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Market Update Report: China
Month: June 2006

I. Market Trends:

?? Impact of new housing policy issued by the Chinese government on May 29, 2006

As a result of new macro-economic control policy effective from June 1, both the supply and sale of new residential units in Shanghai dropped last week from a week earlier as potential buyers and developers sat on the sidelines to see how the local government will implement new state regulations.

China's central government last month tightened mortgage, tax and land policies in a bid to curb property prices and ordered local governments to issue enforcement details. It wasn't clear when those details would be released. The effectiveness of the six new measures depends on whether the local governments will implement them fully.

The public reacted quickly to the new measures. An online survey showed that 77.48 percent would postpone their house-buying plans until the market becomes clearer.

Residential transactions within the inner ring road area dropped 24.1 percent from a week ago. Downtown prices rose 11.5 percent while most areas outside the inner ring road reported a slide in sales prices and transaction volume.

II. Recent Headlines of Importance to the Housing Industry/Building Materials Market:

✍ State may curb foreign funds buying properties (Shanghai Daily, June 23, 2006)

China plans to restrict purchases of real estate by foreign investors to reduce speculation and prevent a property bubble, a government official said. The Chinese government is worried that overseas investment is bringing too much foreign currency into China and that it will cause property bubbles. According to Lin Zheyang, deputy director general of the Commerce Ministry's Foreign Investment Administration, new rules defining what type of overseas investor can buy property may be announced this month.

Comments: China's reserves of foreign currency have doubled over the past two years to US\$875 billion as the trade surplus widened. Funds from all over the world are trying to get into Asia Pacific and China is on top of their list. With foreign investors poised to pour billions of dollars into Chinese real estate, restricting investment from overseas could help slow growth in foreign exchange reserves and ease pressure on property prices.

✍ **Builders troubled by state rules on apartment sizes** (Shanghai Daily, June 27, 2006)

The Chinese government established new real estate policies in May to continue its effort to rein in speculation and prices. But in some cases, the rules were general in nature, leaving ambiguities to be ironed out at the local level.

The central government, for instance, announced last month that local governments should ensure that 70 percent of all units built are no larger than 90 square meters. However, it did not make clear whether the 70 percent rule applies to a single project or to the total development in a particular area.

If the 70% applies to single project, many developers will be forced out of the market because small apartments mean higher costs and lower profit margins. But if the rule applies to total development in a particular area, it would require a lot of work by local governments in planning and quota allocation - and it raises the potential for corruption.

Industry analysts found the 90 square meters size figure to be arbitrary, especially if implemented nationwide. Yin Kunhua, a professor at Shanghai University of Finance and Economics, believes the 90 square meters figure may be appropriate for second- and third-tier cities but is too small for big affluent cities such as Shanghai and Beijing.

Comments: It is still unclear whether the central government will issue further guidance on its 90-square-meter policy or simply allow local governments to resolve the details.

Some developers are modifying designs to comply with the new rules while many have stopped working on their projects in anticipation of further clarity. Given the different interpretations of this new policy, developers don't know how to design their project's future phases and they have to halt future design due to the uncertainty.

Shanghai, which has halted issuing construction licenses, is expected to unveil its program within one to two months. Meanwhile Shenzhen in Guangdong Province has already unveiled its municipal regulations, specifying that the number of flats under 90 square meters must account for at least 70 percent of the units built in each project.

✍ **Property sales shrink while prices climb** (Shanghai Daily, June 26, 2006)

Last week, 3,432 new properties were sold, dropping 15.9 percent from a week earlier. The average price rose 13.1 percent to 9,576 yuan (US\$1,197) per square meter.

The transacted volume of residences, including villas, budget houses and apartments, decreased by 18.2 percent to 2,851 units, while prices jumped by 15.2 percent to 8,444 yuan.

The prices of apartments slightly dropped to 8,899 yuan per square meter last week, although the transacted volume dipped by 10.7 percent to 2,000. The sale of apartments inside the Inner Ring Road shrunk 24.1 percent, but prices rose by 11.5 percent. Both the sales volume and the price of apartments between the Inner Ring Road and the Outer Ring Road dropped.

Comments: It became more expensive to sell a home after June 1, since the government

imposed a 5.5 percent tax on the total sales price of a property that is sold within five years, up from the current two years. 5.5 percent tax will also be levied on the capital gain from "luxury" properties sold after five years.

Many analysts believe the new round of measures designed to cool the property market will be more effective than those implemented in 2004 and 2005, because they focus more on slowing the demand growth and boosting the supply.

III. PROJECTS: This section consist of housing developments and other projects that could mean opportunities for US exporters, sites that people may want to visit for research, and content for the Chinese newspaper and US newsletter.

?? Shanghai Sheshan (Zhongkai) Villa project

Shanghai Sheshan (Zhongkai) villa project includes 81 villas located in Sheshan area, suburb of Shanghai. It is a very unique project developed by Shanghai Zhongkai Real Estate Co., Ltd.. The developer invested almost RMB100 million inviting ten US architectural firms to do the initial architectural design. Meanwhile it also invited four local architectural firms to do the final design. It aims to complete the project by the end of 2007. It is likely that they will use some imported building materials such as windows & doors. Landscaping design is still in the process.

IV. TRADE LEADS: See attached China Inquiry Summary Sheet.

V. ACTIVITIES:

1. Shanghai International Real Estate Summit and Expo, June 5-7, 2006
2. Visit program arrangement for CINTRAFOR research visit in Shanghai, June 12-16, 2006
3. Pre-mission trip to Qingdao and Guangzhou, June 20-23, 2006
4. Database Update