industry in China will continue to stay robust for at least a further twenty, or even thirty years.

Then, what the housing market of China, especially at the turn of the new century, will be? The following are the predictions:-

**I. The supply and demand.** Overall speaking, supply will be greater than demand in the country, particularly in the coastal cities. In the central and western regions, the condition will be stable in most of the cities. With more affordable housing available in the market, this situation is likely to continue. Owing to the dwindling of the supply of housing by units (which is 40 per cent of the annual housing production at the moment), housing purchase by salary earners will have an obvious growth. Hence, a suitable control of the total production will narrow the discrepancy between the demand and supply of commercial housing.

It has been observed that even in cities with considerable housing stock (Shanghai, for example), there is no lack of warm received sites and purchasers who are unable to locate suitable housing for the time being. This is well worth the attention of the government and the developers. While putting the overall production in good control, they should also attend to the variety of housing needs. Properties of different grades, classes, specifications, prices and at different locations should be developed for different strata of consumers.

**II. Price trend.** In a market where supply exceeds demand, property prices are normally stable or tend to fall, as evident in cities like Shanghai and Guangzhou. Extensive development of affordable housing will also lead to an overall price drop, as the "premium" has to be trimmed from the selling prices of this category of flats (no land cost, no exorbitant charges, less developing profit, etc). This has been well reflected in the sale of housing in the first half of 1999. Compared with the same period a year ago, sale of commercial housing has shown an increase of 9.8 per cent in floor area but a decrease of 1.7 per cent in sale revenue. It can be predicted that the overall level of housing prices in the next one or two years will not rise but may fall. This can be construed as a "rectification" of the high property prices (in relation to income) and the irrational pricing components in the past. However, such "rectification" will not be conspicuous in medium and small cities and towns, where the housing prices are not high in the first place, and the "premium" in the property is far from big price in the second.

In the long run, however, in a situation where the demand is met by or slightly exceeds the supply, housing prices will follow the economic and growth inflation and move up steadily. Nevertheless, it is unlikely that a 15-20 per cent average annual increase of the last twenty years will repeat.

**III. The relationship between sale and rent.** In order to speed up economic growth, the housing reform policy put forward by the central government stipulates that all housing units built under the affordable housing scheme are for sale but not for rent. All who can afford are encouraged to purchase their homes. Opening up of the housing secondary market is emphasized to stimulate property transactions. This implies that the privatization of housing is being enforced in cities.

However, while the emphasis is on the sales market, the potential of the rental market should not be underestimated. The housing problem of the tens of millions of "mobility force" in China has not been given due or the slightest attention. They will surely be part of the consumption group of the urban housing market in the future. Their housing problem cannot be solved solely through purchase. It is more likely that the main solution lies in "renting". The relevant departments of the central government are giving further consideration to lowering rental duty and formulating policies to regulate the property rental market. It is believed that in the future the housing market will be one with a balanced combination of frequent rental and sale activities.

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