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Qiulin Ke Karen Sieracki

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Market maturity: China commercial real estate market

Qiulin Ke

*The Bartlett School of Built Environment, University College London,
London, UK, and*

Karen Sieracki

KASPAR Associates Ltd, Tunbridge Wells, UK

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Abstract

Purpose – The purpose of this paper is to explore the evolutionary path to market maturity that China property market has taken over the last few decades. The focus is on the commercial real estate markets in Beijing and Shanghai. It will help international investors understand the market environment, risk and market activity process.

Design/methodology/approach – In this research, the authors apply the market maturity framework and its key determinants based on previous work undertaken by Keogh and D'Arcy (1994) and Chin *et al.* (2006) for the analysis of Chinese commercial property market. Particular focus is on Beijing and Shanghai. The questionnaire is designed to obtain fair and objective views from international property consultancy firms active in Beijing and Shanghai markets. There are not many of these international property consultancies. The reason why this type of business was selected was to insure that the business had an understanding of China's place in the global commercial real estate market as this market matures from its emerging market status.

Findings – The findings reveal that the respondents felt the commercial property markets in Shanghai and Beijing were now moderately mature. However, issues such as poorer level of standard market information, development instability, low transparency of the legal system, high taxes and high government intervention still existed in China's commercial property market, therefore hindering its progress towards greater market maturity.

Research limitations/implications – The small same size of the survey is the major limitation of the research.

Practical implications – International investors and analysts can benefit from the research findings through a better understanding of the behaviour and trends in this unique market which will be reflected in their decision-making process.

Originality/value – An explorative approach was used due to the lack of data to examine the perception of China's commercial property market's evolution and maturity. The findings can then be placed in the context of other Southeast Asian cities. The evolutionary process of China's property market is rarely examined in previous studies of China property market due to the lack of data and transparency.

Keywords China, Evolution, Beijing, Commercial property market, Maturity, Shanghai

Paper type Research paper

1. Introduction

As the Chinese economy has transformed into dynamic private sector-led economy and has become integrated into the global economy, its property market has experienced dramatic changes. Starting from a closed, centrally planned economy in the early 1980s, the Chinese commercial property market emerged first in the cities of Beijing, Shanghai and Guangzhou, driven by the demand for international standard office space by multinational companies coming to China to set up regional headquarters or/and offices. This created a user market of demand for land and buildings from overseas companies and local businesses from which the commercial



property market emerged. Over the past few decades, China's property market has gone through a remarkable and relatively quick transformation. Unprecedented rates of urbanization, huge infrastructure development and integration with the world economy, have gone hand-in-hand with the rapid development of its property industry. Now China's property market has become the second largest Asian property market behind Japan and has attracted most attention from domestic and international investors.

Despite this level of growth, commercial property market data is very uneven and difficult to obtain. There are a limited number of data sources. Therefore any analysis or survey will be affected by these limitations, unlike in western developed commercial property markets. However, these limitations should not prevent further work and discussion.

Property market activities are linked to economic and urban development. Changes in property markets have been analysed from their evolutionary beginning towards "maturity" (Keogh and D'Arcy, 1994; Berry and McGreal, 1995; D'Arcy and Keogh, 1997). Market maturity is dependent on the state of economic development. The underlying assumption is that property markets become more complex as they become integrated into global economic and financial flows. This evolution follows roughly a common direction which is the development of market structures and practices like those in the fully mature property markets of the world's financial centres (Keogh and D'Arcy, 1994).

Commercial real estate market maturity is only a starting point to understand its behaviour and trends. Keogh and D'Arcy (1994) define that market "maturity" is a function of the following: the degree of diversification of user and investor opportunities; flexibility of adjustment of property interests; market openness; the existence of information and research systems; professionalization, and standardization of property rights and market practices. Mature property markets are generally most open, which can be measured by the availability of information and the presence of international participants in local markets. According to Keogh and D'Arcy (1994), a mature property market has the ability to accommodate a full range of use and investment objectives, diversified investment mechanisms such as the formation of property unit trust or funds, the shares of publicly quoted property companies, and the securitization of individual properties.

