China’s Property Market: Too Big To Fail?

Dr Charlie In, Executive Chairman of Cedar Strategic Holdings Ltd, says China’s outlier cities like Bijie in Guizhou Province could be China’s next hotspot

Contrary to the views of observers that China is facing a property bubble, those who have visited southwest China will bear testament that the property market there remains hugely attractive, with growth most apparent in the third- and fourth-tier cities. Commentators frequently bemoan China's slowing economy and the millions of properties left uninhabited nationwide. Yet, there remain hidden gems in these untapped areas/opportunities.

China's property sector is “too big to fail” – 16% of direct contribution to GDP

The property sector's slowdown in recent years has been in part engineered by the Chinese government, which has been trying to curb a US$6 trillion shadow-banking industry and reduce overcapacity and pollution.[1]

The slowdown has already taken a toll on local governments' fiscal revenues. According to the National Bureau of Statistics, the growth of new builds/developments, a leading indicator of property investment, fell 27.2% year-on-year in the first quarter, while sales in residential areas contracted by 5.7%. Statistics released by the Ministry of Finance on 19 May 2014 showed taxes related to the property market contributing lesser to the growth of local fiscal revenue; business tax for real estate was down by 4.2% in April.

The market slowdown has prompted local governments into action as the property sector is and remains a key growth driver of the nation's economy, contributing some 16% of gross domestic product (GDP) and 25% of fixed-asset investment, and has significant spillover effect to over 60 industries.[2]

Considering the importance of the property sector to its economy, several city governments have announced loosening measures, including the relaxation of purchase restrictions, lower down payment requirements and easier access to local bank mortgages. The central bank was reported to have asked banks to speed up mortgage lending, set mortgage rates at reasonable levels and do more to meet first-home buyers’ mortgage requirements.[3]

Sheng Laiyun, a spokesman for the statistics bureau, said that “the property market has had new developments including falling prices in third and fourth-tier cities... relevant departments will closely follow the changes in the property market and improve property macro-control policies accordingly,” in what can be interpreted as a sign and willingness of the Chinese government to introduce “targeted easing” following years of tightening measures.

Many economists believe a persistent and sharper downturn in the property sector is the biggest risk to China's economy in the next couple of years and with the property sector playing such an important role in the nation's economy, it's unlikely China's politburo will allow such a scenario to happen; China cannot afford a collapse in any of their key sectors like banking and property.

China's economy continues to be on an upward trajectory

Having said that, the Chinese economy continues to be on an upward trajectory; growing in the high single-digits while the rest of the world languishes behind – the United States reported a 1.9% growth in 2013[4] while Europe flat-lined with GDP contracting by 0.4% in the Eurozone.[5] By contrast, GDP growth in China for Q1 2014 expanded 7.4% year-on-year, according to its National Bureau of Statistics, with the World Bank forecasting China's GDP growth to hit 7.6% and 7.5% in 2014 and 2015, respectively. This positive view on the Chinese economy is also shared by Deutsche Bank, which predicts an 8% GDP growth for the country next year. The fastest growing province in China is currently Guizhou, which reported a remarkable double-digit growth of over 20% in 2012.

In addition, China's growth is supported by robust policies that aim to move China towards a quasi-capitalist industrial base that houses high-value industries – like IT, cleantech and service businesses, as opposed to low value manufacturing – and freer market trading environments. Furthermore, the nation's lawmakers are consciously migrating the country’s industrial hubs westward – beneficiaries include outlier cities like Bijie, and its county, Jinsha, which is quickly becoming the heartland of Guizhou Province.

The introduction of high-value industries in such places is significant. Not only do they provide employment opportunities for local workers, but they also pay more and create greater disposable income for these urban residents, which in turn has a direct impact on domestic consumption, including spending on residential properties and tourism.

China is a fast urbanising nation, targeted to reach 70% by 2030

Since the 18th National Congress of the Communist Party of China, the nation’s approach to urbanisation has become a top priority and been raised to the level of national strategy. In this context, urbanisation relates to the physical growth of urban areas as a result of rural resettlement into modern houses and increasing suburban concentration, as well as the processes by which rural residents migrate to live and work in cities and suburban towns. Effective urban planning places equal emphasis on large cities, medium-sized cities, satellite suburbs and large towns.[6]

Urbanisation is a lengthy process. It can be divided into an initial period with an urbanisation rate of less than 30%; a development period with the rate between 30% and 70%, and mature period with a rate surpassing 70%. A post-rural society can be divided into four types: a low-level urbanised society with an urbanisation rate between 51% and 60%; a mid-level urbanised society with a rate from 61% to 75%; a high-level urbanised society with a rate from 76% to 90%; and a completely urbanised society with a rate exceeding 90%.[6]

This means that there are huge untapped opportunities for cities with urbanisation rates that are below China's current 50%; the lower the urbanisation rate, the greater the upside to be gained in terms of housing demand and domestic consumption.

