Changes in the Chinese Property Market: An indicator of the difficulties faced by local authorities

MYLÈNE GAULARD

ABSTRACT: For the past decade, China has faced an extremely sharp rise in property prices and increasingly large investments made in this sector. Although some economists consider this change to be no more than the result of the increase in urban salaries that has gone hand-in-hand with China’s strong economic growth, this article will show that it is in fact a “property bubble” resulting from the speculative activities of certain economic agents operating in this sector. Local authorities play a major role in this, especially in their efforts to increase their income, and their behaviour needs to be analysed in order to better understand that a bursting of this bubble might expose economic problems of a far deeper structural nature than those usually identified.

KEYWORDS: Property market, land, speculative bubble, budgetary deficit, decentralisation.

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n observation often made since the last international economic crisis points to the decoupling of the economic development of China, which appears to be maintaining a high rate of growth, from that of the wealthiest countries of Western Europe and North America. However, the Chinese economy experienced a slowdown in 2012, and while Gross Domestic Product (GDP) grew by 9.3% in 2011, it only reached 7.8% in 2012. This slower rate of growth is more often than not put down to the economic crisis that China’s main commercial partners are experiencing. The economic slowdown in these countries has weighed considerably on Chinese exports, which now represent “only” 31% of GDP as opposed to 38% in 2007. Along with a reduction in imports, this has led to a drop in the trade surplus from 9% to 2% of GDP over this period. Since the domestic market is unable to take over from external demand, China appears to have no choice but to depend heavily on the economic circumstances of so-called developed countries to maintain its rate of growth.

However, this article will show that commercial dependence, which is so often emphasised, is actually just one of the problems China faces. Attention will instead be paid to the Chinese property bubble, which has been growing since the early 2000s and is likely to burst in the very near future and expose problems that are far more structural in nature than a mere slowdown in the export market. Firstly, we will analyse the increase in Chinese property prices, the opening up of this market in the 1990s, and the reasons why we consider the current increase in prices to be a “bubble.” We will then focus on the role played by local authorities in this change, in particular in order to reveal the major difficulties the Chinese economy will have to face up to in coming years. Straightforward changes in the property sector or a property “bubble”?

Although some economists argue that the recent rapid growth in the Chinese property market can be explained by strong economic growth going hand-in-hand with a process of liberalisation of this market, the change observed carries all the hallmarks of a speculative “bubble.”

A justified rise in property prices

Description of the Chinese property boom

Property prices doubled between 2004 and 2011 in China’s 35 biggest cities (see Graph 1), and many economists have sought to analyse this change in an effort to understand, in particular, if it represents a bubble, or in other words, if a gap is opening between the basic value of goods and their market price. Before presenting this debate, it must be noted that although the increase was slower in 2011, prices have actually continued to rise in the biggest Chinese cities. This was one of the trends researched by the NDRC (National Development and Reform Commission), and by Tsinghua University, based on a sampling of 1,000 new and pre-owned properties in 70 cities.


employs 14.3% of urban workers, and uses 40% of the steel produced in China. This change is even more marked in the coastal cities, and Guangdong Province, the nerve centre of the Chinese economy, was attracting more than one third of the country’s property investments as far back as 2006.  

A change linked to the liberalisation of the property market

This concentration of property investment and the increase in prices in the richest regions experiencing the strongest economic growth has led certain writers to reject the theory of a property bubble, i.e., an increase in prices that is disconnected from economic growth and in particular from the basic value of goods. Economists ranging from Kindleberger to Shiller have defined a bubble as an excessive rise in prices in relation to the basic value of the goods exchanged and incomes. This rise tends to be aggravated by the speculative behaviour that it encourages or, in other words, decisions to buy purely with the aim of selling the purchased goods at a higher price. Yet the aforementioned writers do not see the Chinese situation as a property bubble, because the increase in prices has simply kept pace with economic growth and the increase in incomes nationally, and has taken place against a backdrop of liberalisation in the property market.