The JLL global property market maturity index (2010) analysed market maturity for 22 key cities around the world against four key criteria. In the report, a "mature property market" was defined as: a highly transparent real estate market characterized by the free flow of high-quality market information; robust regulatory enforcement and fair transaction processes; high connectivity with international real estate capital markets in terms of both capital inflows and outflows; commercial buildings that are environmentally sustainable and resource-efficient and a robust domestic and international corporate base. This market maturity criteria in the JLL report were similar to the ones proposed by Keogh and D'Arcy (1994). There was one newly added criterion which is that a mature market offers environmentally sustainable buildings underpinned by professional management. This demonstrates the evolution of commercial real estate maturity criteria linked to social and economic changes.

The evolution of property markets to their maturity has been observed in Southern European countries (Keogh and D'Arcy, 1994; Keogh, 1996; de Magalhães, 1999). For example, Keogh and D'Arcy (1994) undertook a comparative analysis of mature and emergent commercial real estate markets in London, Milan and Barcelona. They

concluded that there was no single, universal evolutionary path to be followed by all property markets. Market maturity should be considered in terms of the relationship between local property market cultures and market efficiency seen in the context of historically specific development paths. The cities with a comparable degree of economic development, urbanization, economic and political maturity such as London and Milan can have property markets which are profoundly different regarding the traditional criteria of maturity. They pointed out that conceptual property market maturity does have fundamental limitations.

The studies of the emerging property markets evolution and maturity in central and eastern European countries (Adair *et al.*, 1999; Keivani *et al.*, 2001; McGreal *et al.*, 2002) identified the important role that international companies played in both the occupier and investment markets. In these countries' economic transitional period there had been significant international investment in the Czech Republic, Hungary and Poland. International investment was instrumental in the establishment of commercial real estate markets in these regions, given the non-existent domestic sources of funds. Consequently in response to the globalization of investment markets, local property cultures were amended to suit the practices and requirement of global institutional property markets.

There have not been many studies on commercial real estate market maturity in Asia. One main barrier has been the difficulty in obtaining data, survey responses and standard definitions. Chin and Dent (2005) and Chin *et al.* (2006) investigated the evolution of property markets in certain Southeast Asian cities. These studies indicated there was significant difference among these local markets. This work reinforced the previous studies' findings that the institutional approach to market maturity was the place-specific outcome of a complex interplay of global economic forces and those social, economic, institutional and cultural structures that frame each market, rather than a linear and universal evolutionary process (de Magalhães, 2001).

The Chinese property market is unique in many respects. It took a different evolutionary path from other emerging markets such as those in the central and eastern European countries. In the economic transitional period, developers and investors from Hong Kong, Singapore and Taiwan followed the rule of local geographically and cultural proximities, alongside the domestic developers, played a leading role in forming China's property market and the property-led urban regeneration in 1990s, especially in the large cities such as Shanghai and Beijing. At the same time western real estate investors were absent from these cities, mainly due to unfamiliarity with China's property market institutions and the constraints the Chinese government placed on foreign direct investment (FDI) in China's real estate market. This was despite these booming Chinese cities attracting a substantial amount of industrial capital from the west as the Chinese government encouraged foreign investment in targeted industries. The rapid growth of China's property market was domestically driven. The market was largely controlled by the Chinese government and state-owned enterprises (SOE). This helps to explain the low level of market transparency. For many international investors, the risk of doing business in China was great.

China's commercial property market history is relatively short compared to developed markets. However, the property markets in cities such as Beijing and Shanghai have fast tracked to a maturity level. According to the JLL Real Estate Market Maturity Index in 2000, Beijing and Shanghai ranked 15th and 14th on the global key cities' market maturity index, respectively, placing them in the "emerging"

market category. In 2010, they held tenth and 11th positions which was classified as the “transitional” market. The index also questioned how much of the “western-centric” definition of maturity was important and relevant to China’s market. It argued that the future commercial property market maturity profile of China is likely to be very different from those in the developed countries and may not meet the exact criteria of a mature market as currently defined in the short to medium term.

China’s growth over the past three decades has provided a “text-book” case study of market-driven economics. The fast evolving and growing property market not only attracted investors, but also researchers. Research activities grew, though the information flow is relatively poor and data is incomplete. The main research themes of the Chinese property market were the evolution and development stages of its property market. In 1990s, most of the research focused on land use right reform, its related issues and recommendation, the privatization of land market and urban development (e.g. Walker and Hin, 1994; Wu, 1995, 2000; Chan, 1999; Li, 1997; Zhu, 2002). Most of the studies were qualitative in nature, due to the unavailability of historical data. Since 2000, research focused on housing market reform, house pricing and the factors affecting the housing prices (e.g. Li, 2000; Fu *et al.*, 2000; Mak *et al.*, 2007; Wu *et al.*, 2012). Most of the research was quantitative, benefitting from the availability of data in housing sector.