China's urbanisation is currently in a critical transition period, having achieved a 2.8% CAGR in urbanisation ratio between 2001 and 2012. A United Nations report on World Urbanisation Prospects predicts that China will maintain a relatively fast rate of urbanization between now and 2030, when the level of urbanization will reach 65-70%. Many domestic and international research institutions and experts have made similar predictions. The Chinese government estimates that 60% of its population will live in urban areas by 2020, compared with about 53% last year. This translates to 115 million new urban residents, a Deutsche report states.[7]

At present, more than 10 million rural residents move to the city each year in China. It is expected that in the medium- to long-term, China’s urban population will increase by approximately 300 million, which is the equivalent of the entire population of the United States, said Chinese Premier Li Keqiang at a seminar of cadres at the provincial and ministerial level on promoting urbanisation, organised by the Central Organization Department, Chinese Academy of Governance, and the National Development and Reform Commission in September 2012.[8]

With these signs of growing housing demand, Cedar Strategic Holdings Ltd (CSH) is making strategic investments into China's residential market by beach-heading into the fast growing Jinsha County and Bijie City of Guizhou Province.

Guizhou Province is the fastest growing provincial economy in China

Located in southwest China, Guizhou Province adjoins Sichuan and Chongqing to the north, Yunnan to the west, Guangxi to the south and Hunan to the east. It is a picturesque place with abundant natural and cultural scenic spots, and has in recent years enjoyed rapid development.

Data from the China’s Statistical Yearbook 2013 shows Guizhou Province as the fastest growing provincial economy in 2012 with a growth rate of 20.2%. For the first three quarters of 2013, Guizhou tied for first place with Tianjin, with a growth rate of 12.6%, followed by Chongqing, with a growth rate of 12.4 percent.[9]

Bijie City's remarkable GDP growth spurring strong demand for housing

Located in the northwest of the Guizhou Plateau, Bijie borders the Sichuan Province and Yunnan Province, and is now part of a nationwide economic campaign known as the "Great Western Expansion", initiated by the central government. In accordance to the Bijie-Dafang City Planning 2010-2030 programme, plans and construction are underway to upgrade aged infrastructure, improve the natural environment and strike a harmonious balance between urban and rural areas.

Related to the programme and by virtue of its prime geographical position, there are plans to help develop and transform Bijie into a regional transportation and logistics centre in the intersection of Sichuan, Chongqing and Guizhou, serving China's southwestern region. The city opened its first and new RMB1 billion-airport, Bijie Feixiong Airport, on 16 June 2013.[10]

Home to the Guizhou-Bijie Economic Development Zone, Bijie City stands to benefit greatly from China's present and future trajectory, which is quickly attracting high-value and service orientated business, and boasting attractive demographics.

Bijie's economy has experienced a remarkable growth in recent years. The nominal GDP increased from approximately RMB40.3 billion in 2008 to RMB87.8 billion in 2012, representing a CAGR of 21%.[11] While the 6.5 million registered population of Bijie has remained stable in recent years, demand for residential properties has been strong, owing to robust economic growth, urbanisation, increasing number of migrants and rising incomes of city residents. Bijie's disposable income per urban resident increased from RMB11,094 in 2008 to RMB19,243 in 2012; a CAGR of 15%.[12]

Bijie City is Guizhou's next property market beacon

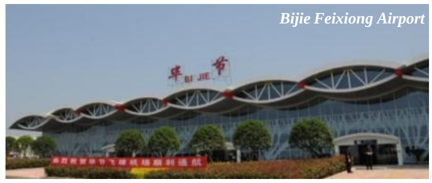
Bijie's residential market is largely supported by owner-occupation demand, either from first-time buyers comprising of young residents and migrants, or from family buyers for multiple uses or upgrade purposes. As a major city in Guizhou Province, Bijie is expected to experience a higher urbanisation rate in the near future, which will further boost property demand.

Notably, Bijie's urbanisation process is at a significantly slower rate than the national average, representing a greater growth potential. China's urbanisation rate stands at around 50%, whereas local authorities have advised CSH that the current rate stands at just over 30%. Bijie is striving to push the urbanisation rate to 45% by 2020[12], therefore allowing room for growth in a more sustainable manner.

From a property perspective, the number of unsold units is much lower in Bijie when compared to the likes of Beijing, Shanghai, Shenzhen or Guangzhou, where the supply of value-for-money housing in prime locations is limited. Local intelligence states that inventory on hand is little and completed projects are 95% sold, if not almost 100%.