The opening up of the property market in the 1990s resulted in a sharp rate of growth in this sector, and at this point a short history of property in the People’s Republic of China needs to be set out in order to understand this change. With the establishing of the PRC in 1949, urban property was nationalised, and for more than three decades, the state had sole power to distribute this property to households, in particular through the work units (gongzuo danwei), which enabled households to obtain accommodation at very low rents. It was only in the 1980s that privatisation began to take place, initially in several coastal cities before being rolled out nationwide. At first, this involved starting to privatise certain state-owned housing, which was sold to foreigners or private sector employees.

In 1988, the constitution was changed in order to encourage the development of the private property sector, and although the state retained its status as sole landowner, the constitution now authorised it, along with local authorities, to sell land use rights lasting for a maximum of 70 years. Later, in 1994, a series of measures was brought into effect in order to encourage Chinese households to purchase, at below market prices, the housing that had until then been provided to them by their work units. In 1998, at the same time as a surge in the privatisation of the least profitable state companies, the remaining work units were prohibited outright from procuring accommodation in any form whatsoever for their employees, and from then on this old benefit was instead to be directly incorporated into the salary paid. This liberalisation of the market explains why the surface area supplied by the private property sector increased from 25 million square metres in the mid-1980s to nearly 500 million in 2007.

The Ministry of Housing and Urban-Rural Development and the National Bureau of Statistics estimate that, owing to this mass privatisation, 80% of housing is now held by the private sector. Some economists confuse this rate with the rate of household property ownership as it is calculated in the majority of other countries, where it indicates the percentage of households that own their homes. While the Centre for Financial Research of the People’s Bank of China estimated the rate of property ownership to be 89.68% in 2010, it should not be forgotten that the survey carried out that year reflected only 4,000 households (out of 400 million across China), and that this rate did not take into account illegal workers whose only option when it came to finding urban accommodation was to rent because they had left the countryside without first obtaining an urban residency permit; it is estimated that such workers represent as much as 30% of the working population in cities.

Despite these few reservations, there is no doubting the fact that the opening up of the property market has seen more and more households taking ownership of their homes. This trend pushes prices up, a phenomenon accentuated by the fact that three quarters of urban families, whether property owners or not, would now like to obtain a new home because of the low level of legal protection afforded to tenants and their wish to improve their living conditions, as illustrated by the fact that the average living space had grown to 27 square metres by the end of 2009, compared with just 6.7 in 1978.

Increasing urbanisation (see Graph 3) is another reason behind an increasingly high level of demand for housing in cities, and the fact that it is easier to obtain a residency permit (hukou) in China’s ten biggest cities (in particular Shenzhen and Shanghai) suggests that this movement could increase compared with just 20% of the total population in 1980, urbanisation reached a level of 50% in 2011. The big increase in the average urban salary, which grew by 260% between 2001 and 2010, as illustrated in graph 4, goes even further towards explaining the pressure on property prices.

All the hallmarks of a bubble

An increase in the ratio between property prices and average household incomes

Although the basic value of a property is one of the most difficult concepts to calculate, there are certain indicators of a gap between the market price and the economic development of an area. In particular, in the view of Robert Shiller, who analysed price increases in the United States property sector in the years leading up to the bursting of the bubble (1988-2003), a bubble can be identified by the enthusiasm shown by the entire population, especially the media, for a sector that allows immense

fortunes to be created, at the same time that a gap is growing between the rate at which incomes are growing and the increase in property prices. (15)

There is no ignoring the fact that a high proportion of Chinese billionaires now come directly from this sector: according to the Asia Pacific Wealth Report of 2010, 18% of Chinese billionaires in 2008 were property developers, compared with 27% in 2010. Above all, the ratio between average property prices and the average annual incomes of households, which were studied at length by Chung and Kim (16) with regard to the property bubble that developed in South Korea in the decade starting in 2000, is becoming ever higher. Chung and Kim considered that while a “reasonable” level for

this ratio could be set at between 3 and 4 to 1, it was greater than 10 to 1 in the South Korean cities that formed the study. Similarly, this ratio has reached an average of 8.5 to 1 in Chinese cities, and is in excess of 15 to one in the large coastal cities (see Graph 5). Such figures clearly indicate the presence of a bubble, and are all the more marked when compared with the ratio of 8 to 1 observed in Spain or the United States at the height of their property bubbles.