Due to the relatively short history of the Chinese commercial property market and lack of quality market data, the studies of Chinese commercial property markets are scant. To the best of our knowledge, there are only a few papers (e.g. Ke and White, 2009, 2013) investigating office rental pricing and adjustment in Shanghai and Beijing. There are few qualitative studies of the Chinese commercial property market structure.

This paper analyses the evolution and maturity of Chinese commercial real estate markets by focusing on China’s two largest commercial property markets: Beijing and Shanghai. The aim of the paper is to help international investors understand the market environment, risk and market activity. There is no such research that systematically examines the issue of China’s commercial property market’s evolution towards maturity.

The paper is structured as follows. Section 2 discusses the evolution of the Chinese commercial property market. Research methodology is discussed briefly in Section 3. Section 4 analyses the survey findings and conclusions are made in Section 5.

2. The evolution of commercial property markets in Beijing and Shanghai

Until the 1980s, there was no market mechanism for the transfer of real property in China. Land was a public good either owned by the state or held in collective ownership by village communities. Since the 1980s many cities in China have expanded rapidly and collectively owned land that was absorbed into urban development. The commercial property market emerged, first in large and significant cities such as Beijing and Shanghai. User demand for office space happened at the beginning of the 1980s as foreign companies arrived. Office demand became exacerbated as there was a shortage of commercial office space either for sale or for rent in these markets.

Beijing and Shanghai were the most attractive cities for foreign companies as virtually every major multinational corporation required an active presence in these two cities. These two markets are among the world most liquid markets. They are

China's two national economic centres, providing substantial investment market potential for foreign investors. Beijing and Shanghai also have the most foreign property enterprises where international investors along with local investors encounter fewer restrictions and less market uncertainty. More transparency is associated with higher investment. Beijing and Shanghai are most transparent markets in China, not far behind at the top end of the "semi-transparent" category according to JLL's 2012 the Global Transparency Index.

Over the past three decades, Beijing and Shanghai's commercial property markets evolved. The first period, from 1980 through to 1992, was the experimental period of land reform. The property market started to emerge with laws and regulations as land transfer became operational. The arrival of foreign companies created strong demand for office buildings. However, internationally acceptable office premises were not available. Most of the foreign companies worked in hotels where rooms were converted to offices. For example, the first commercial office premise in Shanghai was not available until 1983 when Jingjiang Club, a refurbished old colonial building, was open to tenants at market rates (Zhu *et al.*, 2006). By the end of 1988, there were only four commercial office buildings in Shanghai (Jingjiang Club, Union Building, Ruijing Building, Gaoyang Building) amounting to a total floor area of 58,500 square metres in the nascent office market (Shanghai Municipal Bureau of Statistics, 1989).

The second period, between 1993 and 1996, was a transformational period. There was a sharp rise in rent as a result of the severe shortage of office space combined with an increasing demand for office space from the massive influx of foreign companies establishing regional offices. According to DTZ, by the end of 1993, the total prime office stock was 0.15 million square metres in Beijing and 0.12 million square metres in Shanghai with low vacancy rates. There were few property investment transactions during this period. Office property was owned and occupied by SOE. To meet the rising demand of multi-national companies, large scale office building construction commenced from 1993.

The commercial property market was volatile during this period. Investment in commercial property greatly increased, followed by a dramatic fall. A huge amount of capital moved into property market which then became overheated. Many speculative office projects started during this period. As the pace of economic growth slowed down; the extra office space could not be absorbed. The property market was out of control. Consequently, the Chinese government intervened through tight credit controls. The banks suspended property lending. At the same time, slower economic growth led to less demand for office space. Many office buildings became void. Office property prices fell. Many office projects that commenced in the beginning of 1990s were left uncompleted. The Chinese banks held massive amount of non-performing office assets on their balance sheet.

