

A study of Real Estate in China



An economic investigation proposed by M. BOMSEL Olivier to
a group of students of Mines Paristech

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I. Introduction

The purpose of this study is to explore the economic rationale underlying the huge real estate programs launched countrywide by the Chinese central and local authorities. It is also to observe how the Chinese institutions and organizations adapt in order to monitor such an ambitious process. The massive access of each Chinese family to an owned house, the combination of the demographic, industrial, financing and environmental constraints associated with this goal, the timeframe of this policy, make it a very unique historical challenge; and an economic process worth to be studied both by academics and business executives.

During a two-week period in February 2013, a group of eight second-year students of MINES ParisTech has investigated the Chinese real estate policy. Although two of them had already got a Chinese experience, for the others the investigation has been a total discovery.

On the Chinese side, the trip has been organized thanks to Pr. Zhang Bin of the University of Suzhou. He has received a strong support from the government of the Anhui province who has been quite helpful in making contacts in Hefei and Shanghai. And has given all the team a very warm welcome for which we are all grateful.

The report summarizes the main findings of the trip. The first section sums up the main steps of the Chinese housing policy. The second describes the local environment and the projects visited during the trip in Shanghai, Suzhou and Hefei. The appendices present the program of the visit and a research study carried out by the Shanghai center for real estate development.

II. Overview of real estate regulations in China

A. Short historical review

Back in the days of imperial China, there was no right of property. The land belonged to the emperor, and the landlords paid taxes in order to use the land. The individual had no private property rights. Although the system evolved with the different dynasties, it remained that the emperor was the owner of the land and that people couldn't own their land.

After a brief appearance of the western notion of property right at the end of the empire, the communists abolished the institution of property. The land was first confiscated and then distributed to the peasants. Nevertheless all the resources were soon collectivized and the Communist Party created communes in order to administrate them. Eventually this system failed and after the troubled times of the Cultural Revolution, the policy changed with Deng Xiaoping's government.

With the 1982 constitution, two forms of ownership were established: state ownership and collective ownership. The aim of Deng Xiaoping's policy was to favor the economic development without abolishing the system of state ownership.

Between 1980 and 1998 the system of urban housing had the followings characteristics:

- It was handled by the State
- Houses were supplied as a compensation in kind
- The rents were very low and heavily subsidized

The production or administrative departments (usually called "danwei") allocated housing to workers according to their skills or merits. However this system faced many weaknesses. Among others, there was no balance between demand and supply; the heavy weight of subsidies was a burden for the state's budget. For example in 1978 the average renting price was 0,13 Yuan/m² per month. Moreover the allotment was unfair amongst departments, for wealthy departments had more housings than poor ones. Also, public companies had more housings and their quality was usually better.

In 1998, the system changed. A reform was enacted in order to speed up the construction of housings. In 1998 on July the 3rd, the Chinese Welfare Housing distribution system changed. The allotment of housings wasn't done in kind anymore but in money. Thus the real estate market was activated.

In 2003 the market was thriving. Not only social housings were built – houses at affordable prices for the poorest people - but also commercial housings. In 2005 the central government started to enforce regulations on the real estate market to control the prices because of their soaring this year.

In 2004, a new amendment stated that: "The lawful private property of citizens shall be inviolable. The country shall protect in accordance with law citizens' private property rights and

inheritance rights. The country may, as necessitated by public interest, expropriate or requisition citizen's private property and pay compensation therefore." Thus it introduced a new fundamental right.

In 2007, a law was passed that gave for the first time the interests of private investors the same protection as a public investor's. Thanks to this law, ownerships rights are protected if they do not harm public interest.

To summarize, there are now three kinds of property: state, collective and private. However, as land still remains to the State, people have to pay for a land-use right. The usufructuary right enables private investors to possess, utilize and obtain profits from the land. For example they can build and sell apartments. Transfers are however limited and regulation is rather blurry. According to the law, the purchaser has only a use right for 40 to 70 years (it depends on the purpose of the construction: residential, industrial, tourism...), and any change must first meet the approval of the state.

This law also defines what a security right is. Holders of security rights have priority if a debtor defaults on his obligation. This law offers a better supervision of the access to property thanks to a registration system. However there is not yet a unified procedure.

To conclude, to purchase a housing, two rights are needed:

- The right to use the land
- The property right

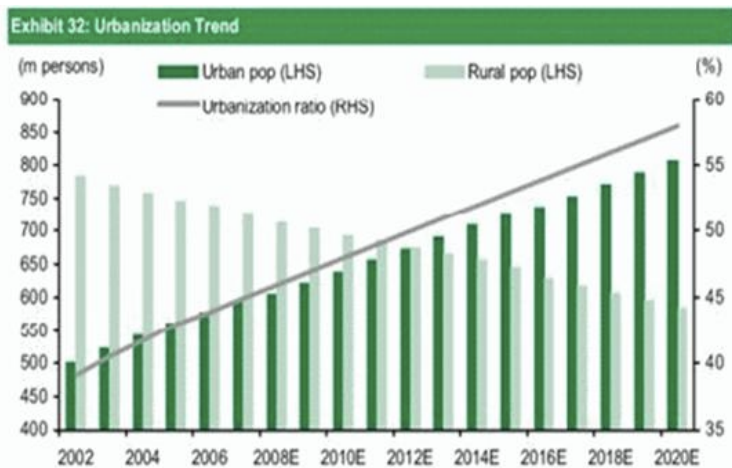
The land occupation right can last up to 70 years. Since this law wasn't established 70 years ago, nobody knows what will happen when this time is elapsed.

B. Today's regulation

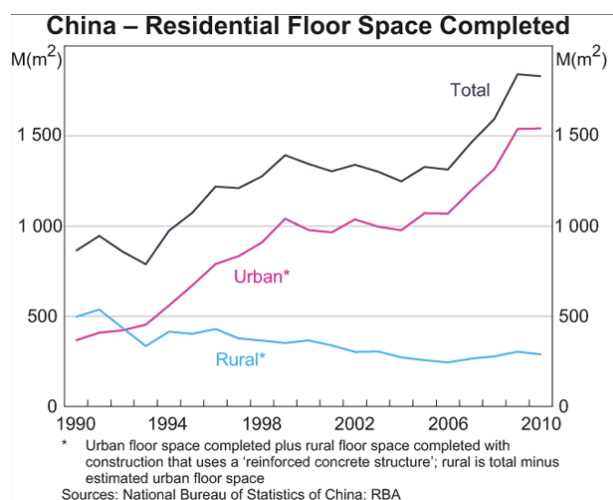
In the recent times, two important factors drive the real estate market: demand and policy. Government policy has caused several actions in the real estate market that have changed its development path. Such policy is designed and issued by the central government and enforced by the local authorities.

