SHOULD FOREIGN REAL ESTATE INVESTMENT BE CONTROLLED IN CHINA?

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ABSTRACT

Housing prices in China has been increasing rapidly in recent years. While local speculators are blamed for the escalating house prices, foreign real estate investors are also regarded as accomplices for causing the problem. New measures known as the Opinions on Regulating Market Access and Management of Foreign Investment in China’s Real Estate Market were introduced to restrict foreign real estate investment in the country. This paper attempts to examine the justification of the control and its impact on foreign investors. The investigation shows that foreign real estate investment is a tiny portion of the total real estate investment in China and has not cause a threat to the market. The scale of foreign investment does not justify the introduction of the controls.

Keywords: Real estate market, foreign investment, house prices, control measures

INTRODUCTION

Foreign real estate investment in China has a long history and can be dated back to over a century ago when foreign powers such as America, Britain, France, Germany, Italy, Russia and Japan, etc. set up occupied territories in China (Chan & Jia, 2001). Foreign real estate investors retreated after the communist government took power in 1949. The real estate market then went into hibernation when all private real estate assets were subsequently confiscated and vested in public ownership. It was eventually revived after the introduction of the ‘open door’ economic reform policy in 1978, and foreign investors were welcomed back.

At the beginning, foreign investors were mainly overseas Chinese from Hong Kong, Macau, Taiwan and other countries in the region. Their success soon attracted investors from other countries to jump on the bandwagon in the 1990s (Zhang, 2002). The amount of foreign direct investment (FDI) increased rapidly. Since 2002, the inflow of FDI in China has exceeded US$50 billion, surpassing the United States as the largest recipient of FDI inflows in the world (OEDC Observer, 2003).
The influx of FDI also led to an increase in real estate investment in China. Real estate prices went up rapidly along with the booming economy. The escalating real estate prices however had a temporary set back in 1993 after the introduction of the macro economic control policy. Afterwards, prices began to rise again. Between 1997 and 2004, there was a 42.40% increase in commercial house prices and 28.85% increase in affordable house\textsuperscript{1} prices (NBSC, 2005).

The rocketing house prices worried the people and the central government. Various measures had been introduced to stabilise house prices. The latest round of control measures was introduced in May 2006 when the Premier Mr. Wen Jiabao announced 6 major policies (the so called State Council’s 6-point policy) to cool off the over-heated housing market.

While local speculators were blamed for the escalating house prices, foreign real estate investors were also regarded as accomplices for causing the problems. On 24 July, 2006, a 14-point policy document *Opinions on Regulating Market Access and Management of Foreign Investment in China’s Real Estate Market* was introduced to restrict foreign real estate investment in the country. This new control policy was reported worldwide and caused a lot of concerns among foreign investors. There is no doubt that China has the right to control foreign real estate investment in the country; however, there is query if the control is justified.

This paper attempts to examine the justification of the control and its impact on foreign investors. It provides an overview of the growth of foreign real estate investments in China, the amount of foreign real estate investment and its contribution to high house prices. There is an analysis of the new control measures and the newly passed *Property Rights Law*. A conclusion is provided at the end of the paper.

**METHODOLOGY**

The paper will firstly look at the inflow of FDI into China since the adoption of the ‘open door’ policy. Statistical figures of FDI inflow, growth of GDP and foreign exchange reserves will be studied. This is followed by a study of statistical figures of foreign real estate investment in China. The changes of the funding of foreign real estate investment according to the economic policy will be looked at.

In order to find out if the recent control of foreign real estate investment is justified, it is necessary to look at the amount of foreign funded real estate investment and the increase of foreign real estate investment firms in recent years. Statistical figures in recent years will be used to work out the ratio of the amount of foreign funded and domestically funded.
funded real estate investment, and also demonstrate the market share of foreign real estate firms in China.

FOREIGN INVESTMENT IN CHINA

China opened up itself to the world in 1978 when it adopted the ‘open door’ policy to reform the economy and modernise the country. The Chinese-Foreign Joint Venture Law was passed in July 1979 to attract foreign investments (Zhang, 2002). Since 1980, special economic zones were set up in Shenzhen, Zhuhai and Shantou in Guangdong Province and Xiamen in Fujian Province, and the entire province of Hainan was also designated a special economic zone. In 1984, the so-called gold coast of China was established when 14 coastal cities—Dalian, Qinhuangdao, Tianjin, Yantai, Qingdao, Lianyungang, Nantong, Shanghai, Ningbo, Wenzhou, Fuzhou, Guangzhou, Zhanjiang and Beihai—were further opened to overseas investment (China in Brief, 2000). In 1986, other measures such as preferential tax policies were introduced to encourage more investment.

