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ANALYZING CHINA'S REAL ESTATE BUBBLE

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ARTICLE DETAILS

ABSTRACT

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This paper is focusing on the topic of the bubble inside of China's Real Estate market. China's Real Estate market has been developed rapidly from the past forty years. In order to figure out whether there is a bubble inside this market, in other words, whether the housing and renting are over-valued, data and historical events that happened in other countries are being used to compare and contrast to figure out the bubble.

KEYWORDS

China's Real Estate market, rapidly, bubble, over-valued.

1. INTRODUCTION

In 1980, real estate was defined by the government as a commodity for the first time in China. This was also the start of the real estate market. The following ten years were harsh for China's real estate, since the government witnessed the housing bubble and started to control it [1]. Up until today, the government is still working on controlling the real estate market by implementing certain policies and limiting top enterprises. Despite their efforts, however, large cities such as Shanghai and Beijing are still famous for shockingly high renting and housing prices. Large amounts of people, even those with decent jobs, can not afford their own houses and have to obtain bank loans. The real estate market's future therefore, is full of questions: Will making real estate less commercial and more based on true value work for the majority in China? Is the market today a bubble? This research mainly focuses on whether China's real estate market is, in fact, a bubble or not.

China's real estate value have been changing over the past forty years due to the government's reforms and policies. Before 1978 in China, land was owned directly by the government, and the government distributed houses. For example, during the Great Leap Forward period, most peasants live in communes, where everyone live together in one huge house that was built by the Communist Party, the government. There was no value given for that real estate and, therefore, no real estate market yet. The government started to accommodate policies during the economic reform around 1978, and people were allowed and even encouraged to purchase their own houses, which directly boosted the real estate prizes. For instance, a lot of businessmen saw the opportunities in Hainan, south of China, and went there in what became the catalyst to the very first trend of private real estate construction and sales. In this second time period, real estate had been defined as commodities, which greatly related to the reason why the prizes bloomed. Houses were mostly controlled by businessmen, and with advertisements that sparked people's desires, and houses rapidly rose over its true value. While the market grew rapidly, the government aimed for fairness. Therefore, two policies Economically Affordable Houses and Housing Provident Funds, were launched [1].

1.1 Methods to Define a Bubble

To define whether there's a bubble in China's real estate market, the most fundamental step is to define the true value of the real estates. In other words, we must determine how houses' prizes should be appropriated. However, the definition of true value seems to be overlooked. Many reports recorded the real estates simply as being "overvalued" in the market while not defining the value of the houses or for renting. This was caused by a variety factors involved in this market, and people take the factors into account differently, therefore there's no such "true value" is commonly agreed upon. However, if observing the real estate from its original and basic usage, it originated from the need of the public. Most of the houses were built for people's living. When people view the value of buildings as goods, they tended to build mass quantities of construction that were impossible to be consumed. For instance, when the policies first launched in the 1980s, a large number of businessmen went to Hainan and built thousands of houses. Later, they realized there were too many houses. Therefore, many house that were in construction were left behind and caused a large problems in the local neighborhoods. In order to avoid similar situations from happening again, real estate's fundamental value should be based on people's needs, as its main usage is to provide shelters for the public. The commercial side of its value should come second, after fulfilling the need of the people.

Whether there's a bubble in the real estate market has been a popular topic as there are plenty of ways to model a bubble. According to *IVESTOPEDIA*, a housing bubble is "a run-up in housing prices fueled by demand, speculation and exuberance." This site also points out that these bubbles usually "start with an increase in demand, in the face of limited supply;" the term "housing bubble" is defined as a "temporary condition caused by unjustified speculation in the housing market that leads to a rapid increase in real estate prices;" while economist Robert Shiller lists seven factors that define a bubble: "Sharp increases in the price of an asset like real estate or dot-com shares... A decline in lending standards." [2]. While this research varies from each other, there are also crucial similarities among these three different opinions: they all mention how the prizing boost rapidly or abnormally is a sign of the housing market's bubble, which fits China's real estate situation perfectly [3,4].

2. MAIN TEXT AND TABLE

While taking the rapid price change as a factor to determine whether there's a bubble, it would also be helpful by compare it to other bubble instances in different countries, such as the United States and the United Kingdom, to help analyzing the bubble. Also, compared to Japan and

Thailand, two other Asian countries that used to have real estate bubbles, it will provide historical evidence to help determine whether there is a bubble in the market [5].

According to the *National Data: National Bureau of Statistics of China* website, China's real estate value have been increasing for twenty years.

Table 1: China's Real Estate Value Percentage in Total GDP

Time(year)	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006
Total GDP (hundred million)	79715.0	85195.5	90564.4	100280.1	110863.1	121717.4	137422.0	161840.2	187318.9	219438.5
Real Estate Value (hundred million)	2921.1	3434.5	3681.8	4149.1	4715.1	5346.4	6172.7	7174.1	8516.4	10370.5
Real Estate Value Percentage	3.66%	4.03%	4.07%	4.14%	4.25%	4.39%	4.49%	4.43%	4.55%	4.73%

Time(year)	2007	2008	2009	2010	2011	2012	2013	2014	2015	2016
Total GDP (hundred million)	270232.3	319515.5	349081.4	413030.3	489300.6	540367.4	595244.4	643974.0	689052.1	743585.5
Real Estate Value (hundred million)	13809.7	14738.7	18966.9	23569.9	28167.8	31248.3	35987.6	38000.8	41701.0	48190.9
Real Estate Value Percentage	5.11%	4.61%	5.43%	5.71%	5.76%	5.78%	6.05%	5.90%	6.05%	6.48%

From the upper two charts, it is obvious that the percentage of the real estate value have been increasing gradually over these twenty years. Until 2016, the percentage of real estate value has almost doubled compared to the value in 1997. However, according to the *National Association of House Builders*, the residential investment, in the United States is averaging approximately 3% to 5% of GDP [5]. In 2017, real estate construction contributed 6% to the United States GDP [2]. This comparison between China and the United States, both with a large economic output, shows that China's real estate value is obviously higher, which indicates a bubble in the market.

While looking at the China's real estate value specifically in its percentage in GDP, it is also obvious when taking the historical instances and comparing them with the situations nowadays in China. For example, Thailand had a major collapse of its housing market in 1997 due to the economic crisis. According to the research, there's a similarity between the Thailand housing market and Chinese housing market: the overproduction of houses. The overproduction of housing created excess supply, while developers were reluctant to lower housing prices to clear the market [6]. This is a phenomenon very similar to the China's real estate market. As mentioned earlier, this had already happened once in Hainan province, and it hasn't disappeared yet. Due to reluctant developers, a large amount of people in China couldn't afford housing while the advertisement of newly built estates could be seen everywhere in cities.

3. CONCLUSION

China's Real Estate Market has been developing for forty years since 1978 when the policies were reformed. Due to the growing economy, the

housing market has been continuously expanding as well. However, except the growing economy that resulted in the increasing housing demand of people, the market has also been overvalued. By analyzing and compared with both the temporary United States' housing market situation and the historical bubble in Thailand housing market, it can be determined that there's a bubble in China's real estate market. The bubble isn't fully uncontrolled though, as Chinese government had released a series of policies to make an effort to restrict the rapid growth of real estate prices.

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