Property in Guizhou Province is generally affordable to the common man, particularly among the nation’s growing middle-class consumers that live in these areas. Data collated by E-house China R&D Institute benchmarking Guiyang, capital of Guizhou Province, to Beijing, Shanghai, Shenzhen and Guangzhou, shows the affordability of housing to average 7-times annual income, relative to 11-times to 19-times in the four first-tier cities. Officials in Bijie say the ratio of home prices to annual income in the city to be about 5-times, with the appetite for new homes strong; new builds and/or housing demand is conservatively estimated to be around one million sqm per year.

Assuming 20% of the 6.5 million Bijie population urbanises in the next ten years, and for a family of four, there will be demand for some 325,000 new homes each year.


Bijie Feixiong Airport

With an average home measuring 100 sqm, this translates to a demand of 3.25 million sqm of GFA to be built and sold each year! This number could possibly be higher as local intelligence suggests officials are aiming for a take-up rate of 4 million sqm of GFA per annum.

From a developer's perspective, the return on investment is attractive, coming in between RMB1,000 and RMB1,200 psm of profits, representing approximately 28% and 33% of the average property price of RMB3,600 psm in Bijie. This compares favourably to what an investor can earn in tier-one cities like Beijing, Shanghai, Shenzhen or Guangzhou, where land and construction costs are considerably much higher.

An added factor to consider is the role of property ownership in China. Property is considered the most prized asset in the Chinese culture. And, unlike potential owners in the West that may have other priorities, buying a property is a *must* for the Chinese.

First-mover advantage enables CSH to cherry-pick

Leveraging on our wide network in China, CSH enjoys first-mover advantage as a trusted Singapore brand, and in working with reputable state-linked construction firm, China Gezhouba Group Company Limited, the company is well-positioned in the property market of Bijie City – differentiated by our affordable and well-designed quality housing and amenities, as well as providing Singapore-style post-sales services, particularly in estate management and value enhancement, hence instilling confidence in the market about CSH.

With the option to acquire over 4 million sqm of residential & commercial GFA in Guizhou, we are relooking at our capital structure, cash flow and the availability of low-cost funds, so as to seize upon this tremendous opportunity to deliver value-for-money properties with a higher rate of return.

The Chinese idiom *Tian Shi Di Li Ren He* (天时地理人和) loosely translates to mean the stars are aligned; the odds are in our favour.

It is very hard, if not impossible, for China's property market to collapse. The property sector and its related industries, including the banking sector, when taken in totality, are much too big to fail. Southwest China, in particularly places like Jinsha County and Bijie City, will shortly emerge as the hotspot(s) of China's next development cycle.

CSH believes that the window to enter the Bijie property market is now, begetting the question: how should CSH calibrate between risks and rewards, supply and demand, and the availability of low-cost funding?

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3 *“Chinese cities expected to ease property regulations”, Xinhua, 19 May 2014*
4 *“U.S. GDP grew 2.6% in the Fourth Quarter 2013, up from last estimate”, Forbes, 27 March 2014*
5 *“Eurozone GDP growth gathers speed”, BBC News, 14 February 2014*
6 *“New Approaches to China's Urbanisation”, China Today, 16 August 2013*
7 *“China ‘still a sound place to invest’”, The Straits Times, 25 May 2014*
8 *“Promoting Coordinated Urbanisation – an Important Strategic Choice for Achieving Modernisation”, Speech by Li Keqiang (CPC Political Bureau Standing Committee member and now Premier of the PRC since March 2013), 7 September 2012*
9 *“Top 10 fast-growing provincial economies in China”, China.org.cn, 22 December 2013*
10 *“Bijie Feixiong Airport opens its first air route”, China Daily, 21 June 2013*
11 *“Property Market Research Report on Guiyang, Zunyi, Kaiyang, Liupanshui, Bijie and Wanzhou” by Jones Lang Lasalle (Hong Kong) dated 25 October 2013 commissioned by Cedar Strategic Holdings Ltd.*
12 *“Bijie hits gas on road to prosperity under 8-year plan”, China Daily, 12 March 2013*

About Dr In Nany Sing Charlie

Dr In has extensive experience in business management, capital sourcing, consulting, marketing, mergers and acquisitions, and was instrumental in arranging the public listings of several PRC Companies. He is the first Singaporean to be honoured by the British Chinese Youth Federation at the 2010 Golden Mulberry Award as the “Most Respected Financial Writer of the Year” in the Business/Finance sub-category of The Big Ben Award.

Previously the Chairman of Direct Marketing Association of Singapore, Dr In served as an advisor to Asia Pacific Management Institute, Sapphire Corporation Limited, Sky China Petroleum Services Ltd and Ying Li International Real Estate Limited. He was also an adjunct faculty member of the Singapore Institute of Management for 20 years, and 17 years at the University of South Australia. He is currently the advisor to Talent Advisory Panel of the People’s Association in Singapore.

Dr In holds a Masters in Business Administration from the University of East Asia and a Postgraduate Diploma in Direct Marketing from ADMA/Macquarie University Australia.

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