Within the first 5 years (1979 – 1984) of accepting foreign investment, the total actually utilised foreign direct investment (FDI) was US$4.1 billion (NBSC, 2006). Thereafter, the amount of FDI increased dramatically. Since 2002, the annual inflow of FDI in China has exceeded US$50 billion, surpassing the United States as the largest recipient of FDI inflows in the world; see Figure 1 below (OEDC Observer, 2003).

Figure 1: Foreign direct investment in China and the US

![Figure 1: Foreign direct investment in China and the US](image)

Source: OECD

Figure 2 below shows the amount of actually utilised FDI in successive years from 1985 – 2005. It can be seen that the rapid growth of FDI lost steam in 2000 when China’s deflation problem reached the climax. It started to pick up again in 2001. In 2001, China joined the World Trade Organization (WTO). After joining the WTO, the rapid growth of FDI continued and China has attracted more than US$248 billion in foreign direct investment (Bloomberg News, 2006). In 2002 -2006 the country's average annual economic growth was over 9% (ANZ Economic Outlook, 2005 & 2006).
The adoption of the economic reform policy in the late 1970s has seen China attract enormous amounts of FDI and enjoy outstanding economic growth. In addition to fast annual growth in GDP, the annual growth of foreign exchange reserves (FER) is even steeper; see Figure 3 below. In 1981, the country only had a small FER of about US$27 billion. In 2005, it was over US$800 billion (NBSC, 2006). In the first quarter of 2007, it increased to around US$1202 billion (Financial Times, 2007). These two economic indicators alone are strong enough to attract more foreign investment funds into China. Financial Times (2007) reported that “$25bn of funds have flowed into China every month so far this year.”
Regarding the real estate sector, the market was overheated in early 1990s. The influx of investment capital led to a booming economy. In 1992, the GDP rose to 14.2% (Yu, 2001) and hundreds of billions of Yuan (tens of billions of US$) flooded the coastal cities. The resulting rising real estate prices triggered the nerve of the central government and were subsequently cooled off by the macro economic control measures introduced in 1993. The impact from the macro economic control and subsequently the Asian financial crisis caused China to enter a period of deflation. Consumer prices index began to drop in 1995 and peaked in 2000 (NBSC, 2006). The tough investment atmosphere led to a decline of operation profit in real estate enterprises, see Table 1 below:

**Table 1: Operating profit of real estate enterprises**

<table>
<thead>
<tr>
<th>Year</th>
<th>Operating Profit (US$ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1996</td>
<td>216</td>
</tr>
<tr>
<td>1997</td>
<td>-125</td>
</tr>
<tr>
<td>1998</td>
<td>-129</td>
</tr>
<tr>
<td>1999</td>
<td>-424</td>
</tr>
</tbody>
</table>

Source: NBSC, 2006, Table 6-40

The poor real estate market condition led to a decrease of foreign real estate investment funds in 1997 - 2001, see Table 2 below:
Table 2: Change of foreign real estate investment 1997 – 2001 (Amount in 10,000 Yuan)

<table>
<thead>
<tr>
<th>Year</th>
<th>Investment Using Foreign Fund (US$ billion)</th>
<th>Foreign Direct Investment (FDI) (US$ billion)</th>
</tr>
</thead>
<tbody>
<tr>
<td>1997</td>
<td>4608565</td>
<td>3279010</td>
</tr>
<tr>
<td>1998</td>
<td>3617581</td>
<td>2588698</td>
</tr>
<tr>
<td>1999</td>
<td>2566022</td>
<td>1804807</td>
</tr>
<tr>
<td>2000</td>
<td>1687046</td>
<td>1348026</td>
</tr>
<tr>
<td>2001</td>
<td>1357044</td>
<td>1061150</td>
</tr>
</tbody>
</table>

Source: NSB, 2006, Table 6-33

In the above table, FDI is a subset of Foreign Funded Investment. It can be seen that the amount of real estate investment using foreign funding dropped from US$5.55 billion in 1997 to US$1.64 billion in 2001. At the same time, the amount of FDI in real estate dropped from US3.96 billion to US$1.28 billion. The retreat of foreign funds was very substantial.