Various objectives drive this policy.

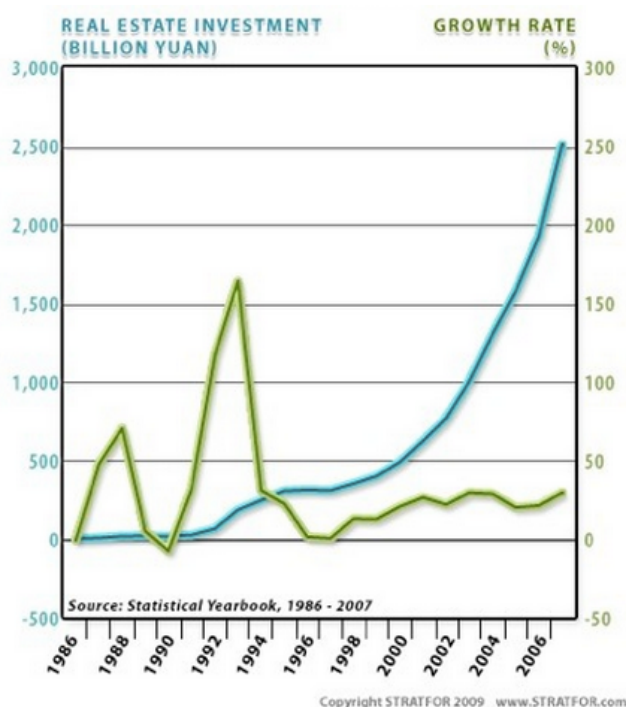
The first one is urbanization. Today, the urban population has reached 50% of the total population, and is forecasted to be 60% by 2020. Not only people from countryside but also people from small and middle cities are moving to large cities. It is forecasted that from 2010 to 2020, 19 million rural residents per year will become new urban residents. Therefore, a huge demand needs to be satisfied. To give some figures, if each person needs 20m² to live, then China has to build 380 million m² per year in cities. Therefore in 2011-2012, 35 millions houses were built, and it is planed that 50 other millions will be built by 2015 so that at the end of the year, 25% of urban habitants will have their accommodation.



Source: BNP Parisbas estimates



The second is the tension between demand and supply. With the growing demand and the increase in land value resulting from the urban extension (price for land superior to 15 millions Yuan per hectare in 2010), real estate is seen as the best investment against inflation. Indeed investment for RE was evaluated at more than 300 billions Yuan in 2012, and 260 billions these past 3 years.

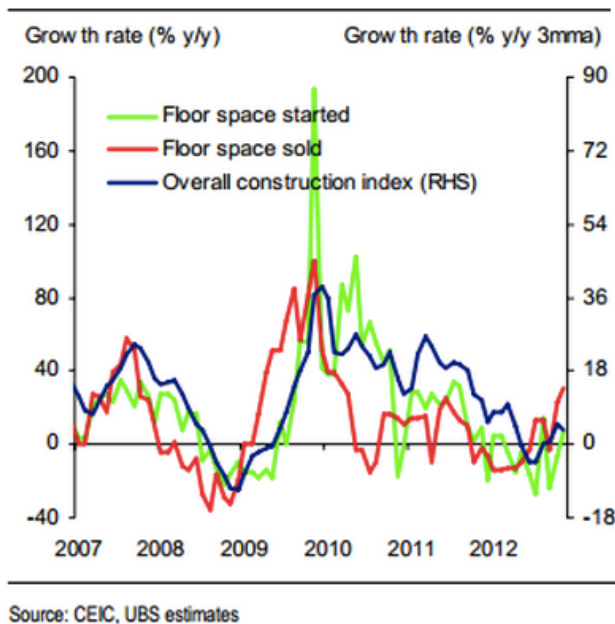


Therefore the real estate market is subject to strong speculation. And as the local governments sell the land by auction to the developers, they can also participate in the speculation.

Last but not least, most Chinese individuals would prefer to own a house rather than to rent one. The withdrawal of the State from the social sphere creates a need for individual social

guarantee. The owning of house is seen as a safety capital ensuring the survival of the individual in the market economy. In order to help average income workers to purchase a house, the government has set up a low level of cash payment (10 to 15%) and a wide access to cheap loans (interest rate of 4,76% today, 3,6% in 2009). These loans are subsidized through fixed fees collected on wages and social expenditures.

However, the consequence of the soar of housing prices is that many people still cannot afford to purchase any. In order to stabilize the prices, the government had to intervene. The first attempt was to raise the interest rates, but it resulted in a strong recession of the market threatening its dynamic balance.



Therefore, since 2010, the government has introduced more targeted measures in order to limit speculation:

- No more than 2 houses per native family, 1 for family from outside the city.
- Limits on mortgages:
 - o Interest rate: a 1.5 times higher one in the secondary market. But control for a not too high rate so that it does not become too hard for not rich people.
 - o Personal contribution: 10% to 30% for the 1st housing, 50% in the secondary market (help preventing speculations).
- Housing provident funds loan (with a lower interest rate)
- Taxes:
 - o Higher if you sell out your house less than 5 years before buying
 - o Tax for inheritance of property: 3% of its value at the time of the reception (The government is trying to raise this tax at the present time)
 - o In Shanghai, local tax on real estate (different policy): 0,6% of the 2nd house transaction price every year if the area is superior to 60m²/person. There are plans to establish this tax in other cities.

It is still too early to assess the impact of these rules, but the prices in 2012 have remained quite stable.

Besides these regulations, the Government is involved in various programs aiming at selling houses at affordable price for low-income workers. The general principles and the modalities of such programs are described in detail in Appendix 2. Some local examples will also be described in the following section.

III. Local markets

We will talk here about the situation of the three cities we have been to during our journey: Shanghai, Soochow and Hefei; and we will try to see if there are or aren't some regulations specific to the province or the municipality. We will give as examples the projects we visited in these cities.

A. Shanghai

- **Situation**

Population

24 million people now live in Shanghai, making it the densest city in China. This population has increased by 50 % during the last ten years. This phenomenon is due to a high rate of immigration from the West of the country. In fact 10 million out of the 24 million inhabitants come from immigration.