The third period (1997-2000) was marked by a substantial increase in the supply of office property. During the Asian Financial Crisis, China's economic growth and FDI slowed and office take-up was low. The overinvestment in real estate in the previous time period resulted in an oversupply of office space in the markets. Office rents fell and vacancy rates rose. For example, in 1997, the vacancy rate in Puxi office market Shanghai was above 60 per cent and above 50 per cent in Beijing according to DTZ market reports.

The fourth period starting from 2001 was characterized by some improvement in market transparency. Sustained economic growth and increases in FDI further

stimulated the demand for office space. Rents rose and the investment in office buildings increased before the global financial crisis in the second half of 2007. This period witnessed massive inflows of global funds into the Chinese property market.

The transformation of the commercial stock in Beijing and Shanghai over the past decades has been rapid. According to DTZ property market reports, in 1993, the commercial office stock in Beijing and Shanghai are 150,185 square metres and 122,397 square metres, respectively. By the end of 2013, Grade A office stock in these cities has increased to 6,762,483 square metres and 6,088,488 square metres, respectively. It was largely built by the domestic developers. This was unlike the other emerging markets in central European cities which were mostly driven by external actors including foreign property developers, investors, agents and the users of property (Adair *et al.*, 1999). Foreign capital had been restrained in China's property market unless it was for self-occupation. The first generation of local Chinese developers grew up by participating in joint-ventures between foreign development capital and local land plots in the late 1980s (Zhu *et al.*, 2006). The initial developers of investment-grade property in Beijing and Shanghai were from Hong Kong who brought advanced techniques and experience to project construction. This greatly increased the benchmark for quality in these markets and many of these projects still stand as landmarks in the two cities.

FDI has been recognized as one of the most important driving forces facilitating China's modernization and regional economic growth. Foreign investment was a central driver for promoting urban restructuring together which transformed global cities in China. Government and local conditions were important in constructing development zones and in channelling foreign investment. For instance, FDI was the major force behind Shanghai's development as a global city. Built on geographical and historical advantages, the inflow of foreign investment led to the significant spatial and economic transformation of Shanghai. Hong Kong developers and real estate capital played a leading role in remaking Shanghai old downtown and shaping a new pattern of office location. They understood the intangible cultural capital embedded in the Shanghai's past which gave them competitive advantages and confidence (Zhu *et al.*, 2006). Now Shanghai has become the most important location for regional headquarters of multinational corporations and a pre-eminent commercial, financial and logistic hub in China.

Beijing plays a dual role as a political centre as well as an international financial centre. SOE are one of the major occupants of office buildings, alongside multinational companies. These Chinese corporates have often preferred owning to renting which reflects the history of SOE owning their own premises.

Beijing and Shanghai office markets are different in certain aspects. For example, Ke and White (2013) failed to find FDI having a significant impact on office rents in Beijing; whilst it is one of the significant factors influencing Shanghai Puxi office rents (Ke and White, 2009, 2013). Lecomte (2013) found that the Beijing office market was nationally dictated due to being significantly influenced by Chinese national GDP. Shanghai's office market was significantly influenced by local GDP and employment.

Within China, there is a relationship between the openness of the property markets and transaction volumes. Shanghai and Beijing are the most transparent markets in China with the highest real estate transaction volumes. Totally, 80-90 per cent of investment transactions in these two cities have involved foreign investors, who have forced the pace of change and encouraged greater transparency in the commercial property market (Jones Lang LaSalle, 2008). One of the important driving forces of

improved transparency in these cities is the globalization of its real estate investment. Exponential growth in the number of active real estate developers, occupiers, investors and real estate funds requires much greater transparency. The presence of international real estate consultants and advisors has contributed to this market transparency and globalization (D'Arcy' and Keogh, 1997).

The major international real estate players are all present in Beijing and Shanghai. They collect local market data and information, undertake market research and provide professional services of property management, acquisition, disposal and investment. This facilitates the improvement of market transparency and fosters market maturity. According to Jones Lang LaSalle's global real estate transparency index, China has moved from an opaque to a semi-transparent market over the past decade. In 2008, Beijing and Shanghai were at the low end of semi-transparency category. In 2012 they rose to the top end of semi-transparency.

