

China Property Sector

What and when property tax will be?

After MOF and MOHURD hosted the meeting to discuss property tax on 12 May, some government think tanks further proposed Shenzhen and Hainan to be added in the trials after Shanghai and Chongqing. Our view is 1) the legislation would not happen so soon given the legislation process. 2) Trials in Shenzhen/Hainan are possible and essential to provide a successful model (curbing speculation and easing reliance on land sales). 3) We think the success lies on higher tax rate, inclusion of existing homes and houses in different cities. If trials roll out to Shenzhen/Hainan with higher rate and wide inclusion, it may have some negative impact on the sector sentiment (Agile for Hainan, Logan for Shenzhen). However the downside might be limited given that the sector is already trading at 1x 2020 P/B.

- **Is property tax legislation on the way? – Not so soon.** Legislation of property tax was first mentioned in 2013 as part of tax revenue and tools to curb property speculation. It has been formally added into the legislation planning in 2015. Since then the process has been slower than expected due to both technical reasons (nation-wide property network) and effectiveness debate. Until recently in May, MOF, MOHURD and other government parties discussed how to push forward the property tax, which indicates some progress. However we do not expect it to happen any time soon as 1) the legislation draft has not been submitted this year so technically earliest it will be next year. 2) So far there is no success model (Shanghai/Chongqing) in terms of either controlling property price nor easing the government financing reliance on land selling. 3) the economy is just on track to recover so adding tax burdens may hurt the trajectory. The more approachable ideas would be extending the trials to more cities such as Shenzhen or Hainan.
- **Why property tax trials in Shanghai/Chongqing were not so successful:** We think the reasons are **1) Tax rate is relatively low.** In Shanghai, the property tax rate is 0.4-0.6% per year together with 60 sq m exemption per family member for Shanghai Hukou and 30% discount to the property price. So it shows the maximal tax rate would be 0.42% (0.28% most of the time) of the property price per year which can be easily covered by rents yield of 1.5%. Also its contribution to total tax revenue was only 4% in 2019 which was hard to replace land selling. **2) The costs of property tax collection is relatively high** as it's based on personal declaration. The total 2019 property tax revenue was only RMB21bn compared to RMB47bn tax department expenses.
- **Would it be different if trials extend to Shenzhen/Hainan?** We think the key lies on the tax rate, treatment of existing units and houses in different cities. **1) If the tax rate could be close to rents yield say 1.5%,** then the holding costs would be much higher for the buyers and also the contribution to total tax revenue would be 20% in Shanghai's case. **2) Another key point would be extending the property tax to existing units with some exemptions.** Shanghai only charged property tax on new transactions. However for trials in Shenzhen, it would be better to extend to existing homes so that people with multiple units could release to the market. This would improve the overall supply together with demand curbing in the above. 3) Lastly we think it would be good to link the tax to all houses under the same person/family in the whole nation. As in Hainan, many property holders own units in different cities so this could stop loopholes for nation-wide rolling out.

OUTPERFORM
(Maintain)

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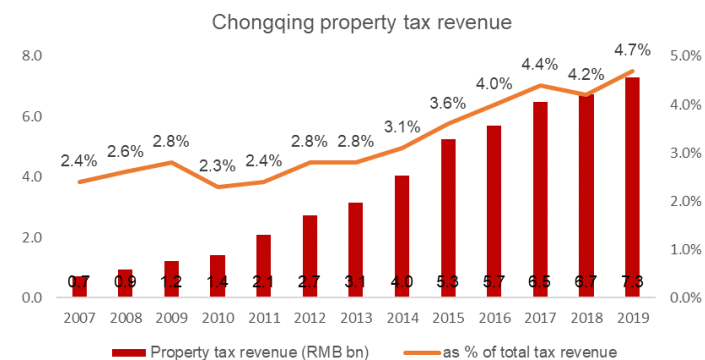
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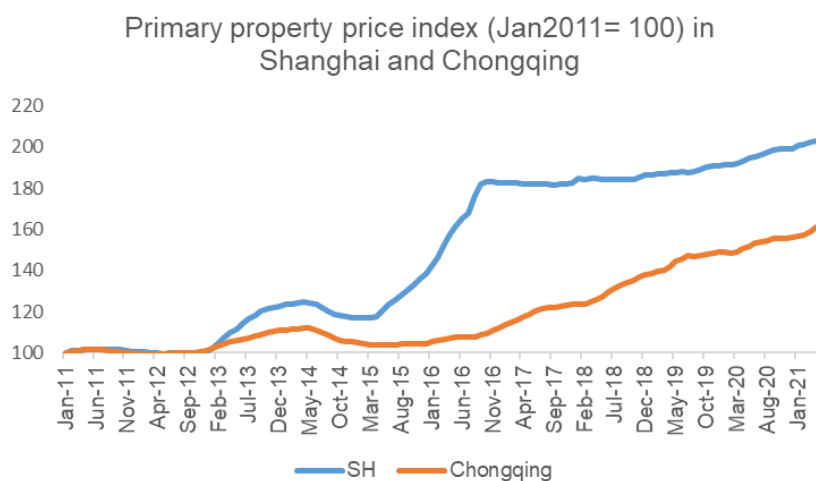
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Figure 1: Property tax in Shanghai

Source: MOF

Figure 2: Property tax in Chongqing

Source: MOF

Figure 3: Property price trend in SH and Chongqing since property tax rolling out