Real estate market

This exodus has increased the demand for housing and stimulated the supply, therefore the growth of the real estate sector. It has also led to higher prices on the market and to speculation.

Moreover, Chinese people prefer to own their houses instead of renting them. This cultural feature has also fed the growth of RE. Finally, since 2008, with the economic crisis, investments in industry have decreased and have been reoriented towards the real estate sector, considered less risky.

Thus the real estate sector is now in **full expansion**. In 2012, the investment in the real estate sector reached 240 billion Yuan, leading to a 9.7% growth rate compared to 2011.

The average price for an apartment is 22.000 Yuan/m² for newly built houses on the primary market and 17.000 Yuan/m² for old houses on the secondary market. These prices are rather steady. They only increased by 0.3% from 2011 to 2012.

- **Policy**

The real estate market in Shanghai, as in the rest of China, has known a **deep change** these past thirty years. Indeed, thirty years ago, the real estate was completely planned by the state. Houses belonged to the government and were distributed among the Danweis (work units). With the Reform, the government sold its lands to real estate developers who then constructed buildings to sell them on the market.

Although the real estate sector has been liberalized, the government still has a say in it and intervenes to **monitor the real estate market**. It leads two main actions concerning the commercial houses and the affordable houses (subsidized by the government):

- Affordable houses: the goal is to provide enough of them for the lowest-income families, at the right price. In 2012, these houses represented 40% of the sales on the market.
- Commercial houses: the goal is to stabilize their prices, fight against speculation, and make sure they are used for living and not only for investment. In 2012, these houses represented 60% of the sales on the market

• Affordable houses

These houses are the **top priority** for the local government. That is why it sells its lands in priority to the real estate developers that lead social housing projects. With a growing population, more and more of these projects are led far away from the city center and require the development of infrastructures as well.

The government owns these houses that can **either be rented or partly owned** by low-income families. The ownership ratio is set according to different criteria but the government remains the ultimate owner: the part owner cannot rent the affordable house he has bought and can sell it only five years after buying it, either to the government or to another person. The benefit of the sale will go both to the government and to the part owner, according to the ratio.

The government has launched a **development plan for 2011-2015**: 62 million m² (920 000 apartments) of affordable houses will be built in the Shanghai area. 30 millions of them have already been built. The building program is divided into thirty different RE promoters, building about 2 million m² each. The apartments built go from 30 to 70 m² and cost about 7 000 Yuan/m².

This affordable housing system is still the subject of an on-going reflection: should they be rented or partly owned? Should people be given money or apartments? Should all these affordable houses be built in the same area?

• Commercial houses

To make sure that most people can find a house on the market, the government keeps selling its lands and encourages the building of smaller houses. Moreover, the **regulations of the prices** have proved to be effective as they are now 0.3% lower than in 2011.

To limit speculation and investment, it is now forbidden to own more than two houses. People are also strongly discouraged to buy a second house. Indeed, the banks require harder conditions to obtain a loan: the interest rate is 1.5 times the interest rate of the first house, the down payment is 60% of the total value of the house (compared to 30% for the first house). Moreover, if the surface of the second house exceeds 60 m²/occupant, the owner must pay a tax on the extra m². Every year, the owner has to pay a tax of 0.6% of the sale price of the house on 70% of its surface, if it exceeds 60m²/occupant.

Finally, a **tax system** has been enforced to deter people from buying too many houses or houses that are too big.

However, these measures do not stop the development of luxurious housing projects, such as Wonderful Palace, a project of three-story and 300 m², richly decorated houses. For these houses, the prices are about 40 to 50 000 Yuan/m², which amounts to 2,5 million euros for the whole house.

These prices show a **big disparity** between the poorest and the richest and the necessity for the officials to provide affordable houses. The mean price on the market is about 20 000 Yuan/m².

We were taken to two projects where luxurious neighborhoods were built. The first one, Wonderful Palace situated in Jiangwan was selling luxurious apartments between 250 and 300 m² in buildings that would “reflect a noble and graceful life” if the brochure is to be believed. We visited an exhibit apartment with “perfect and extraordinary presidential quality space”. We are all stricken by how big and luxurious (sometimes almost opulent) the mansion was.

The second one was selling luxury houses and apartments. The neighborhood looked like a wealthy American suburb minus the roads. After seeing the model, we went to see a three-story house where each floor was almost as vast as the apartment we had just seen. It was also furnished, and interesting fact; all the pictures in the house were pictures of Caucasians people, as if to say, “this is the kind of house rich Europeans and Americans live in”.



Inside of an apartment in Wonderful Palace

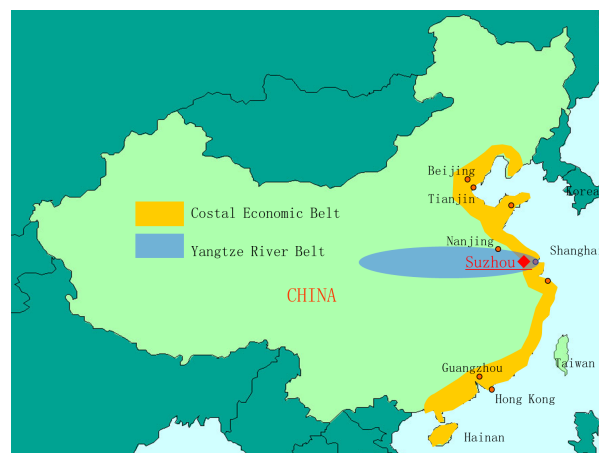


That's the model of the second luxurious project, a wealthy neighborhood with individual houses.

Although measures are being taken to regulate the market, Shanghai's RE sector won't be able to face an ever-growing population forever. Fortunately, Shanghai is going through a new economic phase. Many manufacturing companies are now leaving the city and moving westwards, while the service-providing companies represent a growing part in Shanghai's economy. As a result, the city has a 7.5% growth rate, which is below the national average, while developing regions in the West display a two-digit rate. Therefore, other cities are now emerging, offering new attractive destinations to country people who want to go to towns. The largest cities such as Shanghai will have a lower demographic pressure which will make the RE sector easier to manage while stabilizing it.

B. Suzhou

- Situation



Suzhou is a major city located in the southeast of Jiangsu Province in Eastern China, located adjacent to Shanghai Municipality. The city is situated on the lower reaches of the Yangtze River and on the shores of Taihu Lake and is a part of the Yangtze River Delta region.