In the report of Real Estate Market Maturity Index by Jones Lang LaSalle (2010), Beijing and Shanghai fast tracked from an emerging market to a transitional market. The report said the two cities' fast advance up the global real estate market maturity rankings was due to their unique combination of massive infrastructure investment, highly effective government policies, long-term planning, impressive speed of real estate delivery and a vibrant domestic economy. However, transparency is one of the issues that affects commercial property market efficiency and maturity. The maturity profile of China is different from those in the developed world, and understanding these differences will be vital for international capital markets, where perceptions of risk – and therefore attitudes to pricing and location – are influenced by traditional perceptions of maturity.

3. Research motivation/methodology

The paper's methodology is qualitative with primary research based upon evidence presented through a questionnaire survey. Chin *et al.* (2006) undertook qualitative research about the market maturity of selected Southeast Asian property markets. The markets included in their research were Bangkok, Hong Kong, Kuala Lumpur, Singapore and Taipei. They applied the market maturity framework developed by Keogh and D'Arcy (1994). They made several key additions to these market maturity characteristics based on the works of Armitage (1996) and Lee (1999, 2001). Chin *et al.*'s questionnaire consisted of three parts: the perception of market maturity, the institutional environment and the issues affecting international investment. No Chinese city was included in their analysis.

This paper aims to complement their research findings by addressing this Chinese gap. It explores the issues of the relative market maturity of China's two largest property markets, Beijing and Shanghai and compares these results with Chin *et al.*'s survey findings of the other Asian property markets. To be consistent, this paper followed Chin *et al.* (2006) work and used a common questionnaire through applying the same market factors as in their study for each element and its perceived level of maturity. The use of a common questionnaire would highlight any behaviour difference between the two surveys. In order to gauge attitudinal opinions and the significance of various factors influencing market maturity, this paper's survey utilized the same scaling techniques as in Chin *et al.* (2006): 1 represents "very well developed" or "very mature" and 5 represents "very limited development" or "very immature".

The paper's questionnaire was first sent to two investors in London who were active in China's property market for piloting and to ensure the relevance of the market maturity criteria. The target group for this survey was researchers working in the research departments of renowned international property consultancy firms in either Beijing or Shanghai. These firms operate on the front line of Chinese property markets by providing professional consultancy for both their clients and investors. They are important stakeholders in the Chinese property investment decision-making process and at the same time, they are familiar with international standards and practices. Therefore this target group are able to judge the level of market maturity of the local Chinese property market in the context of other mature property markets.

Questionnaires were sent to 18 renowned international property consultancy firms and their regional offices in Beijing and Shanghai. There are not many such firms so it is a limited universe. Totally, 11 (61 per cent) responded which is a good rate. The respondents were the heads of research departments or senior researchers with more than five years' experience in China's property market. Five respondents were from Beijing and six were from Shanghai. Their views about the factors that constitute market maturity were similar. Therefore further breakdown in the analysis was not done due to the small size.

4. Survey findings and analysis

The survey questions were in three parts, as seen in the studies of Chin and Dent (2005) and Chin *et al.* (2006). The first part concerned market maturity; the second part dealt with the institution environment and the third part looked at the issues affecting international property investment.

Table I above illustrates the survey findings looking at the perceptions of market maturity in Beijing and Shanghai. There was a narrow range among the respondents' answers. This is shown in the relatively low standard deviation across the market maturity factors. This demonstrates most of the respondents held similar opinions concerning market maturity in the Chinese commercial property market.

Compared with the findings in the study of five other Asian cities by Chin *et al.* (2006), the scales of the market maturity factors in Beijing and Shanghai were higher (i.e. less developed) than the mature markets of Hong Kong and Singapore, but lower

	Mean	SD
Market openness	2.83	0.69
Property services professional level	2.86	0.35
Presence of property intermediaries	2.33	0.47
User and investor opportunity	2.43	0.73
Market value	2.14	0.35
Market flexibility	2.57	0.73
Market information standardization	3.43	0.73
Market information availability	3.14	0.64
Development stability	3.33	0.94
Quality of property products	2.29	0.45
Average	2.74	

Table I.
Perception of
commercial property
market maturity in
Beijing and
Shanghai

Notes: 1 represents "very well developed" or "very mature", etc., and 5 represents "very limited development" or "very immature", etc.

