Stop speculatingstart living China is trying new ways of skimming housingmarket froth*The party wants people to rent*

Stop speculating, start living

China is trying new ways of skimming housing-market froth

The party wants people to rent

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PAN JINGYUAN has little time for traditional family values. The 26-year-old says she has no intention of ever getting married and loves living far from her parents. But Ms Pan is traditional in one way—she sees a home as the best investment for her savings. She plans to buy a small flat in the southern city of Shenzhen, where she works at the headquarters of a restaurant chain. “There is no way the government would ever let prices really fall,” she says.

Such confidence has long been rewarded. Property prices in cities have roughly quadrupled this century, a rate of growth far exceeding that of the American housing bubble of the early 2000s, albeit from a lower base. This has led to a series of concerns: that homes are increasingly unaffordable, that the economy is too reliant on property and that housing prices, having gone up and up, might someday crash.

The government has, until now, tried to reduce the risk by periodically applying brakes on the market. Whenever real estate overheats, the authorities restrict funding to developers and make it difficult for people to buy new homes—for example, by increasing mandatory down-payments. When prices stabilise, they relax the controls. But such measures create volatility. Every three years or so, prices surge again.

So officials have started talking about a "long-term mechanism" to calm the housing market. Several times during the past year China's leader, Xi Jinping, has said that "homes are for living in, not for speculating on." The government appears to be adopting three main approaches. Together these could reshape the architecture of China's housing market.

The most promising is a push to develop a market for good-quality rental housing. Only about a fifth of urbanites rent homes in China, compared with a third in the rich world. In some countries, such as France and Germany, the proportion of renters is much higher still. China's rental housing is often shabby because it is aimed at low-income households. Rosealea Yao of Gavekal Dragonomics, a research firm, estimates that only around half of rental units in Beijing, the capital, and Shanghai have their own kitchens and bathrooms.

No dogs or migrants

A big reason for the slow development of the rental market is that there is not much profit in it. Cities tend to give more benefits to homeowners, such as the right to send children to local schools, so families far prefer to buy homes. It is mainly migrants from the countryside who rent, choosing dingy digs shunned by urbanites. Annual rents are about 1% of house prices, a low yield by global standards. Instead of taking a chance with messy tenants, many investors keep their properties empty, waiting for their values to rise.

One of the government's new approaches is to offer incentives to developers to build decent rental properties. It is doing this by selling land for rental projects at steep discounts, in effect guaranteeing hefty yields for developers. In some big cities, plans call for these discounted plots to account for about a quarter of future land supply. The government has promised to give renters the same rights as homeowners, though some doubt that it will actually do this. Many urbanites would resent additional competition for school places.

Shenzhen, which borders on Hong Kong, is among the first cities in China to sell large-scale plots for rental housing. The boomtown hopes that good-quality rental homes will attract the skilled workers it needs for high-tech industries. On the city's edge, Vanke, China's biggest developer, recently took over an apartment complex and began converting each unit into four or five tiny flats with living space little bigger than a bed. (One of Vanke's rental projects in Guangzhou, another southern city, is pictured.) The flats may be cramped, but they are clearly superior to other, mostly squalid, rental flats in Shenzhen. For officials, what matters is that Vanke has nearly quintupled the number of apartments available for rent in the complex.

A second approach will be the introduction of a property tax. Officials have talked for years about raising an annual levy on homeowners based on the value of their housing, as is commonly done in other countries. A possible benefit would be to nudge speculators to sell or at least rent out homes that they would otherwise leave unoccupied. At the same time it would give local governments a new revenue source, reducing their unhealthy dependence on land sales.

Yet apart from two small trials of such a tax in Shanghai and the south-western city of Chongqing, the government has dragged its feet. It has worried that a full property tax, implemented suddenly, would depress sales, says Eva Lee of UBS, a bank. But with the economy now in good shape, there seems to be less inhibition. The boss of a large developer predicts that a tax will be announced later this year. Still, required legislation could take up to two years to implement.

The third approach to the house-price problem involves striking a better balance between supply and demand. One way of doing this is sensible: expanding the availability of land where demand for housing is strongest. Because China wants to preserve land for farming, cities face strict limits on rezoning agricultural plots. But since last year, the government has let cities swap their land-use quotas—a potential boon to the fastest-growing urban areas.

The other way is more destructive. By imposing population limits on China's largest cities, officials hope to combat what they call "big-city disease": congestion, pollution and excessive pressure on urban resources (including, by implication, housing). Beijing aims to keep its population to 23m by 2020, while Shanghai wants no more than

25m people by 2035. Both are incremental increases over their current sizes and far below where, left unchecked, they would wind up. Population caps may help to calm the property market, but only by stunting the growth of the most productive cities. That would be a heavy economic price to pay for a stable housing market.

There are plenty of moving parts, too. Capital controls have trapped cash inside China, making property all the more alluring for investors. Rising incomes and changing lifestyles add to upward pressure on prices. Families want bigger apartments; more unmarried people also want their own homes. Mr Xi might succeed in skimming some froth from a bubbly market. But speculators are a hardy bunch. China has surely not seen the last of them.

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