The spectacular rise in urban incomes described above needs to be examined more closely. The salary data only relates to salaries paid by urban establishments in the formal sector, yet the informal sector currently accounts for more than 50% of the working population of China. Moreover, it does not take into consideration migrant workers who have left the countryside in order to work in the cities without an urban residency permit, and who may be paid 40% less than so-called resident workers. This analysis of urban incomes in large Chinese cities therefore explains why the increase in the ratio between property prices and average household incomes has been so great since the mid-aughts, using data obtained through field studies, which is more accurate than macroeconomic data gathered on a national scale. (18)

This development looks as though it could be dangerous for the Chinese economy, because the ratio weighs heavily on household consumption, which at just 37% of GDP is one of the lowest levels in the world. On top of the precautionary savings set aside by households in order to cover healthcare, education, and retirement spending (areas for which the state is offering less and less cover), additional savings are being built up because of the wish of Chinese households to one day own their own home. It is even estimated that young urban couples are more often than not obliged to use up the savings of all four parents in order to become homeowners.

The increasing burden of bank credit

The increasing burden of bank credit on the Chinese economy is another clear sign of a bubble. According to the People’s Bank of China, the volume of bank loans rose to 145% of GDP in 2011, whereas the rate had been even estimated that young urban couples are more often than not obliged to use up the savings of all four parents in order to become homeowners. (17)

Local authorities playing a part in the inflation of the property bubble

Local governments are directly involved in the inflation of the property bubble, and the role they play in this market can be explained, above all, by the financial difficulties they have faced in recent years. These difficulties, and the fact that income from the property sector is essential to them, largely explain the central government’s inability to control the development of this sector.

A role related to the specific status of the land market

Local governments (provinces, townships, and villages) get around the fact that banks are prohibited from lending to them by creating ad hoc companies called Local Government Financing Vehicles (LGFV) (difang zhengfu rongzi pingtai 地方政府融资平台). Using these financing bodies, the authorities have been able to absorb nearly 50% of the bank loans paid out over the past ten years, (22) and it is thought that each local authority is currently linked to approximately ten LGFs, as opposed to four in 2008. Three-quarters of these bodies are dependent on lesser authorities, below township level, which makes it very difficult to control them. (23) According to an audit carried out by the National Audit Office (NAO, shenjishu 审计署) in 18 provinces, 16 cities, and 36 townships, (24) the territorial entities studied have a debt ratio exceeding 400% of their income. This level of debt is made

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23. Zlotowski in Patrick Artus et al., L’émergence de la Chine impact économique et implications de politique économique, op. cit., p. 284.
possible largely by the proliferation of these financing bodies. According to the China Banking Regulatory Commission, only 27% of the loans paid out to LGFVs are covered by the revenue earned from the investments made.

Yet this increasing debt is leading local authorities to play a role in the inflation of the Chinese property bubble. Indeed, in order to capitalise their financing bodies, the authorities transfer to them land or buildings that serve as a guarantee to the banks. At this point, grasping the specific status of land ownership is essential in order to gain a better understanding of the rapid growth that has taken place in the property sector since the 2000s: legally, the land continues to belong to the state (or, more specifically, to the central government in urban areas, and to local authorities, mainly village committees, in rural areas), and the proportion that the local governments are authorised to sell by granting land use rights (rather than “ownership rights”) remains indeterminate, with negotiations more often

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**Graph 3 – Rate of urbanisation as a percentage of the total population**


**Graph 4 – Actual average annual urban salary in China (in yuan)**

Source: National Bureau of Statistics, China Statistical Yearbook, 2011 (actual salary calculated from the average nominal salary deflated by the consumer price index)
than not taking place at a local level. This means that local governments have the power to requisition land, and explains why the land of more than 50 million peasants was expropriated in the decade starting in 2000.\(^{(25)}\) As we will see below, after recovering land that was initially requisitioned by the state, the local authorities sold the usage rights of this land to property developers, or used it directly in order to make significant investments themselves in construction projects that were often of a non-residential nature.