(i.e. more mature) than Bangkok, Kuala Lumpur and Taipei. Chinese market information standardization (mean 3.43) and development stability (mean 3.33) were less mature. The level of market information standardization and level of property development stability were perceived to be lower in China than in the other five Asian cities. The factor of market information availability in Beijing and Shanghai had the mean of 3.14 which was slightly lower than Taipei (mean 3.3) and Bangkok (mean 3.2). The Chinese figures were higher than Hong Kong, Singapore and Kuala Lumpur (means 1.4, 1.4 and 2.9, respectively). Market information in Beijing and Shanghai was felt to be less available than Hong Kong, Singapore and Kuala Lumpur. These findings were consistent with JLL's 2012 global transparency index which shows China's tier 1 cities were less transparent than Hong Kong, Singapore and Kuala Lumpur.

Global transparency index

A mature market should be able to offer extensive information flows (including information standardization, easy availability and good quality) to enable a high level of research activities providing input into the property decision-making process (Keogh and D'Arcy, 1994; Armitage, 1996). Market information standardization is about the quality of market information. Market information is defined as including everything from the methodology of obtaining market information to the output of research reports.

There is no property investment performance index in China. The continuity of the property market data and the consistency of property data standards are poor. This contributes to low transparency of the Chinese property market which is domestically driven, and largely controlled by the government and SOEs. Growth and physical development take priority over transparency. In this vacuum a growing professional service community collects its own market data and information, and produces research reports for its clients. Some market data is made available.

Different property valuations in China also contribute to low market information standards. The Chinese appraisal industry was formed in 1993 when the real estate valuer qualification system was instituted. Property valuation falls under different associations including China Appraisal Society, a national professional society for Certified Public Valuers, China Institute of Real Estate Appraisal, China Real Estate Valuer Association. These multiple professional bodies cause many valuation anomalies. The valuers associated with the different bodies cannot be substituted by each other. Asset valuation, real estate valuation and land valuation can only be done by three different types of qualified valuers upon approval by the respective competent authorities from the three different bodies. Currently, there are 15 appraisal standards in China, of which eight have been adopted since November 2007. In addition, there are over 20 areas that will be addressed in new standards currently under development. Despite China's asset appraisal industry being still heavily government influenced there is now evidence that theoretical sophistication is emerging after two decades. However, the issues such as consistency, reliability and quality do not match those of international practices.

China's property market, especially the development market is subject to changes in government policies that are influenced by various interest groups. Chinese development projects rely on finance. The level of development stability will depend heavily on the country's financial systems. A mature market provides a sound grounding to maintain the stability of the development process (Keogh and D'Arcy,

1994; Armitage, 1996). In China, the equity market and bond markets are still underdeveloped. Real estate investment trusts and other diversified investment vehicles such as property unit trust or funds or the securitization of individual property do not exist in China. Banking finance is the major funding source for Chinese developers. Most of the respondents rated development stability in Beijing and Shanghai as low. This is due to the government intervention which continues to enforce regulations limiting developer's access to bank finance, especially for land purchases, as well as for construction. This is to control the rising property prices although the Chinese government is aware of the threat posed to the greater economy if the Chinese property market crashed.

Noticeably, the survey respondents viewed the market value of Beijing and Shanghai commercial property as high (mean 2.14), but lower than that in Hong Kong (mean 1.7) and Singapore (mean 1.9). At the end of 2011, Beijing was China's most expensive city for offices and the third most expensive office market in Asia, behind Hong Kong and Tokyo (Cushman and Wakefield, 2012). Office demand in Beijing is driven mostly by domestic high-tech/telecom and financial sectors. In contrast, Shanghai's office market is dominated by multi-national corporations, especially those from financial, pharmaceutical and high-tech sectors. Shanghai is viewed as one of the most favourable cities for foreign companies with the most open and competitive property market in China (Chen and Hao, 2010).

The average score for Beijing and Shanghai market maturity factors was 2.74. In the survey study of Chin and Dent (2005), the average maturity factors scores for Hong Kong and Singapore were 1.5 and 1.67, respectively. These markets were identified as the most developed and most mature markets. The average scores of market maturity factors for Kuala Lumpur, Bangkok and Taipei ranged from 2.7 to 3.1. They are defined as emerging markets. Beijing and Shanghai markets fall into the emerging market category, more or less the same level as Kuala Lumpur. The most developed factor for Beijing and Shanghai commercial property markets was the quality of property products. Despite constant media coverage about the substandard quality of property in China the survey respondents regarded commercial office buildings in these cities as being of a high standard. The least developed factor for Beijing and Shanghai property markets was on market information and standards.