The central government was alerted by the unfavourable economic condition and introduced various measures to strengthen the economy. The interest rate was adjusted downward, macro control measures were relaxed and the real estate market was given a chance to recover. The biggest boost to the economy was China’s accession to the WTO in 2001. With the improving economy and the real estate market became more active; the operating profit of real estate enterprises also improved, see Table 3 below.

Table 3: Operating profit of real estate enterprises

<table>
<thead>
<tr>
<th>Year</th>
<th>Operating Profit (US$ million)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>885</td>
</tr>
<tr>
<td>2001</td>
<td>1516</td>
</tr>
<tr>
<td>2002</td>
<td>3056</td>
</tr>
<tr>
<td>2003</td>
<td>5200</td>
</tr>
<tr>
<td>2004</td>
<td>10366</td>
</tr>
<tr>
<td>2005</td>
<td>13540</td>
</tr>
</tbody>
</table>

Source: Source: NBSC, 2006, Table 6-40

The improving economy and potential huge investment return attracted foreign investors to increase their investment in real estate again, see Table 4 below.
Table 4: Change of foreign real estate investment 2001 (Amount in 10,000 Yuan)

<table>
<thead>
<tr>
<th>Year</th>
<th>Investment Using Foreign Fund (US$)</th>
<th>Foreign Direct Investment (FDI) (US$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>1357044 (1.64 bn)</td>
<td>1061150 (1.28 bn)</td>
</tr>
<tr>
<td>2002</td>
<td>1572284 (1.90 bn)</td>
<td>1241285 (1.50 bn)</td>
</tr>
<tr>
<td>2003</td>
<td>1700040 (2.05 bn)</td>
<td>1162667 (1.40 bn)</td>
</tr>
<tr>
<td>2004</td>
<td>2282001 (2.76 bn)</td>
<td>1425587 (1.72 bn)</td>
</tr>
<tr>
<td>2005</td>
<td>2578111 (3.15 bn)</td>
<td>1714093 (2.09 bn)</td>
</tr>
</tbody>
</table>

Source: BSB, 2006, Table 6-33

It can be seen that the amount of real estate investment using foreign funding and FDI had been increasing since 2001. The majority of foreign real estate investment is in Shanghai. Figure 4 below shows the distribution of foreign real estate investment in China in 2005.

**Figure 4: Distribution of foreign real estate investment**

![Figure 4: Distribution of foreign real estate investment](source)

Source: Latitude, quoted by Zhang, 2007

In the first half of 2006, newly established foreign-invested real estate enterprises increased by 25.4% over the same period of previous year. The amount of foreign capital actually utilised was up 27.9% (Xinhua, 2006). DTZ, an international property advisor, reported that foreign investors spent US$4.5 billion in the first quarter of 2006, exceeding the amount for the whole of 2005 (China Daily, 2006).
CONTROL OF REAL ESTATE INVESTMENT

Since 2000, real estate prices, particularly in the housing sector, have gone up significantly. In the big cities, the growth was over 50%. In the first half of 2006, the average house prices in 70 medium-large cities increased by 5.8%. The biggest price changes were in Shenzhen (14.6%), Beijing (11.2%), Xiamen (11.1%), Hohhot (10.4%), Baotou (10.3%) and Guangzhou (10%); disregarding the central government’s previous measures in restraining house prices. Only 2 cities had recorded price drop – Shanghai (5.4%) and Jinzhou (0.5%) (Soufun, 2006).

The price drop in Shanghai and Jinzhou was out of line with other cities. There was no clear reason for the disparity. One speculation was that the statistical figures of these two cities were based on different sampling assumptions. Another reason could be that Shanghai is a municipality under the direct control of the central government. Hence it has to implement the central government’s directives with full force. In contrast, Jinzhou is an industrial city in Liaoning Province in north-east China. The investment environment there may not be as attractive as other cities to real estate speculators.

House prices continue to rise through 2006 to 2007. Figure 5 below shows the price movement of residential real estate in Beijing, Shanghai, Guangzhou and Shenzhen up to the second quarter of 2007.

