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First Comment: Property tax in China

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Chongqing, a city located at southwestern China, was given green light in principle from the Ministry of Finance in respect to introducing property tax on high-end property. The tax rate is expected to be about 1% and the imposition would be in effect as early as the first quarter of this year.

The launch of this tax is part of the government's effort to keep the sky-high house prices from rocketing further. Earlier measures taken with a view to curbing urban house prices have proven of little success. According to the China Real Estate Index System (CREIS), house prices in major cities of China soared by 20% in 2010.

We believe the imposition of the tax of about 1% is minimal given that house prices have risen by 20%. The impact on the overall property market would not be remarkable. Property buyers and speculators would be more or less indifferent to a taxation amounting to RMB 20k on property priced at RMB 2mn. Even if house prices this year increased half as much as they did last year, (i.e.10%), the 1% taxation would be well offset.

However the significance lies in the message sent to the public by the government: more stringent measures would be introduced until prices are kept under control. Chongqing city is the pioneer. It is likely that other major cities such as Beijing and Shanghai would follow suit, either on their initiatives or as required by the government. The imposition would be applicable not only to high-end property. The imposed tax rates are also expected to step up.

There is little wonder why the tax rate would start off at 1%. On the one hand the government is fighting sky-high prices; on the other hand the government is concerned about the social stability. Any large-scale one-off measures which might disrupt social stability are avoided. RMB appreciation is one of the typical examples.

In spite of the glamorous sales growth in 210 reported by mainland property developers, we are inclined not to include their stocks in our portfolio. We believe houses are generally overpriced. Plus we try to avoid sectors against which the government is set to have unfavorable policies.