Since 1988, the Chinese Constitution has stated that authorities are permitted to sell land use rights that were typically acquired at a very low price by public companies (Graph 9) or bodies close to the local authorities who wished to profit from the low price of land\(^{(26)}\) and very quickly release income from their property investments. It was estimated in 2010 that 71% of the land use rights in Beijing had been bought by public companies, compared with 37% in 2003.\(^{(27)}\) Of the 129 State companies controlled by the central government and monitored by the State-owned Assets Supervision and Administration Commission of the State Council (SASAC), 70% had made investments in property,\(^{(28)}\) and it can be assumed that this percentage is higher still in the case of public companies that are dependent on the local authorities. For this reason, one third of the 2008 recovery plan was channelled towards the property sector.\(^{(29)}\)


\(^{26}\) Michel Aglietta, Guo Bai, La Voie chinoise, Paris, Odile Jacob, 2012, p. 357.

\(^{27}\) Jing Wu, Joseph Gyourko, Yongheng Deng, “Evaluating Conditions in Major Chinese Housing Markets,” art. cit., p. 34.


\(^{29}\) Ibid.
This system not only enables public companies to invest in the property sector, but also further benefits them through the subsequent sale of usage rights at higher prices. A law introduced in 2004 as part of the fight against corruption has made it mandatory for transactions involving the transfer of land use rights to take place on the market, rather than through direct negotiations with local authorities. Although this is not an easy rule to apply, it does explain why the proportion of property value accounted for by land has not stopped rising since the middle of the decade, representing 23% of the price of homes, and even as much as 60% in Beijing, because successive instances of speculation on the use rights of a piece of land will push its price up considerably.

32. Kun Liu, Procédures et acteurs de l'utilisation du foncier chinois dans un contexte de mutations socio-économiques, op. cit., p. 79.
Investments intended for the wealthy

In 1998, a law was introduced defining the concept of “price-subsidised housing” (jingji shiyong fang 经济适用房), for which the sale price is subsidised, as opposed to the existing “subsidised rental housing” (lianzu fang 廉租房), for which rent is subsidised. The aim of this new concept was to provide housing for families earning modest incomes at a price of only 3 to 5% more than the construction cost, with an injection of funding coming mainly from the Housing Provident Fund. Today, figures show that only 3% of new housing falls under the price-subsidised housing category, compared with a high of 25% at the end of the 1990s. This is because the authorities involved in the property market can see little real point in investing in this unprofitable sector. With a view to increasing the sale price of use rights, local governments have even gone to the length of imposing limits on the supply of land that can be used for residential purposes. This helps explain the inflexible nature of land prices available on the market and pushes housing prices up even further. As Graph 2 (see above) shows, investment in non-residential construction is increasing at a much faster rate than in residential construction.

Local authorities also show a reluctance to attract residents earning low incomes, instead favouring investment in the luxury residential sector, which is likely to attract households earning high incomes that will provide them with considerably greater income from taxation. This behaviour is at the root of an even higher ratio between property prices and the incomes of the poorest households: Gao Lu claims that while this ratio averages out at 20 to 1 in the ten largest cities of China, it is only 2.45 to 1 for the richest 20% of households, as opposed to 22.69 to 1 for the poorest 20% (compared with an average of 5.6 to 1 and 9.7 to 1, respectively, in the rest of the world). This development is behind the emergence in China of “neoliberal urbanism,” whereby there is an increase in infrastructure and property intended for the wealthiest categories to the detriment of the majority of the population.

