Small property rights housing in major Chinese cities: Its role and the uniqueness of dwellers

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A B S T R A C T

As China has rapidly urbanized, housing prices in many cities have skyrocketed, reducing housing affordability and leading to the rise of an informal housing sector. This paper provides the first comprehensive demand-side analysis of the small property rights housing (SPRH) sector, using data from the 2015 China Household Finance Survey (CHFS) across twenty-seven major cities. This study shows that SPRH, despite its ambiguous legal status, has an average unit size larger than those in the formal sector. People who buy SPRH for basic needs (consumption demand) are more likely to be the locals with a middle range (“sandwiched”) financial and social status. They often have a large family size and thus have a strong demand for living space, and at the same time, they are willing (and able) to compromise on the benefits associated with legal property rights for a lower price. In this sense, the existence of SPRH supplements the short supply of affordable housing provided by local governments. Wealthy locals with high-risk preference are more likely to buy SPRH for investment. Such investment threatens social justice, and those people’s strong influence on public policies is a potential reason for the continuing prevalence of SPRH. Findings in this paper contribute to a more solid understanding of the mechanisms and social structures behind this informal housing sector in Chinese cities.

1. Introduction

In the past decade, housing prices in China have increased dramatically, especially in some large cities, such as Beijing, Shanghai, Shenzhen and some other provincial capital cities. According to the China quality-controlled housing price indices in eight major cities compiled by Zheng at Tsinghua University’s Hang Lung Center for Real Estate (Zheng, Sun, & Kahn, 2016), the average housing price of eight major cities has increased by four times in last ten years. This rise in prices has far exceeded the income growth in these major cities. Dwindling buying power coupled with rising housing prices has led to a soaring housing price-to-income ratio in China. In many major cities, the price-to-income ratio\textsuperscript{1} in the formal housing market has exceeded 10 in the last decade (Wu, Gyourko, & Deng, 2010). Meanwhile, the short supply of public affordable housing and the weak administration and corruption in this system have failed to meet the demand of its target population. By benefiting more high and middle-income families rather than lower-middle and low-income families, the mismatch and short supply of public affordable housing add to the severity of this housing dilemma (Man, Zheng, & Ren, 2011).

The deteriorating affordability of housing and the short supply of public housing for middle to low-income households led to a massive demand for affordable housing alternatives. This demand, along with the dual land system, has led to the emergence of a unique informal housing sector in China. There are currently two major components in China’s informal housing sector. One is urban villages (“chengzhongcun” in Chinese), and the other is small property rights housing (SPRH) (“xiaochanquanfang” in Chinese). Both types of housing refer to residential constructions on village land that is collectively owned and lack the legal property entitlements. Therefore, such informal housing units cannot be legally bought or sold on the market, property rights are not protected by law, and the residents are unable to enjoy most urban public services associated with legal property rights, such as public schools and police.

There has been a rich literature on urban villages (He, Liu, Wu, & Webster, 2010; Wu, 2016; Zheng, Long, Fan, & Gu, 2009, and others). These studies provide a coherent and consistent knowledge of the formation and nature of urban villages, the housing conditions and social

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\textsuperscript{1} Price-to-income ratio is the basic housing affordability measure. If PIR is equal or greater than 5.1 in an area, it means housing is severely unaffordable (Man et al., 2011).

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groups living in them. On the contrary, less has been known about small property rights housing (SPRH). Very few studies have examined this sector, and sometimes they provide conflicting arguments about the nature of SPRH and the social groups residing in it. However, the size and the role of SPRH in China’s whole urban housing sector cannot be neglected – Unofficial data suggest that for new housing constructions from 1995 to 2010, about 8% of the urban housing construction was for SPRH. Until 2010, the total area of SPRH construction reached 760 million square meters.\(^2\) The defects of SPRH have been widely criticized by the public, such as causing social injustice and bringing extra burden to urban infrastructure and public services. Since 2007, the central government has been continually issuing documents to call for a stop to the growing trend of SPRH (Shen & Tu, 2014). However, few SPRH developments have been demolished since then, and such developments have still been increasing at a steady rate.

This paper aims to fill the gap in our knowledge of small property rights housing in Chinese cities, by examining the distinctive characteristics of its owners (for both consumption demand and investment demand) and exploring their incentives. Specifically, using a unique large-scale survey dataset, we will answer the following two research questions: First, what are the characteristics of the households who buy SPRH as consumption demand? What drives them to live in informal properties that are not protected by law? Second, who are buying SPRH as an investment? Why are they willing to take the risk investing in SPRH instead of formal commodity housing?