Figure 5: Residential price index

![Residential Price Index of Beijing, Shanghai, Guangzhou & Shenzhen](image)

Source: DTZ (2007)
The unruly housing price had seen the central government introduce a number of control measures in the past. However, the result was far from satisfactory. In May, 2006, the Premier Mr. Wen Jiabao introduced 6 major policies (the so called State Council’s 6-point policy) to cool off the over heated housing market.

Local developers and speculators are regarded as the culprits for the escalating house prices and are targeted by the 6-point policy package. This policy package covers 6 main areas:

1. Adjusting the structure of housing supply. The emphasis is on the development of middle-low price and medium-small size commercial housing, affordable housing and low rent housing. Local governments are required to establish and implement housing development programs, and ask for the proportion of medium-small size residence in new residential development.

2. Further developing the regulatory functions of tax, credit and land policies. It requires strict implementation of policies for housing development and sales, and perfection of tax policy on housing transactions. Credit policy needs to be discriminately and appropriately adjusted to guide and regulate demand for housing. The scale of land supply for development should be determined scientifically. Land use supervision should be strengthened to prevent land hoarding.

3. Rationally control the scale and progress of demolition of old houses in urban areas so as to slow down the rapid growth of derived demand for housing.

4. Further rectifying and regulating real estate market order. It requires the strengthening of supervision of the whole process of real estate development so as to stop unauthorised alternation of projects, illegal transactions, hoarding of housing resources and manipulation of prices.

5. Expediting the establishment of low rent housing system in urban areas, standardise the development of affordable housing, positively develop second hand housing market and rental market, and gradually resolve the accommodation problems of low income families.

6. Perfecting the disseminating system for real estate information and statistical data. It requires market supply and demand information to be released accurately, totally and on time. It also requires correct public opinion to be upheld.

To implement to 6 major policies, the following actions are taken by the relevant authorities:
1. All urban people’s governments are required to include housing construction in their 11th five-year (2006 – 2011) program. In particular, they should include the construction target for ordinary commercial housing, affordable housing, and low rent housing in 2006 and 2007 into the program and publish it by the end of September 2006.

From June 1, home units smaller than 90m² must account for at least 70% of the total floor space in any new residential projects.

2. As a measure to discourage speculations, from 1 June 2006, a transaction tax will be imposed on the sale price for property owners who resell their ordinary homes² within five years of purchase. Previously the grace period was two years. The tax rate will stay unchanged at 5.5% of the sale price. For individuals who sell their non-ordinary homes after 5 years, a transaction tax based on 5.5% of the difference between the sale price and the purchase price is levied.

3. Developers have to provide 35% funding from their own capital for any project before they can seek loans from commercial banks. Commercial banks are required to be cautious when dealing with development funding or rolling credits for developers who have a large amount of idle land or vacant commercial housing units. Commercial banks are not allowed to accept commercial houses that have been vacant for over 3 years as collateral.

4. From June 1 2006, individual home purchasers need to have a down payment of at least 30%. For those who are buying a home smaller than 90m² for their own occupation, the down payment rate remains 20%.

5. All urban people’s governments have to prepare annual land use program and to guarantee that the land supply for medium-low price, medium-small size commercial housing, affordable housing and low rent housing is not less than 70% of the housing land supply. Land supply for development of villas and the like remain prohibited. Land supply for low density or large size housing developments is highly restricted.

The relevant governments are required to use a fixed portion of the proceeds from sales of land use rights, and with the support from other government finance, to build low rent housing. A considerable scale of construction of this type of housing has to be commenced by the end of 2006.

6. Urban people’s governments are required to promulgate clearly the scale of construction of low rent housing in 2006 and 2007 before the end of 2006.

² Homes with floor area of 144m² or less
CONTROL OF FOREIGN REAL ESTATE INVESTMENT

As far as foreign real estate investment is concerned, the sharp increase in foreign investment in recent years has also worried the central government. Foreign real estate investors are regarded as accomplices for causing high house prices. In July, 2006, a 14-point policy document *Opinions on Regulating Market Access and Management of Foreign Investment in China’s Real Estate Market* was jointly released by 6 ministerial departments, including the Ministry of Construction, the Ministry of Commerce, the National Development and Reform Commission, the People’s Bank of China, The State Administration of Industry and Commerce and the State Administration of Foreign Exchange to control foreign real estate investment in the country. The document covers 4 main areas:

1. Entry of foreign investment to China’s real estate market;
2. Development and operation of real estate business by foreign invested enterprises in China;
3. Purchase of real estate by foreign institutions and individuals; and
4. Supervision of foreign investment in China’s real estate market.