The investments made in the construction and luxury residential sectors – rather than in developing areas of the property sector that serve the households most in need – are a strong indicator of mass speculation, and could yet prove to be instances of considerable overinvestment. Such phenomena have attracted increasing media attention in recent years, with reports on the proliferation of ghost cities – Ordos in Inner Mongolia being one fairly typical example – as well as under-used airports and roads and an increase in the number of empty homes, which current estimates number at more than 70 million. In his 2008 doctoral thesis, Kun Liu observed that “by failing to take all the various types of homes into consideration, the supply of land for the property market does not effectively meet the full range of demand, and instead has a tendency to aggravate the imbalance between the provision of luxury housing and the general demand for ordinary housing.”

We will now look at how the behaviour of local authorities to push property prices up can be explained by the profound financial problems they currently face and that they will have to tackle due to major structural faults in the Chinese economy and the financially unbalanced relationship between the central government and local authorities.

Property: An indispensable source of income for local governments

Increasing financial difficulties

The role played by the local authorities in inflating property prices enables them to draw considerable income from this sector. In 2009, from a total income of 3,258 billion yuan made by all the local governments, an estimated 481 billion (or 15%) was generated by the property sector. It should also be remembered that this sum does not factor in significant income such as that earned from the sale of use rights of land expropriated from peasants, who receive derisory sums in compensation. In Beijing and Zhejiang Province, for example, the sale of land use rights alone represents 30% of local government income. At a national level, if the income generated from land transfers is added to that made from investments in property, the total income from property rises to 1,366 billion yuan, or nearly 50% of the overall income of the governments in 2009.
This income is currently essential for local authorities because of the serious financial difficulties they face. Following the decentralisation policy of the 1980s, local governments were handed responsibility for 75% of public spending carried out on Chinese territory, but taxation no longer generates enough income for them to balance their budgets. The recentralisation that took place in 1994 did not lead to an improvement in their budget balance; on the contrary, although it left the majority of spending in the hands of local governments, the majority of their income was channelled back into the central government budget. Indeed, since 1994, the central government has received 50 to 55% of the annual income from taxation, compared with 33% during the previous decade, despite the fact that since the end of the 1990s, 80% of public spending has been the responsibility of the local authorities. The latter must assume financial responsibility for public services in addition to implementing the social policies of the state, which means that more than 90% of spending on education, healthcare, and environmental protection is currently covered by local authorities.

This change in the way government spending and income are apportioned is at the root of the deepening deficit of local authorities, which increased from 3% of GDP in 1994 to 8.5% in 2011 (Graph 11). In a similar development, while central government debt is only 17% of GDP, that of the local governments had already officially reached 27% in 2010 compared with 18% at the end of 2008 (Graph 12). Faced with the recentralisation policy introduced in 1994, it was very much in the interests of the local authorities to stimulate the property market, make significant profits through the sale of land use rights, and attract the wealthiest households by constructing luxury housing in order to increase taxation revenues from this group. The fact that the majority of decisions pertaining to public investment are decentralised also explains the instances of overinvestment referred to above, such as the construction of several airports only a few dozen miles apart.

44. Christine Wong, “Central-local Relations Revised,” China Perspectives, September-October 2000, No. 31, pp. 52-63.
This kind of behaviour is encouraged all the more by the fact that foreign investment is also playing a part in the increase in property prices. Indeed, this sector currently attracts more than a quarter of the direct foreign investment coming into the country (Graph 13). The profits generated by reselling property and land use rights at prices higher than the purchase price is now encouraging the vast majority of economic agents to look to this sector rather than to an increasingly unprofitable means of production. In the same way, public companies, the vast majority of which are now dependent on local authorities, also find themselves faced with profitability problems linked to the difficulties the latter are experiencing when it comes to balancing their budgets. The result is that all these actors are encouraged to seek to profit from the property sector in order to increase their incomes.