Population

The population of Suzhou is 12.3 million, including 6 million of native people.

Real estate market:

In order to match the growing demand, the building construction has significantly increased during the last 15 years. For example, in 1998, 47 036 m² were build, against 1.8 km² in 2008.

The average price on the real estate market is 15 000 Yuan/m². In average, the cost of the land represents 30% of the total price of a real estate project.

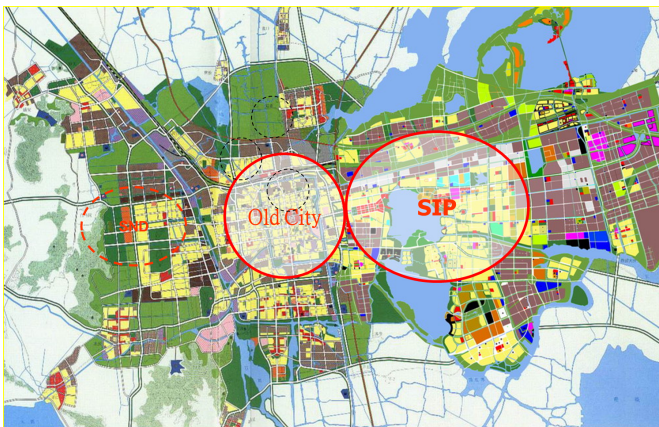
- **Policy**

There are two kinds of loans: the commercial loans and the loans provided by housing provident funds. The commercial loans are loans given by private of public bank with an interest rate of 7.06%. The second kind of loan is provided to people who work and have already contributed for these funds; the interest rate is 0.76%. Moreover, the down payment for a loan to buy a house on the primary market is 30%. On the secondary market, it is 50%.

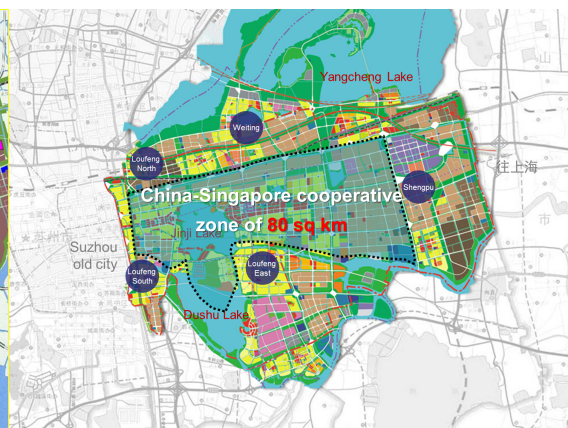
- **SIP development zone: example of Genway**

General presentation

SIP (Suzhou Industrial Park) is a 288-km² zone, which aims at being a dynamic economic zone. This project started in 1994 with the signature of an agreement between the government of China and Singapore. This area, which contains two lakes, is organized in three districts: central business district, science and technology and industrial district, tourism area. The science and technology and industrial district gathers high technologies industries, universities and housing, to create a strong cooperation zone between the educational and industrial sector. SIP represents 3.4% of the land of Suzhou but more than 15% of its economy.



The situation of the SIP zone near the old city



China Singapore cooperative zone of 80 km² on a jurisdiction area of 288 km²

Actors

- **Chinese and Singapore governments:** are financing the project;

- **Suzhou Xinjianyuan Holdings Group** (SIP Genway Development Group, Suzhou Harmony Development Group, SIP Commercial and Tourism Development Co., Ltd, SIP Surveying Mapping and Geo-information Co., Ltd) : these groups develop the project by either buying the land and building apartments, commercial, business or touristic centers, or undertaking the job of collecting, processing, managing, updating, and publishing geographical information for the planning as well as land and property development and construction.

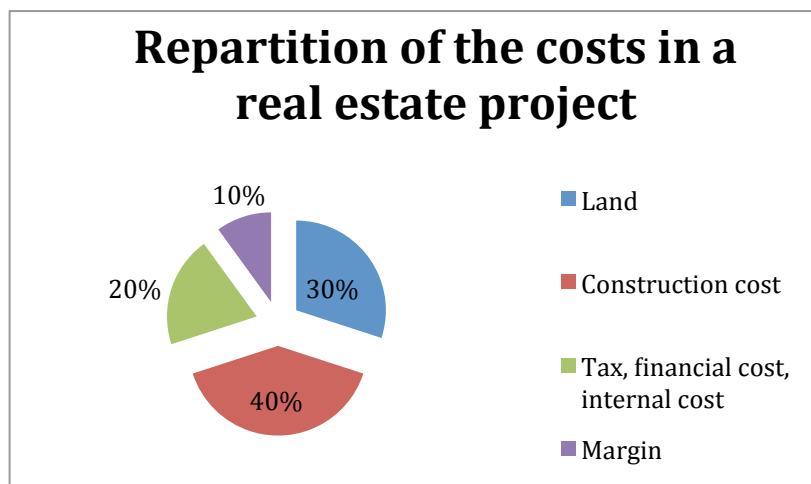
Presentation of Genway

We had the chance, in Suzhou, to meet M. Quin from Genway, who explained us the role of Genway in the SIP project.

Genway, which is one of the developers of SIP, is a state owned real estate firm. It has launched many projects in the SIP zone as offices for corporations working on nanotechnologies, or apartments in the outskirts of Suzhou and near the Jinji Lake.

Concretely, they buy the land from the government, on which they plan to do a real estate project (like apartments or offices for example). In order to do that, they have to get the permission from the government to launch their project. Once they have obtained it, they have 3 years to finish it, and then sell it.

Below is detailed the repartition of costs and margin in a real estate project:



M. Quin also took us to a couple Genway projects. First we went to a residential lot named Central Park. It was a good illustration of the process of a regular real estate development in China. We saw a model of how the finished project was supposed to look. We were then taken to an exhibit apartment. A sample if one may say, of what a regular apartment sold in this project will look like.

Secondly, we visited the Core of the World. It's composed of luxurious apartments and offices, built right on the banks of a lake. Despite the unfinished constructions around the lake, it was pretty obvious from the view we had at the top of the building and the pictures of how the site

was supposed to look when done that this area was meant to be a very nice and rather luxurious neighborhood.



The Central Park project: a residential area of 0,4 km²



A residence of the Central Park project

C. Hefei

- **Situation**

Hefei is located in Anhui province, 900km west of Shanghai. It is a 4 million inhabitants city, but the growth rate of the population was 12% in 2012 and the authorities are expecting 7 million inhabitants in 2020. Consequently, the real estate is expanding very fast.