Under the new control measures, overseas Chinese investors are also regarded as foreigners. On the whole, the policies aim at regulating, rather than restricting, foreign investment in the real estate market (People’s Daily Online, 2006). Foreign investors need to have a commercial presence in China and are required to obtain approval from the relevant authorities before setting foot on the real estate market. Among the various polices, those listed below have most significant impacts on foreign investors:

1. Only foreign businesses with offices in China (other than approved real estate enterprises) or foreigners who have worked or studied in China for more than one year can purchase commercial real estate for their own use. Purchase of commercial real estate not for their own use is not allowed. This measure will exclude foreign speculators from the real estate market.

2. Foreign investors must have a registered capital of at least 50% (i.e. 50% equity) for setting up a real estate investment enterprise valued at US$10 million or above. The requirement raises the bar for opening a real estate investment business in the country. Foreign firms are required to be financially sufficient for running big business in China.

3. Foreign investors cannot apply for loans locally or from overseas unless they have provided from their own resources, 35% of the funds needed for a development project. This is the same requirement for local investors under the
6-point policy. Both foreign and local investors are now subject to the same control.

**IS THE CONTROL JUSTIFIED?**

Apart from the sharp rise in real estate prices, the central government is concerned about that foreign real estate investment has been increasing at high speed in the past few years, see Table 5 above. In the first quarter of 2006, foreign investors spent US$4.5 billion in the real estate market of China, exceeding the whole of 2005 (China Daily, 2006). The number of newly established foreign-invested real estate enterprises increased by 25.4% in the first half of 2006, compared with the same period in the previous year. The amount of foreign capital actually used was up 27.9% (Xinhua, 2006). Foreign investors are regarded as accomplices for causing the escalating house prices.

Despite the amount of foreign capital inflow into the real estate market, the proportion of foreign investment is actually very small in relation to the total amount of real estate investment in China, see Table 5 below.

**Table 5: Proportion of foreign investment in China’s real estate market (10,000 Yuan)**

<table>
<thead>
<tr>
<th>Year</th>
<th>Investment using foreign funding (US$)</th>
<th>Total real estate development funding (US$)</th>
<th>% of foreign investment</th>
</tr>
</thead>
<tbody>
<tr>
<td>2001</td>
<td>1357044 (US$1.64 bn)</td>
<td>76963877 (US$92.99 bn)</td>
<td>1.76</td>
</tr>
<tr>
<td>2002</td>
<td>1572284 (US$1.90 bn)</td>
<td>97499536 (US$117.80 bn)</td>
<td>1.61</td>
</tr>
<tr>
<td>2003</td>
<td>1700040 (US$2.05 bn)</td>
<td>131969224 (US$159.44 bn)</td>
<td>1.29</td>
</tr>
<tr>
<td>2004</td>
<td>2282001 (US$2.76 bn)</td>
<td>171687669 (US$207.43 bn)</td>
<td>1.33</td>
</tr>
<tr>
<td>2005</td>
<td>2578111 (US$3.15 bn)</td>
<td>213978389 (US$261.21 bn)</td>
<td>1.20</td>
</tr>
</tbody>
</table>

Source: NBSC, 2006, Table 6-33

As far as the growth of foreign real estate enterprises is concerned, the real situation can be seen in Figure 6 below. The number of foreign real estate enterprises together with those from Hong Kong, Macao and Taiwan has never been a dominant force in the Chinese real estate industry. In 2004 and 2005, when the number of total real estate enterprises was the highest, they were still less than 10% of the total number of real estate enterprises in China.
The above analysis shows that foreign investment in China’s real estate market is by no means a threat. After all, foreign real estate investment is concentrated in big cities like Beijing and Shanghai and has not yet spread to other cities. Wayne Zane from Colliers International in Shanghai claimed that although competing foreign capital has driven up prices of investment grade commercial properties in Shanghai, foreign buyers only account for about 4% of all purchases in that city (Hudgins, 2006). Given the small size of foreign real estate investment, any claim that it is a threat is exaggerated.