The perception of the institutional environment is shown above in Table II. Comparing this paper's survey findings with the ones by Chin *et al.* (2006), most of the institutional environment perceptions are higher in Beijing and Shanghai than the other four cities in Chin *et al.* (2006) survey but lower than Bangkok. The Chinese institutional environment was felt to be less developed than these Southeast Asian cities. The Chinese legal framework (mean 3.14), Chinese legislative system transparency (mean 3.43) and Chinese legal regulation (mean 3.33) were felt to be less developed than Hong Kong (means 1.56, 1.72 and 1.72, respectively), Kuala Lumpur (means 2.37, 2.57 and 2.57, respectively), Singapore (means 1.43, 1.43 and 1.43, respectively) and Taipei (means 2.73, 2.83 and 2.83, respectively). The Chinese institutional environment was felt to be slightly better than Bangkok (means 3.22, 3.5 and 3.5, respectively). Property tax is high in Beijing and Shanghai (mean 1.67). Beijing's and Shanghai's property tax factor was the same as Hong Kong (mean 1.61). Chinese tax rates for real estate investment steadily increased in recent years. There are many taxes at every level: income tax, business tax, deed tax, land appreciation tax. The high tax rate reduces the internal rate of return for the commercial property investment.

Table II.
Relative perception
of institutional
environment for
commercial property
markets in Beijing
and Shanghai

	Mean	SD
Political stability	2.67	0.75
Currency exchange stability	2.57	0.49
Restriction and regulation on foreign investors	2	0.53
Legal framework	3.14	0.99
Transparency of legislative system	3.43	0.73
Legal regulation	3.33	0.47
Sound financial/economic structure	3	0.82
Liberalization of financial markets	3.67	0.47
Strength and stability of economy	2.5	0.76
Level of transparency of market	3.67	0.75
Profession level	3	0
Perceived corruption level	2.5	0
Government intervention	1.67	0.75
Tax	1.67	0.47
Urban form (planning)	3	0.58
Public infrastructure level	2.17	0.69
Sound financial/economic structure	4	0.71
Strength and stability of economy	3.75	0.43
Restriction and regulations on foreign investors	4.25	0.43

Notes: 1 represents “very well developed” or “very mature”, etc., and 5 represents “very limited development” or “very immature”, etc.

Government intervention in China is higher (mean 1.67) than all the other five Southeast Asian cities in Chin *et al.*'s study. It is widely known that China's property market is a government policy-oriented market. Politics also dominates economics. Since 2009, the Chinese government has introduced various measures to cool the overheated real estate market. They included increasing the mandatory down payment for mortgages; restricting the number of residential properties a person could buy and reducing the credit availability to property developers by raising interest rate and increasing the reserve requirement ratio. These measures were mainly to curb housing prices, so affecting only the residential sector. As the policy became tougher and tougher, it would affect property market sentiment as a whole.

China has capital account restrictions that limit overseas capital flowing in and out of China. Interestingly, most of the survey respondents thought the currency, i.e. RMB, was more stable (mean 2.57) than the currency of Thailand (mean 3.13) and Malaysia (mean 2.6). The survey respondents felt confident for the Chinese economic outlook, although RMB is not freely convertible at the moment.

Table III above demonstrates that most of the survey respondents viewed the transparency of the legal system in China as low, the legal and regulatory enforcement as weak and financial market structure as less well established and not liberalized.

The research further explored the important factors for international investors as shown in Table III above. The survey respondents perceived these market factors as important. The cultural difference was seen to be the least important with the mean of 2, consistent with the survey findings by Chin *et al.* (2006) of the five other Asian cities. The reply range revealed that the respondents considered most of the factors to be “important” or “critical”, particularly in the aspects of “sound financial/economic structure (mean 4) and “restriction and regulation on foreign investors” (mean 4.25).

Table III.
Issues affecting
international
investment for
commercial markets
in Beijing and
Shanghai

	Mean	SD
Political stability	3.25	0.83
Legal regulation	3.25	0.85
Taxation	3.5	0.5
Legal framework	3.25	0.84
Liberalization of financial markets	3	0.71
Currency exchange stability	2.75	0.43
Transparency of legislative system	3.25	1.09
Public infrastructure level	2.75	0.42
Level of transparency of market	3.25	1.3
Profession level	2.75	0.44
Government intervention	3.25	1.09
Perceived corruption level	2.5	0.52
Urban form (planning)	2.25	0.41
Culture difference	2	0
Market maturity	2.8	0.44

Notes: 1 represents “very well developed” or “very mature”, etc., and 5 represents “very limited development” or “very immature”, etc.