Hefei has a strategic position: located in the middle of Anhui province, between the Yangtze River and the Huai River, connected to Shanghai, Beijing and Nanjing and other major Chinese cities via the high speed train, and its airport opens more than 80 domestic and foreign routes including international routes to Taiwan, Korea, Japan or Hong Kong.

As it is the only provincial capital encircled by five fresh water lakes, Hefei also appears to be a very attractive place, which could guarantee good life quality. Therefore, urbanization plans have been set up to take this characteristic into account and create an important environment friendly area.

Real estate market:

In 2012, 300 million Yuan were invested in real estate; it represents a 27.8% growth compared to 2011. This did not have a huge impact on the prices, which increased only by 3% in 2012. They stayed steady at 4.470 Yuan/m², a rather low price for the middle of China. The real estate market in Hefei represents 34% of the real estate business in the whole province, and has a great importance for the budget. Around 26% of the taxes come from this business and 17.8% from the construction market. In the last three years, more than 78 million m² were built and 45 million m² sold. The cost of the land is estimated to be 50% of the total price of a real estate project.

- **Policy:**

In Hefei, native people can only buy two houses, but in the area of the Binhu project, this number is unlimited to attract investors.

- **Binhu Project:**

The Binhu Xinqu is a major urbanization program that is being developed in Hefei. This project possesses unique location advantages, as it is adjacent to the old urban area to the north, facing the Chaohu Lake to the south and bordering Hefei National Economic and Technological Development Area to the west. Three rivers are also meandering through the sector.

Near the Chaohu Lake, Hefei has been investing 75.83 billion Yuan on a 25.46 km² area since 2006. Nowadays, 18.05 million of m² have been built (out of 22.61 million) and 11.42 have already been sold and are in use. The goal of the project is to build a high life quality district near the

Chaohu Lake, with residential areas, social undertakings like schools or hospitals, a cultural sector and also a financial district.

This project was designed with a particular care of the environment to protect the lake and provide high life quality standards. For example there is 18.61 m² of public green area per capita in Binhu.

According to the plan, a traffic network of five south-north roads, seven east-west roads and a ring road is to be constructed to ensure a good regulation of the traffic and direct access to the cores of the district. This part of the project has already been built and is nowadays being finished, and the bus line has also been put into use.

Binhu Xinqu also features interesting water transportation specificities: the new port Hefei Xin'gang will provide easy access to the other important cities along the Yangtze River and coastal regions. The passenger dock and commercial wharf will be built along the lakeshore of Chaohu Lake and shipping can be arranged directly to places along the Yangtze River through Yuxikou Port.

Actors

- Binhu Investment Company finances the whole Binhu project (state owned enterprise), get the money from the government. When the government sells lands, 70% of this money goes directly to the Binhu investment company. This system has proved efficient because between 2007 and 2012 the price of land multiply by 5 and reached 7.000 Yuan/m² for downtown houses nowadays.
- Heifei Binhu Xinqu Construction headquarters and Heifei Chaihu Scenic Area Administration: in charge of general planning, management of the project.
- Government of Anhui province: Invested 500 million Yuan in the first round but is already being given back this money.
- Developers: more than 80. In charge of building and selling.
- Buyers: 60% of buyers are not from Hefei.
- A Shenzhen bureau planned the Binhu project



Banks of a lake in Hefei.



That's a model a commercial center in the Binhu project in Hefei.

IV. Annexes

A. Summary of our journey

Our group, composed of eight students and one professor, went to China to lead an investigation mission on the Chinese Real Estate development.

- **General overview of the organization**

To set the investigation, our only contact in China was M. Zhangbin Wang, a PhD professor at the Dong Wu Business School of Suzhou University. The Development Research Center of Anhui Provincial Government heard about our investigation and seemed interested in meeting us and showing us a real estate project in Hefei. Hence we were officially invited by this Center that organized our visit there and also used its network to get in touch with the Development Research center of Shanghai Municipal Government that enable us to talk with real estate experts of Shanghai and to see three real estate projects in this city. It is interesting to note that our only entry point was our contact, a professor in Suzhou University and through the game of acquaintances our whole journey was unlocked. It seems unlikely that we would have found such a good opportunity in Shanghai without the connections of the Hefei's Research Center.

Thereby our investigation took place in three cities: Suzhou (Jiangsu province), Hefei (Anhui province) and Shanghai (municipality). There we've been shown huge real estate projects and were introduced to developers, commissioners and professors.

- **Suzhou**

We arrived in Suzhou on February 15 in the evening. The following day we had a lecture in the morning with the professor Shen Jian about the past, present and future of Chinese real estate. It was meant to be an introduction for our journey. In the afternoon, we met M. Yan Quin who works for Genway, a company that runs Real Estate projects. Among all the projects managed by Genway, he chose to show us one particular project, the SIP project. SIP is a large urban area near Suzhou that has the attention of Genway for they are developing a whole new zone with industries, schools, houses and offices. M. Yan Quin told us all about this project and also explained what was the low-time profit making logic that drives developers in China.

The next day, M. Quin took us to this SIP area to actually show us various buildings and neighborhoods that are parts of this SIP project. He chose to show us two different projects. He also took the opportunity to explain us how apartments are sold in China, or at least in Soochow, for we would discover later that rules are not exactly the same all over China.

The afternoon was dedicated to meeting important people of Soochow Intellectual Property and Copyright Bureau. It was supposed to be a lecture of Professor Olivier Bomsel on the concept of intellectual property but it turned out to be a political game rather than a simple lecture. We also encountered a major difficulty, the barrier of language. Only few of the people at this meeting actually spoke English and we had no official translator, which made things complicated.

The next day was our last day in Soochow. In the morning, we had a lecture at the university. Professor Xu Tao, our lecturer gave us a quick overview on how finance and real Estate are bounded together. The afternoon, we left the university to go to a shopping mall. It turned out it was Auchan, a French company. We were then able to go see the gardens of Soochow, a well-known place in China. We then took the train to Hefei.

- **Hefei**

Our first day in Hefei started with a meeting with among others, officials from the provincial government and people working in the real estate sector. We were there introduced to M. Li Yu (Vice Director of the Development Research Center of Anhui Provincial Government) and M. [must find the name]. They stayed with us until the end of our journey, which means they were with us in Shanghai too. The aim of this meeting was to summarize the evolution of real estate in Hefei: structure of the market, regulations, enforcement and main projects.