The Chinese government has not publicly made known the reasons for the control. The following suggestions, although unofficial, may possibly be the reasons:

1. The Chinese government is a regime with strong affinity to regulation. Given the unruly nature of the real estate market, no doubt it wants to establish a system to control foreign real estate investment before problems arise.

2. China is under international political pressure to allow its currency to float against the US dollar to reduce its trade surplus. There is speculation that the Yuan will soon be floated freely (Crawford & Young, 2005). Vice Finance Minister Li Yong told participants at the annual meeting of the Asian Development Bank (ADB) in Istanbul that “One big concern to me is that too much hot money is flowing into China." (MoC, 2005). Hot money inflow reached 1.02 billion, 4.45 billion, 5.31 billion and 12.5 billion U.S. dollars in February, March, April and May 2006, respectively (MoC, 2006). The Chinese
government wants to control the inflow of hot money in anticipation of currency appreciation.

3. At present, a substantial amount of foreign investment has been absorbed by the real estate market. The Chinese government wants to channel more foreign capital to other areas of investment. This point is supported by the Ministry of Commerce’s guidelines in March 2007 that the Chinese government wants to encourage foreigners to invest more in service sector and high-tech companies while strictly restricting overseas investment in real estate projects (MoC, 2007).

Although foreign real estate investment is only a small proportion today, the increase in foreign investment will nevertheless fuel the already hot real estate market. The outlook of the Chinese economy and the real estate market has attracted more foreign real estate investment. In March 2006, Morgan Stanley announced that it would triple investment in Chinese property that year. Other big foreign investors such as CapitaLand and ING would also follow suit (Bloomberg, 2006). It appears that the vast supply of Western capital for real estate development has barely begun to flow into China (Kotler, 2007). The Chinese government considers that the control is necessary to help cool off the market.

4. While the control will cause inconvenience to genuine foreign investors, it helps stamp out speculators and create a healthy environment for real estate investment.

5. Before the introduction of the current control, China was one of the few countries among the 184 International Monetary Fund members without limitation on housing investment (People’s Daily Online, 2006).

A number of developed countries like Australia, Japan, Singapore, etc. already have measures controlling foreign real estate investment (Chang, 2003). For example, in Australia, foreigners are not allowed to buy second hand residential properties (Balanda, 2006). In Singapore, foreigners are not allowed to buy “landed” properties. That means properties with a garden, i.e. bungalows, semi-detached and terrace houses, including conservation shops homes are out of reach of foreign investors (Asiahomes, 2004). China’s control of foreign real estate investment is not at odds with other countries.

6. For political reasons, the Chinese government needs to show the people that foreign real estate investors do not enjoy privileges and are subject to regulations. Controlling foreign real estate investment will complement the implementation of the 6-point policy.
LIKELY IMPACTS ON FOREIGN INVESTORS

The new policies bring about a number of new controls on foreign real estate investment and the real estate market is bound to be affected. The likely impacts may include:

1. Foreign investors used to be prominent buyers for high end residential properties in China. Now they have to satisfy the residence requirement. In addition they are restricted to buy residential property for their own use only and the purchase cannot be for investment. This will significantly reduce the demand for high class residential property and the prices of this class of real estate are expected to fall.

2. Foreign businesses or foreigners who are not qualified to buy their own residential accommodation have no alternative but to rent their accommodation. The demand for rental residential property, especially high class ones, may go up. They have to pay high rents driven by high demand.

3. The restriction on investment residential properties will force foreign investors to shift their focus on other sectors of the real estate market. There is likely to be an increase in the demand for premium and quality commercial properties, hotels, service apartments and industrial properties, etc. Real estate prices in these sub-markets may increase as a result.

4. Foreign investors will become strong competitors to local investors. Under the latest round of macro control of real estate, both foreign and local developers are now required to provide 35% of the funds needed for a development project from their own resources before they can apply for loan. The requirement may cause a problem to local developers as they used to getting 100% finance from the banks. There is little opportunity for them to raise the necessary funding locally or from overseas. In contrast, the new control has no control on foreign investors getting finance from overseas. Foreign investors are thus in a better position to meet the finance requirement and become strong competitors to local investors.