This demand-side housing choice analysis can provide us with the insights on the unique role of SPRH in China’s urban housing sector, and the rationale behind its prevalence. Together with the understanding of the supply-side factors (dual land system, the short-supply of formal affordable housing), this paper will help policymakers to better understand the benefits and costs of tackling the SPRH issue in Chinese cities. The rest of the paper is organized as follows. Section 2 introduces the literature review on the informal housing sector in China, and we also lay out our analytical framework. Section 3 introduces the survey data followed by our hypotheses. We present our empirical models and discuss the results in section 4. The last section states the conclusion and discusses the policy implications of our findings.

2. Literature review

2.1. What drives the emergence of the informal housing sector?

The emergence of the informal housing sector has been driven by both demand-side and supply-side forces. From the demand side, the extremely high prices in the formal housing sector push out a significant amount of the middle-class, and low-income households (including millions of rural migrant workers). The huge price gap between formal and informal housing sectors incentivizes them to enter the informal housing sector. Typically, the unit price of SPRH is only 45% to 60% of the commodity housing (Wang & Sun, 2014). In the case of Shenzhen, the price of SPRH is 52.82% lower than the price of PFRH on average (Lai, Zheng, Choy, & Wang, 2017). The main reasons for this huge price difference are the absence of land prices, problematic property rights, and inalienability (Deng, 2009). For urban villages, the average monthly rent per urban village unit is about 20% of a formal rental unit with a similar size in Beijing, although urban village units always do not have a bathroom and a kitchen (Zheng et al., 2009).

On the supply-side, there is a short supply of affordable housing provided by local governments. Owner-occupied affordable housing subsidized by the government, known as “ecomonomical and comfortable housing” targeting middle-to low-income residents, only accounts for 3.4% of China’s total housing stock (Man et al., 2011). What is more, this system faces accusations of corruption because of too high the eligibility criteria and the problematic enforcement, so that it fails to serve its target group of middle-to low-income residents (Man, 2011). The rental public housing has a concise history and thus a small market size (Zou, 2014). Without local urban hukou (household registration), most migrant workers are not eligible for either owner-occupied or rental public housing units. Furthermore, local governments have a weak incentive for public housing supply because of the high-opportunity cost. They have to provide free land to public housing projects. However, if they had sold those land parcels to real estate developers, they would have received a considerable amount of land sales revenue.

Another important supply-side factor is China’s dual-land system and the weak enforcement of the eminent domain, which provide the institutional foundation for the existence of the informal housing sector. In China, land ownership is divided into two categories: state ownership and collective ownership. State-owned land is mostly urban land, whereas land in rural areas and remote suburbs, except a few areas regulated by law to be under state ownership, is owned by village committees. Regulated by land administration law, collective-owned agricultural land can only be developed for agricultural activities or housing for farmers (Deng, 2009; Wang & Zhang, 2017). Any other construction activities, such as commodity housing, should first go through eminent domain to convert the land from collectively-owned to state-owned. During the eminent domain stage, individual villagers or village committees are compensated minimal compared to the market value of the expropriated land. However, if villages or farmers engage in informal housing development by ignoring the eminent domain stage, they can benefit directly from any profit (either rented or sold) received from the land’s market value (Zhang & Lu, 2011). Driven by this profit incentive, village committees or farmers, either collaborate with developers or work on their own to produce informal housing supply (Sun & Liu, 2015).

2.2. Urban villages versus small property rights housing (SPRH)

As mentioned in the introduction section, urban villages and SPRH are the two types of informal housing in China. Although both are informal, SPRH is significantly different from urban villages regarding housing tenure, housing conditions, and the socioeconomic characteristics of dwellers. Dwellings in urban villages are mostly renter-occupied, whereas SPRH units are mostly owner-occupied. From the appearance of the neighborhood, it is hard to tell if the housing development is SPRH or commodity housing. On the contrary, urban villages are described as decrepit and inadequate (Wu, 2016). These differences in tenure status and housing conditions differentiate the two informal housing developments significantly by their residents’ socioeconomic characteristics. While it has been widely accepted that residents in urban villages are mainly migrant low-income workers (He et al., 2010; Wu, 2016; Zheng et al., 2009), there are disagreements in the existing literature about the social groups in SPRH. Deng (2009) argues that SPRH owners are composed of middle-income families, elderly retirees, wealthy people, and artists. Other studies suggest that SPRH is mainly occupied by low- or lower-middle-income migrant workers (Shen & Tu, 2014; Sun & Liu, 2015). Both arguments lack sufficient supporting data.

Besides the different characteristics of their residents, SPRH also differs from urban villages regarding government’s attitude toward them. SPRH has never been demolished massively as urban villages. Several scholars have studied the reasons behind it from a top-down standpoint. One argument is that the existence of SPRH is a tool to mitigate social conflicts. China’s booming economy and rapid urbanization have benefited many urban citizens, yet rural farmers lag far behind economically. In 2015, the average urban income was 2.7 times higher than the average rural income (The Economist, 2016). Profits from SPRH developments may help balance the polarizing situation.
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