

# China's property bubble reaches explosive levels

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Astronomical housing prices forced the Chinese government last week to announce a new round of measures—following two previous attempts last year—to curb property speculation. Central to the latest plan is the lifting of the minimum down payment for a second home from 50 percent to 60 percent of the price. Premier Wen Jiabao also threatened to punish local officials who failed to set and meet targets to limit rising property prices.

In addition, an experimental property tax has been implemented in Shanghai and Chongqing. Shanghai will have a 0.6 percent tax on the value of a second home, while a 0.5 percent tax has been imposed on expensive houses in Chongqing. After two interest rate rises since last October, the Chinese central bank is likely to announce further rate rises in the first and second quarters, in a bid to curb inflation and housing prices.

Last week's announcement underscores the fear within the ruling elites that the bursting of the property bubble could have explosive economic and social consequences.

An article in *China Economic Weekly* on January 25 pointed out that the average real estate price in Beijing in 2010 had reached about 8,000 yuan per square metre. With a total land area of 16.41 billion square metres, the value of land in Beijing was 130 trillion yuan, or \$US19.85 trillion, significantly higher than the US gross domestic product of \$14.5 trillion in 2010. "That means the land value in Beijing is more than enough to 'buy up America'," the article stated.

Together, the land values of Beijing and Shanghai last year were 199 trillion yuan (\$30.3 trillion), which is greater than the combined GDPs in 2009 of the world's five largest developed economies—US, Japan, Germany, France and Britain.

The *China Economic Weekly* warned that Japan entered a period of protracted economic stagnation after the collapse of its asset bubbles, especially in real estate, in the early 1990s. At the high point, "the total market value of land in the Japanese capital Tokyo alone was enough to 'buy up' America. China right now is in the same crisis."

According to a land ministry report, across China the average urban land price in the fourth quarter of last year reached 2,882 yuan per square metre—up nearly 10 percent from the same period in 2009. During the past decade, residential property prices in the major cities have doubled.

The Chinese Academy of Social Sciences recently reported that even though price increases in 2010 were slower than 2009, "it was still faster than the income growth among urban and rural residents, and 85 percent of Chinese households are unable to afford to buy a home".

The glaring irrationality of the capitalist market is expressed in the fact that while hundreds of millions of people cannot buy a home, huge numbers of newly-built flats stand empty in so-called "ghost towns," because investors are hoarding them as commodities, waiting to sell at a higher price.

The scale of China's "ghost towns" was underscored by a figure released by China's national electricity authority last year. About 65.4 million homes in 660 cities were recorded as having had no power usage for six consecutive months. While not every home without power usage is owned by a speculator, the figure has been widely used by economists to show that empty flats could be used to house 200 million people. Millions of poorly-

paid rural migrant workers whose labour power builds these properties are living in makeshift shanties and tents.

The skyrocketing property prices are a product of low profits in other economic sectors, particularly manufacturing, which has been hit by the ongoing turmoil in China's two biggest export markets, because of the European sovereign debt crisis and depressed US consumer demand. Even businesses unrelated to property development, such as industrial and energy companies, have been heavily involved in real estate speculation. The property market offers returns of about 30 percent, whereas manufacturing provides 5 percent at best. The most expensive piece of land in Beijing's CBD was bought last year by the China Weapon Equipment Corp.

The government directly fuelled these speculative activities. In the aftermath of the 2008 global financial meltdown, Beijing ordered the state banks to flood the economy with cheap credit, in an effort to stave off rising unemployment. Bank lending in 2010 was \$1.2 trillion, only a little lower than the all-time record of \$1.4 trillion in 2009. More than a quarter of bank lending went directly into real estate development.

The property bubble was exacerbated by growing US pressure for a revaluation of the Chinese yuan against the dollar, encouraging speculators to buy yuan-denominated assets. Near-zero interest rates in the US also encouraged speculative funds to move into China, where interest rates are much higher. All these factors were exacerbated by the "quantitative easing" of the US Federal Reserve Board that injected hundreds of billions of dollars into the American banking system to cheapen the dollar.

Liu Wei, a director of the State Administration of Foreign Exchange (SAFE), which holds a \$2.85 trillion foreign currency reserve, tried to downplay concerns over "hot money" flowing into China. He declared earlier this month that "we did not find any organised or big-scale hot money inflows". However, he criticised the US "quantitative easing," saying that "it may bring inflationary and asset bubble pressures to the world economy, and add more uncertainties to the global recovery". China's foreign reserves grew by \$200 billion in the last quarter of 2010 alone, indicating that much of it could be speculative capital.

While the Chinese regime is trying to slow property

prices, it cannot afford to trigger a crash in the sector. China's retail growth and government revenues have been "kidnapped" by real estate, to use the phrase of some Chinese economists.

According to the National Statistics Bureau, from January to November last year, total sales of residential homes (4.23 trillion yuan) accounted for nearly one third of the total retail consumer goods (13.9 trillion yuan). Of China's 8.1 trillion yuan in tax revenue in 2010, one third came from land transactions, thus encouraging local governments, in particular, to promote and participate in real estate speculation. Important industries, especially steel, cement and construction materials, are dependent on the expanding investment in real estate.

The real estate boom is also driven by rapid urbanisation, with 15 million rural migrants moving into the cities each year as cheap labour for the corporate elites.

Beijing's embrace of the "market mechanism" and private developers, at the cost of rational urban planning, has created a giant bubble that threatens to engulf the Chinese and global economy. At the same time, high costs and the failure to provide decent housing will inevitably help fuel discontent among hundreds of millions of workers whose basic needs and rights are routinely trampled on.



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