5. The fall in demand for high class residential property may encourage developers to participate in building middle – low price residential properties. The increase in supply will see lower prices for properties in this category.

THE PROPERTY RIGHTS LAW

Despite the control measures, the provisions of the newly passed Property Rights Law should give foreign real estate investors more confidence in investing in China. The law was passed by the Chinese National People's Congress (NPC) on 16 March 2007 and will be in force on 1 October 2007. There are 5 parts and 247 articles in the law. Under the provisions of this law, legal movable and immovable property rights of Chinese nationals
and foreigners are equally protected. There are 6 areas that may concern foreign real estate investors more:

1. The law requires the creation, modification, transfer and termination of various legal interests in property to be registered under a uniform registration system. The registered interests are protected by the law and should not be violated.

2. The law gives property owners the right to manage their properties or to hire a property manager to do the job. They also have the right to change the property manager.

3. The law gives property owners the right to acquire parking spaces first. Developers can only sell or lease spare parking spaces to outsiders after meeting the property owners’ requirement.

4. The law has provision on environmental issues as well. It prohibits the design and construction of buildings that will affect the right for lighting and ventilation of adjacent buildings. It also prohibits persons with an interest in property from causing air, water, noise pollution, etc.

5. Currently the term of residential land use rights is 70 years. The law allows an automatic extension when the existing term expires if the land is not required for public use. While the law does not mention about the length of the extended term and the fee payable, it safeguard property owners’ right to continue occupying the property.

6. The law stipulates that compulsory land acquisition must be for a public purpose. Thus the authority cannot compulsorily acquire private land for commercial development. The dispossessed owners are entitled to compensation according to the relevant law.

On the whole, the new Property Rights Law has introduced more protection to real estate investors including those from overseas.

**CONCLUSION**

In recent years, real estate prices have been rising rapidly in China. In particular, the rocketing house prices have alerted the central government. A series of measures have been introduced to rein in the real estate market. The 6-point policy package introduced in May 2006 aims at regulating local financial institutions and developers; and to fight against speculators.

The sharp rise in the inflow of foreign capital into China’s real estate market also worries the central government. Although the size of investment is very small in relation to the total real estate investment, foreign investors are regarded as accomplices for causing the escalating real estate prices in China. The central government considers that the current
round of macro control of real estate will have a better chance to succeed if foreign real estate investment is also put under control. The introduction of the foreign investment control policies is aimed at complementing the 6-point policy package.

Under the new control policies, foreign businesses (other than approved real estate enterprises) and foreigners are only permitted to buy commercial real estate for their own use. Foreign businesses need to have 50% equity for setting up a real estate investment enterprise valued at US$10 million or above. They are also required to provide 35% of the funds needed for a development project before applying for loan. Although restrictive, the requirements are not over onerous. It is believed that while some foreign investors may find it difficult to meet the requirements, the majority may cope with them easily.

It is expected that the new foreign investment control policies will not cause major upheaval to the real estate market. Instead of investing in high end residential properties, foreign investors are expected to shift their investment to other sectors of the real estate market. Certainly the demand for high class residential properties will reduce. The gap will be filled by an increase in demand for commercial properties, hotels, qualify service apartments and industrial properties, etc.

Should foreign real estate investment in China be controlled? There is no absolute answer to this question. From the Chinese government’s point of view, certainly they would like to put foreign real estate investment under control. Many countries already have it. It is reasonable and legitimate for China to regulate foreign real estate investment for the sake of establishing a healthy investment environment. What is more important is for the government to be seen by the public as being proactive rather than reactive to problems.

From the foreign investors’ point of view, it is certainly not necessary. In particular, foreign investment has so far not caused major incidents in China. To the foreign investors, any regulation is an obstacle to investment. The foreign investment control measures will no doubt cause them inconvenience. However, it would be exaggerated to say that foreign investors will be scared off.

It should be understood that foreign investors have the liberty to choose the most favourable country to invest their money. While they are not obliged to invest in China, the huge market size of China, the improving economy and investment environment, the imminent floating of the Yuan and the potential of huge investment return will certainly be attractive enough to encourage foreigners to continue investing in China. The introduction of the Property Rights Law will further enhance the confidence of foreign investors.
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