We were introduced to the Binhu project, a whole new zone between the old downtown and the lake, designed to welcome 360 000 inhabitants. It provides every service a city needs to have. It's eco-friendly. We visited two project under construction: residential and office building. And we had a tour around the project to see the evolution and to get an idea of the huge scale of the Binhu project.

M. Yu invited us this night to a good restaurant. We were told there, that a lot happens during business meals for you can show your personality. Getting a contract signed often lies on how pleasant the atmosphere is during the meal with your potential business partners. It was rather obvious that this dinner would set the pace of the rest of our journey. Hopefully he was really friendly and the dinner was truly pleasant and almost homely. We all enjoyed it was then almost certain that the rest of our journey would be very good.

After the study of this huge project and the festive dinner, the next day was dedicated to meetings and exchanges with people from Hefei linked to Real Estate, starting with a lecture from M. Bomsel about intellectual property. He explained what were the main differences between Europe/North America and China and the main regulations. It was followed in the afternoon by a discussion over cooperation in business activities.

- **Shanghai**

For our first day in Shanghai was scheduled a meeting with M. Tang Zhong Hi (Director of Development and Research at the Shanghai Municipal Housing Administration Bureau) and M. Chen Qun Min (a PhD Post Doctoral at the Development Research Center of Shanghai Municipal Government) to talk about the evolution of Shanghai's Real Estate Market. We were given a lecture on how was structured the market, what were the main regulations, how they were enforced, what were the main development projects and they gave us an overview of the present market in Shanghai and how they thought it was likely to evolve in the future; followed by a discussion on these topics.

The next day we spent the entire day out of in Shanghai, in the suburbs to see three projects. The aim of the first project was to build an entire neighborhood that would provide schools, services, housing and transportation to people that can't afford to buy a house on the

market. The project was half finished when we arrived but some buildings were done and we were able to visit a sample of the apartments that will be sold.

The second project was a neighborhood for wealthy people for the place called Wonderful Palace was selling luxury apartments. After seeing the model of the area we have been shown an exhibit apartment.

The last project was also a neighborhood for wealthy people. It was selling mainly individual houses in a very American look-like suburb.

The last day was left to wander around Shanghai and discover the city on our own. We took the airplane back to Paris that night.

B. Reading report of “Research and study on the system of housing guarantee in Shanghai”

Synthesis on excerpts of “Research and study on the system of housing guarantee in Shanghai”

by the Shanghai real estate research center

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I) Theory of housing guarantee

A) The guarantee of housing in society

Three main ideas in the theory of housing guarantee:

- welfare and efficiency
- rights and development
- equality and stability

1) (society)Welfare and (market)efficiency

In the welfare state, different approaches and understandings of several capital questions influence the measures on housing. To what extent does the government intervene in the market and monitors it? Are these interventions good for social welfare? Is improving social welfare good for the market efficiency?

Three actors are involved in the housing issues: the state, the market and the family. The main reason why the state intervenes in the housing market is that housing is a special product since it has both a commercial aspect and a social guarantee aspect.

- **Housing is a special product:**

Housing is an unchanging, motionless and perdurable product.

Housing is a combination of land and construction. Construction is a result of human labor whereas land is not.

Above all, housing is necessary for our survival, which makes **state intervention in the housing market necessary**.

- **State intervention can improve social welfare under specific conditions**

Housing is a private good, but housing construction and consumption lead to some negative externalities.

According to Liu Gongyu and Zheng Siqi, the authors of “The economy of cities and real estate”, controlling the use of land aims at reducing the negative externalities produced while using the land. In fact, it would internalize these externalities and make the user responsible of his capital and thus regulate the housing market.

Examples of negative externalities in housing:

Causes: excessively high density of houses or inhabitants, squalid living conditions

Consequences: disease contamination, criminality, social instability etc.

The housing market is unable to internalize all these externalities; this is why the state must interfere in the housing market, in order to enhance social welfare.

This intervention is good providing that:

- 1) The state protects the public interests. Room for maneuver: the state can control the land resources and the rights of land use

- 2) The state must avoid any influence from lobbies in the conception of housing policies
- 3) The state must always adapt their housing measures to the current situation, and must not apply outdated measures that used to be relevant in past situations.

- **The balance between supply and demand is hardly possible in the housing market**

What is improving social welfare concretely?

- 1) Making the resources utilization more efficient
- 2) Making a fair distribution of incomes
- 3) Encouraging collective decisions towards collective issues (and not only unilateral decisions)

In economics, there are two assessments:

- 1) An competitive market leads to a pareto-efficient economy
- 2) Vice versa

They are true only if:

- a. There is a perfectly competitive market
- b. The commodity isn't public
- c. There are no externalities
- d. Information symmetry
- e. There are no macro economical disturbance such as unemployment

Here are the main differences between a house and the other goods:

Average good versus the house

- The quality of the good and the quality of the service around this good have similar tendencies. So the price is relatively low and stable.
The houses price is high and unstable
- Numerous participants in the market leads to a free market, no participant can influence the price making, all of them are price takers.
Generally the number of sellers and buyers is limited, so a single purchase or sale can influence the price
- The market can regulate itself, the competition is open, free and not controlled
The housing market is monitored by private or public physical entities
- Supply and demand are nearly in equilibrium. Whenever their equilibrium is broken, competition enables them to recover the balance.
In the housing market, the change of the market structure precedes the change of the market transactions. Usually, temporary inactivity in the market or temporary increasing activities result in dramatic change in the supply and demand.
- Symmetry of information, easy to get an information about the good
The buyer and the seller don't have the same information

- Buyers and sellers meet each other in some commercial places (stock exchange, or saloons)

Buyers and sellers never gather together in a formal way.

Conclusion:

Due to the numerous imperfections previously listed and the housing markets' potential negative impact on the country's macro economy, the state must control and regulate the housing market to some extent, even if the state longs for a free market...

The governmental measures on housing market address the following issues:

- 1) Ownership
- 2) Finance
- 3) Land construction
- 4) Tax
- 5) Housing subsidies
- 6) Public housing (for housing guarantee)

2) Rights and developments

History has proved that industrialization is accompanied by severe housing problems, since huge rural exodus leads to a serious lack of houses in urban areas.

In all countries, the right of property was born in that very sort of background.

In 1991, the Chinese government wrote the 4th amendment on the right to adequate housing.

[...]