Totally, 75 per cent of the survey respondents thought that the commercial real estate investment markets in Beijing and Shanghai were moderately mature (mean 2.8).

5. Conclusions

The Chinese commercial property market took a different evolutionary path to maturity. It has gone through a remarkable transformation, from being non-existent in 1980s to the second largest market in Asia, with the delivery of 17 million square metres of Grade A office space together with over 300 major shopping centres and 11 million square metres of modern warehouse in the key cities (Jones Lang LaSalle, 2010), all of which was built largely by the domestic sector. Unlike other emerging markets in Central and Eastern European countries where foreign fund and foreign players such as users, investors, developers and agents had played a leading role in these commercial property markets’ formation, evolution and maturity, the Chinese commercial property market is different. It is domestically driven and controlled by the government and SOEs, though at the early stage of commercial property market formation, the developers and development capital from Hong Kong played an important role in property-led urban regeneration in the large cities such as Beijing and Shanghai, due to the culture and geographic proximities.

This paper investigates the market evolutionary path of China’s two largest commercial property markets, Beijing and Shanghai, within the framework of Keogh and D’Arcy (1994) and compares our survey findings to the ones by Chin *et al.* (2006) about five Southeast Asian cities.

To sum up, the survey respondents felt that the commercial property investment markets in Shanghai and Beijing were considered to be moderately mature, but remained as emerging markets. The survey suggests that Beijing and Shanghai were more mature than Bangkok and Taipei in most aspects. Shanghai and Beijing have lower levels of standard market information and development stability than the other five cities. It has the highest tax the same level as Hong Kong and the highest government invention. Most of the survey respondents viewed the transparency,

especially in legal system, as low, legal enforcement as weak and financial market as not yet well established.

The results should be treated cautiously. The survey of Chin *et al.* was conducted in 2005 and improvements could have been achieved in the past seven years in these markets, especially the three emerging markets. The small sample size of the survey was the major limitation. For future studies, the questionnaire could be sent to Chinese domestic consultancy firms. The sample size could be enlarged to garner the domestic opinions of China's property market institution environment and market maturity process. The results could then be compared to the ones from international consultancy firms which were in this survey.

The degree and route of property market maturity varies in different countries. It is widely acknowledged that the underlying economic structure influences urban dynamics and property market activities. Beijing and Shanghai may not meet the traditional western criteria of mature and well-established markets, but these cities' influence on China and on the rest of the world is clear, with growing relevance and is instructive. A clear understanding of how property markets emerge, mature and perform over time in China together with an understanding of the differences in market maturity characteristics between China and other developed markets will be vital for international capital markets where perceptions of risk and pricing are influenced by traditional perceptions of maturity. The evolutionary trajectory of the two cities may influence the future shape of other Chinese cities and other global markets emerging in its wake. Understanding how the Chinese commercial property market develops and matures within its institutional environment would also help international investors to reduce uncertainty. This could arise from unknown effect on the outcome of property transaction, disposal and/or investment. It also has significant bearing on the risk premium that investors apply to Chinese investments.

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About the authors

Dr Qiulin Ke is a Senior Lecturer, Real Estate, at the Bartlett School of Built Environment, University College London. She has published papers in *Journal of Property Research*, *Journal of Real Estate Portfolio Management*, *Journal of Property Investment and Finance*, *Journal of Corporate Real Estate*, *Property Management*, etc. Dr Qiulin Ke is the corresponding author and can be contacted at: q.ke@ucl.ac.uk

Dr Karen Sieracki, BA, MA, PhD, MRICS, has been actively involved in property research and investment management for the past 27 years. She has had over ten years' fund management experience, during which time she created one of the first institutional property research departments in the UK. Dr Sieracki is a Visiting Professor to the Faculty of the Built Environment at the University of Ulster. She sits on the Education Strategy Group and the CPD Events Group for the Investment Property Forum. In addition, she serves on the Editorial Boards of the *Journals of Property Research*, *Property Investment and Finance* and *Journal of European Real Estate Research* and is a Royal Institution of Chartered Surveyors APC Assessor.

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