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[Back to Publications List](#)

China's Housing Market: A Policy Assessment and Outlook for Wood Consumption

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Executive Summary

Prior to the 1980's, the government provided its citizens with public housing. As a consequence, there was a lack of investment in this sector. State-Owned Enterprises (SOEs) were responsible for providing its workers with an apartment or other housing unit. SOEs allocated apartments under a series of rigid administrative regulations that resulted in a rental market with artificially low rents, no home ownership and average living space per capita that was less than 4 m². These conditions led the Chinese government to consider housing reforms by the end of the decade.

During the 1980's, along with other aspects of their economic system, China started to reform its urban housing sector. The housing reforms increased investment in the private (also known as commercial) and public (also known as non-commercial) housing sectors. As a result of these reforms, there are roughly 1 million annual housing starts today. The average living space is 8-10 m², with a goal of 12m² by the year 2010. So far, the housing reforms are focused mainly in the cities of Beijing, Tianjin, Shanghai and those in Guangdong Province.

The introduction of reforms has produced a dual-housing system in China. One segment of this dual system is the SOEs, which continue to provide the majority of housing to its employees. The other segment is the private housing sector, which operates in a more conventional, open housing market. Eventually China hopes to eliminate this dual-housing system. To do so additional market mechanisms must be undertaken to further develop an open, competitive housing market. These mechanisms involve reforms to price setting mechanisms that set current home sale prices and government-set rents.

An important consideration will be a households' income in establishing market price setting mechanisms. The recent reforms have led to two problems. One is that the price on the 'open housing market' is too high to be affordable by average urban residents. As a result there is currently an overstock of newly built housing that was constructed for affluent households. The other problem is that government-set rents can't be raised to market levels without a significant wage adjustment. Thus wage reform will be just as important for housing reform to be successful.

Housing reforms will need to be monitored along with other economic reforms in China. SOEs still control much of the urban housing stock—i.e. the majority of housing is in the public, non-commercial housing sector. The reliance of employees on their work units for their housing needs has not fundamentally changed under the reforms undertaken to date. Successful housing reforms will depend on the reform of SOEs. Wage and housing reforms, and controlling unemployment are a part of much larger and more complicated SOEs reforms. In large part, SOEs reforms will be key for housing reforms to be successful.

It is estimated that housing reforms generated \$80 billion in new household-related spending in 1998 (9% of GDP) and \$150 billion in 1999. However, housing reforms are major undertakings, which will gradually, rather than immediately, bring opportunities for foreign firms. Continued success in generating economic activity will promote further reforms.

China's prediction of 10% annual growth in domestic demand over the next ten years may be over-optimistic, but disposable income has increased by an average of 6% in urban areas over the last five years, and 5.4% in rural areas. A continued growth in income is likely to have a substantial effect on the domestic demand for wood products, hence the outlook for a growing market in China for wood products is optimistic.

Rising incomes among China's emerging middle class, many of whom still live in accommodations provided by their employer, has also raised spending levels on furniture and interior wood products. Demand will initially depend on affluent families that can afford a home purchase and separation from SOEs housing subsidies. As more middle class families become affluent, they also will likely renovate existing units or move into new apartments. Those dependent on heavily subsidized state housing are not likely to contribute much to any potential increase in wood products demand, however. Hence the transition to a western-style housing market is likely to be slow and intimately coupled with wage reforms and the transformation of SOEs to competitive industries. As this happens, over the next several years, demand will grow for higher quality products such as flooring, molding, windows, doors, cabinets, paneling, wall units and furniture. It is expected that consumption of these products will develop into a significant market following these transitions.

Over the last decade and more, China's furniture industry has attained unprecedented development; its output during the period 1986-1997 had developed from 120 million pieces to 476 million pieces, with an average annual increase of 39.8%. Total output value of the industry as of 1998 reached 78 billion RMB and then in 1999 with growth rate to an estimation of 12%. Timber is an important raw material for the furniture industry. A large furniture sector will depend more heavily on imports of timber.

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Back to [Publications List](#)