Source: CMBIS estimates

Figure 4: Property tax details in Shanghai and Chongqing

	Shanghai	Chongqing
Applicable area	Territory of Shanghai	Nine main districts of Chongqing
Taxable target	<ul style="list-style-type: none"> Shanghai resident families Newly-purchased second or subsequent residential properties Non-Shanghai resident families Newly-purchased residential properties 	<ul style="list-style-type: none"> Detached residential properties owned by individuals (including those purchased prior to 28 January 2011) Newly-purchased high-end residential properties Second and subsequent ordinary residential properties newly purchased by non-local residents who do not work or own companies in Chongqing
Taxable base	<ul style="list-style-type: none"> Transaction price is provisionally adopted at the initial stage Valuation price with reference to the market value may eventually be adopted 	<ul style="list-style-type: none"> Transaction price Valuation price will be adopted in the future
Tax rates	0.6% (0.4% in certain cases)	0.5% - 1.2%
Tax payable	Property tax payable = Taxable area of newly-purchased property (construction area) * Unit price (or assessed price) * 70% * Tax rate	Property tax payable = (Construction area of taxable residential property - Tax exemption area) * Unit transaction price * Tax rate
Potential exceptions	<ul style="list-style-type: none"> Shanghai residents <ul style="list-style-type: none"> Potential exemption if aggregate average floor area per family member is no more than 60 square metres Potential refund of property tax paid on new purchase if the new purchase is a replacement of the sole family residential property Potential exemption on purchase of first residential property by a grown up child Non-Shanghai residents <ul style="list-style-type: none"> Potential exemption for qualified "key talent" that hold resident permits, actually work and live in Shanghai and are purchasing their sole residential property Potential exemption for those who hold resident permits for more than three years and actually work and live in Shanghai and are purchasing their sole residential properties 	<ul style="list-style-type: none"> Family exemption <ul style="list-style-type: none"> 180 square metres for detached residential properties purchased prior 28 January 2011 100 square metres for newly-purchased detached residential properties and high-end residential properties <p>One family can only enjoy the exemption deduction once, and only on one property. There is no tax exemption for non-local residents who do not work or own companies in Chongqing.</p>
Effective date	28 January 2011	28 January 2011
Filing period	Annual	Annual

Source: KPMG

Figure 5: Valuation table

Company	Ticker	Last price (LC)	Mkt Cap (LC mn)	Rating	TP (LC)	P/E			P/B		NAV/share (LC)	Discount to NAV	TP Discount
						20A	21E	22E	20A	21E			
Vanke - H	2202 HK	26.20	361,593	BUY	33.92	6.0	5.3	4.9	1.1	1.0	48.47	45.9%	30%
COLI	688 HK	18.48	202,260	BUY	30.49	3.8	3.2	2.9	0.5	0.5	43.55	57.6%	30%
Country Garden	2007 HK	9.79	215,850	BUY	13.36	5.0	3.8	3.4	1.0	0.9	26.72	63.4%	50%
CR Land	1109 HK	36.05	257,070	BUY	44.79	7.2	8.0	7.0	1.1	1.1	63.98	43.7%	30%
Longfor	960 HK	46.05	279,306	HOLD	34.27	11.2	9.6	7.5	2.1	2.1	48.95	5.9%	30%
Shimao	813 HK	21.90	77,476	BUY	44.94	5.0	4.2	3.6	0.7	0.7	59.88	63.4%	25%
Agile	3383 HK	11.38	44,576	BUY	13.89	3.9	3.8	3.4	0.7	0.6	27.68	58.9%	50%
KWG	1813 HK	11.36	36,131	BUY	17.87	4.5	3.7	3.1	0.7	0.6	25.52	55.5%	30%
China Aoyuan	3883 HK	8.50	22,915	BUY	15.48	3.2	2.6	2.2	1.0	0.8	30.95	72.5%	50%
Times China	1233 HK	11.38	22,064	BUY	16.20	3.7	2.8	2.4	1.0	0.7	32.40	64.9%	50%
China SCE	1966 HK	3.43	14,482	BUY	5.60	3.1	2.8	2.3	0.6	0.5	9.34	63.3%	40%
Redsun	1996 HK	2.56	8,520	BUY	3.52	4.2	3.4	2.9	0.6	0.5	5.87	56.4%	40%
Sinic	2103 HK	4.16	14,852	BUY	4.95	6.3	5.6	5.4	1.5	1.3	9.90	58.0%	50%
Vanke - A	000002 CH	26.57	299,458	BUY	31.36	7.7	6.8	6.0	1.4	1.4	48.46	45.2%	35%
Radianse	9993 HK	4.68	18,932	BUY	5.55	4.4	3.8	3.2	0.9	0.6	13.87	66.3%	60%
Dafa	6111 HK	6.04	5,000	BUY	8.32	12.2	6.6	5.8	1.2	1.2	15.13	60.1%	45%
Shinsun	2599 HK	6.16	18,747	BUY	7.75	4.8	4.2	3.7	2.2	0.9	12.92	52.3%	40%
Dexin	2019 HK	3.11	8,401	BUY	3.56	5.9	4.0	3.7	1.4	1.1	7.12	56.3%	50%
Average						5.7	4.7	4.1	1.0	0.9		55.0%	40.8%

Source: CMBIS estimates

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