The essential implementation of policies to fight speculation

The case of the city of Wenzhou possibly foreshadows what could very soon happen in the rest of the Chinese economy. While this south-eastern city was held up in the 1980s as a model of growth due to its high number of small and medium-sized enterprises in the export sector, the sudden 50% drop in property prices between 2011 and 2012 revealed the profound weaknesses of this model. In order to invest in the property sector, many companies in the city had taken out informal loans from non-banking institutions that offered loans under less stringent conditions but at far higher interest rates than the traditional banking sector; when the bubble burst, this excessive debt was exposed and caused the collapse of this shadow banking system. Yet as we have already seen, it is highly likely that the official banking sector is also making comparable loans that have allowed a similar bubble to develop at a national level, and also in the property market.

Paradoxically, it is not so much the liberalisation per se of the property market that has caused this sector to rapidly grow and become disconnected from the rest of the economy. Rather, it is the overlap of this liberalisation with the financial difficulties faced by local authorities and public companies, which are making the most of a banking sector that is still very favourably disposed towards them. Therefore, contrary to the argument that is sometimes put forward as one of the reasons behind China’s economic success, it is by no means certain that the liberalisation of the market, which is taking place in a context in which the public sector is still a major player in the economy, is without its drawbacks for present-day China.

In order to help finance local authority spending and forestall the lack of transparency of the financing bodies used until recently to take out bank loans, the central government launched a pilot programme in October 2011 involving the issuing of municipal bonds in cities such as Shanghai and Shenzhen, as well as in the provinces of Guangdong and Zhejiang. Furthermore, Shanghai and Chongqing are now authorised to levy a property tax, which should help increase the incomes of local authorities and also fight property speculation. That said, this tax poses a legal problem insofar as a property tax cannot be applied if the private right to own land is not recognised in the Constitution, which only authorises the "transfer of use rights." (50)

In order to counter the overheating observed in the property market, the Chinese government has also put in place various other measures, with mixed results. In terms of monetary policy, with the aim of limiting excessive bank debt, the interest rate on one-year loans rose consistently from 5.31% in 2009 to 6.56% by the end of 2011, and above all, the level of required reserves increased from 14% in 2009 to 21.5% in 2011, rising 12 times between 2010 and 2011 while the interest rate increased only three times during the same period.

More specifically in terms of the property sector, new rules were also decreed in 2010, followed a year later by the "Eight New Articles" introduced specifically to restrict the number of bank loans paid out for purchasing or investing in property. For example, starting in 2010, loans were suspended beyond the purchase of a third property, and the minimum contribution required to purchase one’s home was increased from 20 to 30%; in 2011, the personal contribution required to purchase a second home was raised to 60% of the purchase price of the property, and the purchase of a second home by anyone registered as a resident for less than five years was prohibited. This final measure was initially piloted in Shenzhen and Shanghai before being rolled out to all other major cities. A new tax...
applicable to owners of two or more properties was also introduced in 2011. Moreover, in order to fight against speculation, leaving land unoccupied is prohibited, and the local authorities are required to take back land use rights if construction work has not started on a piece of land within two years. However, as the mere digging of a hole in the ground marks the start of construction work from a legal point of view, speculation remains very difficult to control in this way. Also, foreign investment in this sector is subject to very strict controls, and foreign entities entering the property sector are required to have offices in China or to be able to show they have partners working or studying in the country. This condition goes some way toward explaining why the hot money seeking to profit from property speculation often takes the form of FDI, and why direct investment is becoming more and more widespread in the property sector. Furthermore, the construction of social housing sold at a low price has received constant encouragement from the central government, and 36 million subsidised homes are set to be built by 2015. However, this is not necessarily in the interests of the local authorities, although much of the responsibility for building these homes rests with them. Although these measures are most probably behind the slight drop in prices seen in some cities during the final quarter of 2011 (Graph 14), their impact remains limited due to the behaviour of local authorities, which the central government finds even more difficult to control because it is in the interest of the state to let them take action to reduce the public deficit. However, it should not be forgotten that when China experienced the beginnings of a property boom a few years ago, this was swiftly brought to a halt when the central bank raised interest rates to limit overheating in this sector. Indeed, there was an increase in property prices in the early 1990s, during a period when the country was showing strong economic growth and implementing an expansive monetary policy. The free market economy was greatly stimulated in the property sector by the proliferation of property companies during the summer of 1992, and at the same time, state banks were given permission to begin operating in this sector. As a result, property prices rose by more than 30% between 1992 and 1993, before dropping in response to the restrictive monetary policy implemented by the government to curb inflation.