3) Equality and stability

According to Zhang Qun, a Chinese sociologist: "The palace is not safe when the cottage is not happy". Providing housing guarantee is vital for the country's stability.

[...]

B) The housing system of international cities

1) The standards and requirements of international cities

Much space, economic center of the country, international relations, developed services, commercial center, good infrastructures, huge material, financial, information and demographic flows

2) The housing characteristics of international cities

2.a. Supply

Houses are mainly apartments with rather small surfaces, adapted for small families.

Examples:

In London, the apartments stand for 35,9% of the private houses and 75,2% of the public houses. Two-room apartments and apartments with less than two rooms stand for 39,5% of the private apartments and 64,2% of the public apartments. These proportions are far higher than the ones in other British cities.

In Tokyo, apartments stand for 67% of all the houses, which is the highest rate in Japan.

The housing supply is tight.

2.b. Demand

There is a great housing demand in international cities, which is usually resolved by house location, the proportion of self-owned houses is rather low.

Examples:

London: in 1991, the rate of self-owned houses was 57% whereas in other British cities, the rate was 66% in average. In 2001, these figures became respectively 58% and 69%.

New York: in 2005, only 31% of the houses were self-owned.

2.c. Price

The prices soar very quickly.

Example:

London: the average/median price for a house was 363943/250000 pounds. From 1996 to 2009, the prices increased by 241% in London, whereas the average price increase in Britain was 196%.

2.d. Living conditions

The living standards (for instance the surface per inhabitant) in international cities are worse than elsewhere. The suburbs creation and extension are a specificity of international cities.

3) Why do we particularly need housing guarantee system for an international city?

Establishing such a system improves urban administration, strengthens the market and stimulates innovation (both labor force and brains flee away if they can not afford a house=> lack of human resources).

II) Mechanisms of the affordable houses system in Shanghai

There four types of social houses created by the government:

- 1) rented houses with low prices
- 2) rented public houses
- 3) houses dedicate to expropriated people
- 4) sold public houses, which are the so-called affordable houses. These affordable houses are sold to individuals, but they are owned both by the government and the individual.

We will focus on this particular type of social house.

History:

➔ 2007: the State council declared that housing guarantee is a top priority

- ➔ The same year, the Shanghai local government released a report which contains ideas and suggestions about establishing a reliable housing guarantee system.
- ➔ From October 2007 to December of 2008, the local government had been elaborating a concrete actions plan, which had been modified more than 80 times.
- ➔ In January 2009, the action plan is released.
- ➔ In June 2009, the affordable houses measures are officially unveiled.

A) Management of demand

The government's targets are people who have a housing financial burden (they have to pay too much money) or bad living conditions. The measures allow the targeted people 1) to become more financially independent by giving them the opportunity to save money 2) to live in better material conditions.

1) Measures

1.a. The applicant must meet several conditions

6 categories of targeted people corresponding to 6 conditions:

- ➔ families who live together (only close siblings, not cousins, aunts etc.)
- ➔ must have a Shanghai Houkou
- ➔ the current house surface must be under the threshold fixed by the policy
- ➔ the income and property must be under the threshold fixed by the policy
- ➔ did not sell a house recently
- ➔ limitation on the applicants age

1.b. Mentality: the restrictions must be very tight in the beginning, then the government loosen them progressively

From 2009 to 2012, the conditions of application to the affordable houses program have been less and less strict.

Example:

2009: The applicant's family annual income per member must be below 27600 RMB, and its possessions value per member must be below 70000 RMB.

2012: These restrictions became respectively 60000 RMB and 150000 RMB.

They loosened by 117% and 114%.

2) Problems:

The remote location of affordable houses

The government is compelled to build affordable houses in the outskirts in order to guarantee their low price. The inhabitants waste a lot of time and money in the transports.

Involves huge investments

There are few infrastructures in the outskirts, therefore the government has to invest a lot a money in order to develop these infrastructures (shopping mall etc.)

3) Discussion

The policy will be more and more loosened, especially towards the Houkou.

For instance, a family which contain members who don't have the Shanghai Houkou can still live in the affordable house.

How to standardize the affordable houses? Which structure and how much surface?

There are three ways to categorize the affordable houses:

- ➔ Number of inhabitants: 1 person, 2 people, 3 people etc.
- ➔ Number of generations: 1 generation, 2 generations (parents+child), 3 generations (child+parents+grandparents) etc.
- ➔ Family model: single, couple, couple with a child etc.

The third way of categorizing is the best but currently the state's room for maneuver is not sufficient enough to apply it.

So far, the state has been using the seven following categories:

One person, two person (couple), two people (not a couple), three people (a couple with a child), four people (generally three generations), five people, six people, above six people.

The more people there are, the more important are the surfaces of common rooms such as the living room, the dining room, and the balcony.

Here are the surface standards, designed for the 7 categories of families:

| number of people | one person | two people | | three people |
|--------------------------------------|-------------|-------------|--------------|--------------|
| space | | couple | not a couple | |
| main bedroom (12 m2) | 0 | 1 | 0 | 1 |
| secondary room (7 m2) | 1 | 0 | 2 | 1 |
| space for circulation (1,5 m2) | 1 | 1 | 1 | 1 |
| surface for use/person (m2) | 18 | 23 | 25 | 30 |
| surface for living/person (m2) | 12,6 | 16,1 | 17,5 | 21 |
| surface for construction/person (m2) | 25,2 | 32,2 | 35 | 42 |
| number of people | four people | five people | six people | |
| space | | | and above | |
| main bedroom (12 m2) | 1 | 2 | 2 | |
| secondary room (7 m2) | 2 | 1 | 2 | |
| space for circulation (1,5 m2) | 1 | 1 | 1 | |
| surface for use/person (m2) | 38,5 | 43,5 | 52 | |
| surface for living/person (m2) | 26,95 | 30,45 | 36,4 | |
| surface for construction/person (m2) | 53,9 | 60,9 | 72,8 | |