Such a scenario would currently be very dangerous for the Chinese economy, because it could expose the excessive debt of local authorities, along

Graph 13 – Direct foreign investments in China in billions of dollars

Graph 14 – Changes in housing prices in the 70 biggest cities in China, given as the number of cities experiencing an increase, decrease or no change in the price per square metre

with major and risky implications for companies in the property sector, whether public or private, domestic or foreign. Indeed, this situation explains both the reduction in the level of required reserves on 5 December 2011 – the first such reduction granted to the banks by the Chinese government in three years – and the decrease in the reference interest rate in June 2012.

**Conclusion**

The Chinese property market has been experiencing exceptionally rapid growth since the 1990s. The aim of this article was to demonstrate how this rapid growth could be considered a bubble, or in other words, if a gap is opening between the market price of goods and their basic value. Whether one decides to focus on the high price-to-income ratio, the level of bank debt weighing ever heavier on the Chinese economy, or the commissioning of construction projects that do not necessarily match national demand, there are a number of factors that perfectly illustrate this wide gap, which results from speculative activities that can be traced back to local authorities and public companies as well as private developers and many foreign firms. Nevertheless, this phenomenon cannot be understood without carrying out a more in-depth analysis of the particularities of the Chinese market.

In order to better understand the Chinese property market, we have shown how 1988 and 1994 were decisive years in terms of inflating the current bubble. Authorising local authorities to transfer “land use rights” in 1988 marked the beginning of a period of land speculation based on the purchase of these use rights by public companies or private property developers enjoying privileged relations with the local authorities and thus able to obtain the use rights at modest prices with the aim of subsequent resale. In 1994, this phenomenon was further accentuated as urban households were encouraged to purchase the homes they had been provided with by their work units, and this liberalisation of the property market was the trigger for a sharp rise in housing prices that started in the 1990s. Another reason why this year was an important one in the history of the Chinese property market is that it saw the state recen-tralise the income earned from taxation, resulting in increasing financial difficulties for the local authorities, who still shoulder 75% of public spending nationally.

The swift growth observed in the property sector today cannot be compared to that of the 1990s, because the current increase in prices is essential for reducing the public deficit of local authorities, given that half of their resources now come from the transfer of land use rights, and more generally from the property sector. Therefore, the changes in the Chinese property market reveal the serious financial problems facing local authorities and public companies, which appear to be less and less profitable. This analysis helps to better understand why, since the end of 2011, the Chinese government has been trying to boost economic activity by reducing interest rates, not only to counter an economic slowdown attributable to decreasing export volumes, but also to delay the bursting of the property bubble.

Indeed, the drop in prices in 2011 gave rise to a real fear that the bursting of this property bubble was imminent. Should the bubble burst, the consequences on the Chinese economy would be disastrous, especially because the problems of excessive debt and increasing deficits of local authorities would be exposed, and because foreign capital invested in the property sector would be withdrawn. This would put serious pressure on China’s international reserves, which could at present be seen as its main asset.

While the difficulties of the Chinese economy have more often than not been analysed in terms of the country’s strong dependency on its exports and the circumstances in which developed countries now find themselves, the above analysis of the property market indicates problems of a far more structural nature.

Translated by Will Thornely.

Mylène Gaulard is Maître de conférences (lecturer) in Economics at Université Pierre Mendès France – Grenoble 2.
Centre de Recherche en Économie de Grenoble (CREG), Bureau 529, 1241, rue des Résidences, 38400, Saint Martin d’Hères, France (mylene.gaulard@gmail.com).