B) Management of supply

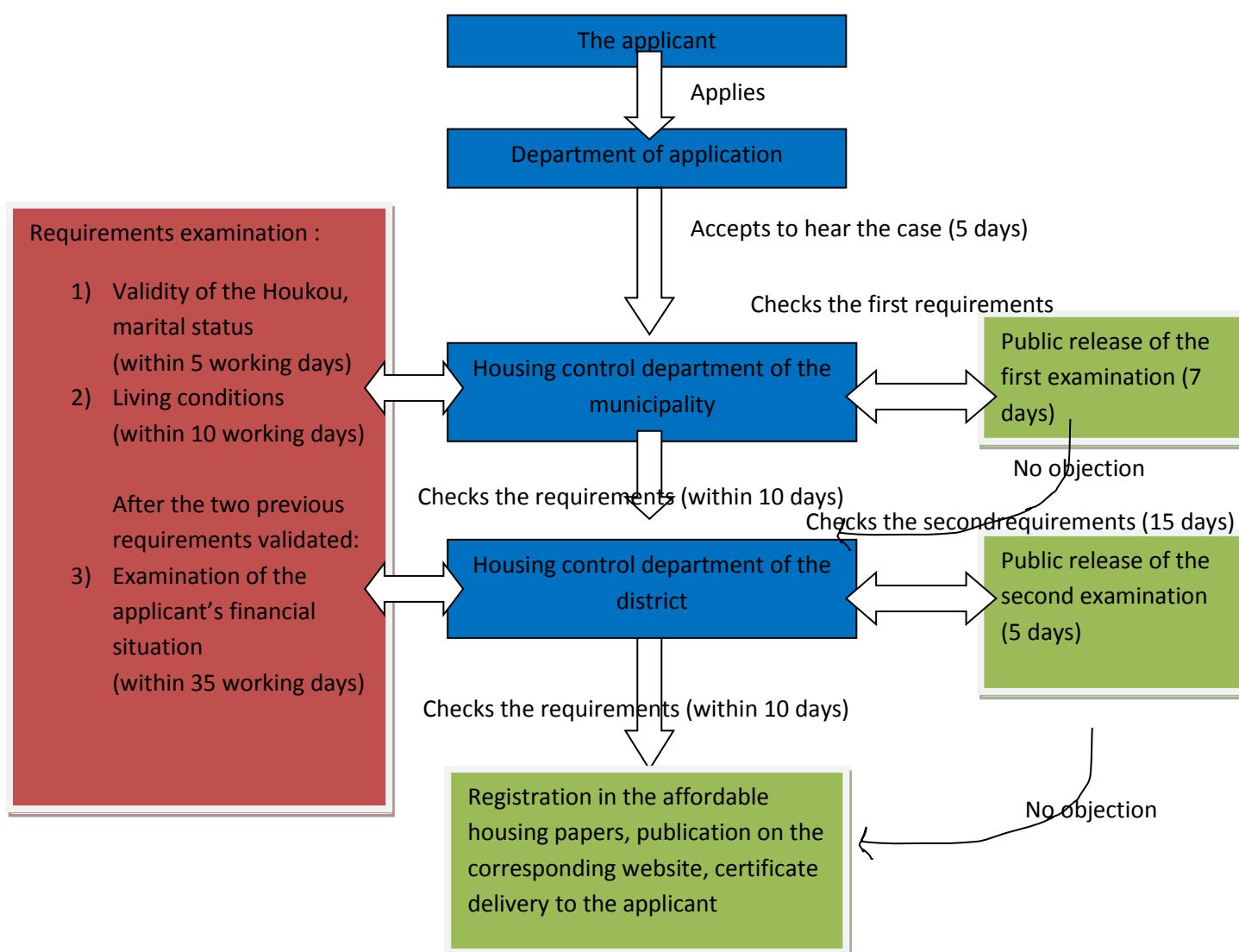
1) The specificity of the measures

1.a. a system of shared ownership

The affordable house is shared both by the government and the individual. In this way, the possibilities to make profit, due to the huge difference between the prices of commercial and affordable houses, are reduced. For instance, sublease and identity usurpation are avoided.

At the beginning, the State compelled each district of Shanghai to build affordable houses, of which surface must account for 5% of the total inhabited surface. Also, the affordable houses were built next to each other.

1.b. the complex mechanisms of application for an affordable house



2) Problems

There are still people who don't deliver the right information during their application for a affordable house. The State has already faced the following situations: people who don't confess they have another houses, people whose bank account contains huge amounts of money.

Controlling the Houkou is already a heavy task for the local administration. Now having an affordable house is conditioned by the possession of the Shanghai Houkou, which makes the affordable houses delivery much more complicated.

C) Management of operations

1) Three different managements

a. **A closed management:**

The system of affordable houses is completely separated from the commercial housing market.

Consequences: the price of the house is established according to the construction cost only; the ownership is shared by the government and the buyer and the house cannot be transferred to another person; once the buyer leaves, the house goes back to the State and under no account must be sold in the market.

b. **A mid-closed management:**

The affordable houses can be sold in the market under certain conditions.

Consequences: the price of the affordable houses depends on the land and also on the buyer's financial means; the ownership is still shared by the government and the buyer, and the latter can only use the affordable house for living; five years after purchasing the affordable house, the buyer has the possibility to give up living in that house and the State must buy his house back.

c. **An opened management:**

After a certain period of time, the buyer can sell the affordable house in the market. The buyer owns entirely his affordable house.

Comparison between the three types of management:

The State has to find a compromise between:

- Financial burdens
- Housing control
- Attractiveness to the customers
- Customers' capacity to improve their living conditions on their own

Financial burden:

The opener the management system is, the lighter the State's financial burden is.

Attractiveness to the customers:

The customers belong to the low and middle income class. Their financial means are rather low. With the opened management, they indeed own their

house, but the average sale price of this house is much higher than they the price they can afford.

In the closed management, the buyer don't own his house.

So the mid-closed management is the most attractive to the customers.

Improving the living conditions:

In the closed management, the house belongs to the State, and the inhabitant cannot improve his living conditions by changing a house and buying a new one.

In the opened management, the sale price of the affordable house is too high, which is a barrier to affordable houses from the beginning!

Here again, the mid-closed management seems to be the best option.

Guaranteeing the State control:

In the closed and mid-closed managements, the State still has the stranglehold on the affordable houses, because the latter partly belong to the State. In the opened management, the State loses control over the affordable houses.

Recap:

| type of management | closed | mid-closed | opened |
|------------------------------------|------------|------------|-------------|
| financial advantages for the State | low | average | high |
| attractiveness to the buyers | low | high | average |
| improvement of living conditions | low | average | high |
| guarantee of state control | high | high | low |
| global mark | rather low | high | rather high |

The mid-closed management of affordable houses is the best. It is currently carried out by the Shanghai authorities.

2) Characteristics: district management

Shanghai is a too large city. To make the housing control easier, each district manages its affordable houses.