China’s Senior Housing – Now and the Future
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China’s ageing population has received growing attention in recent years bringing the issue of "elder care" to the forefront of policy makers, and organizations’ minds. Two significant factors: modernization which has weakened the traditional function of “family support” for the elderly, and the inability of traditional institutions to meet the diverse needs of the elderly, have heightened the need for quality "elderly care" options. As China’s elderly population grows at an accelerating rate, many businesses now view elder care as a “sunrise industry” which can offer attractive returns for investors. Today, growth in China’s senior housing market is presents both tremendous opportunities and challenges.

In this report, Deloitte analyzes China’s senior housing market - where it stands and how it will evolve. Although real estate developers play a central role in the market, elder care service institutions, insurance companies and fund companies are also increasingly important investors. Our study reveals that cooperative opportunities exist between investors/companies of different types. For instance, management and operational cooperation between real estate developers and elder care service institutions as well as joint venture projects between local industrial groups and foreign investors are just two of the many cooperative models to emerge. The various strengths that different investors from varying sectors bring to the table have proven advantageous in quality, operation, and financing.

Although future demand presents opportunities, investors are also facing challenges such as mismatched demand between facility and service provision and the overall market, inconsistent development and implementation of related government policy, financing channel restrictions, and others. These challenges are decisive factors which will affect the operation of senior housing projects and return on investment. For instance, in terms of government policy, the Chinese government has introduced measures in support of the elder care industry that offer preferential tax treatments and subsidies to encourage investment and develop the industry but many gaps exist within these new policies, laws and regulations. In the meantime, unified standards or norms are not in place to safeguard the development and regulation of the industry.

Compared to the Chinese elder care industry which is in a preliminary stage, the senior housing and service market in some foreign countries has matured under different modes of development. For example, the elder care industry in the UK is led by the government while in the US; it fully relies on market development. The difference is attributable to the history, stage of economic development, and the different perspectives of their citizens on the traditional concept of family. The Chinese elder care industry may be developed and the system may be perfected by integrating foreign experiences with local cultural tradition and actual demands.

In addition, due to the complicated Chinese taxation system, the investment in and operation of the senior housing and elder care service industries have fallen under the jurisdiction of many types of Chinese taxes. Toward the end of this report, we have specifically compiled the Appendix that includes the Chinese taxes relative to the elder care industry and have given a brief overview on the basics of the senior housing industry and the preferential government policies. Also, an Appendix about overseas Renminbi Real Estate Investment Trust (CNH – REIT) is attached to the report to assist you in understanding how this investment tool can help you profit from the potential opportunities in the senior housing market.

This report may not have been completed without the full support of real estate developers and medical service institutions. We would like to give our special thanks to Poly Real Estate (Group) Co. Ltd., Orpea China and those who have made intellectual contributions to this study.

Yvonne WU  
Managing Partner  
Deloitte China life sciences & health care

Richard HO  
Managing Partner  
Deloitte China Real Estate
In 2013, 132 million people in China, or 9.7% of the general population were over 65 years old, and the elderly dependency ratio had increased to 13.32% from 11.17% in 2007. According to a forecast by the Population Division of the UN Department of Economic & Social Affairs, China’s elderly population is expected to grow by more than 8 million per year, accounting for 30.8% of China’s total population by 2050. Over 100 million out of the approximately 430 million elderly people will be over eighty years old (Figure 1). Compared to a global aging rate of 2.5% annually, China is aging at a rate of 3.3%.

The enormous number of the elderly in need of care signals a great opportunity for elder care facilities and services. The Guidelines by the State Council on Accelerating The Development of Elder Care Service Industry issued in 2013 states that developing elder care facilities is one of the main tasks in the development of the elder care service industry in China. According to the recently issued Guidelines on Accelerating The Development of Elder Care Service Industry, the State Council demands sufficient expansion of elder care capacity to allow 35-40 beds per thousand elderly persons by the end of 2020, which will be double the current level. If we assume that capacity remains unchanged at the level of 35-40 beds per thousand elderly persons (an increase of 15-20 beds per thousand elderly), a 260-million elderly population by 2050 will represent a potential demand of 3.9 to 5.2 million new beds for elder care in China.

As a result, investors from a wide range of industries have entered the senior housing market in recent years. Over eighty elder care facility programs whose information has been disclosed to the public are located in the cities of Beijing and Shanghai, and the provinces of Zhejiang, Hainan, Shandong, Sichuan, and Guangdong. In addition to real estate developers, insurance companies and specialized elder care service institutions have invested in the construction and operation of elder care facilities. In terms of product structure, a variety of care facilities and services have been designed to meet the different needs of the elderly at different ages. Regardless, the development of profit models are still in the initial stages.

Figure 1: Forecast of China’s elderly population and % over total population in 2007 through 2050

Mr. Fu, executive general manager of a large-scale real estate group
Rapid economic growth in China has dramatically improved the people’s quality of life, as well as their health, and extended their life spans. Meanwhile, a modern family structure and rhythm of life, combined with people’s greater mobility and greater convenience is forcing the Chinese to change their traditional way of caring for the elderly. Over the next 15 years, the first generation of parents affected by the one-child policy will be entering their eighties and thus will be in need of more professional care, triggering an explosive demand for senior housing.
1. Real estate developers are leading the market with participants from other industries to test the water. The development potential in senior housing has drawn investors from a wide variety of industries including real estate developers, insurance companies, elder care service institutions, industrial groups and other financial investors who have assumed different or overlapping roles (Fig. 2). Generally speaking, real estate developers make up the principal share in senior housing development and the operation of elderly service facilities. Elder care service institutions focus on providing care service with some involvement, to a certain degree, in senior housing development. Insurance companies, on the other hand, play their role by integrating senior housing development and operations of service facilities with insurance and wealth management products, while directly funding some high-quality projects. Meanwhile, other investment institutions participate in the senior housing market in different ways.

1.1 Real Estate Developers – Major force in Development and Construction
Due to their experiences accumulated over years in real estate development, developers are taking the lead in senior housing development and construction. According to some publicly listed documents, over thirty real estate developers have entered senior housing development and operations, and over eighty others have expressed a willingness to enter the market. Specifically (See Table 1 for detail), Vanke has pilot projects including Beijing Xingfuhui and Hangzhou Liangzhu Culture Village. Poly Real Estate has pilot projects in Beijing Hexihui and Shanghai Xitangyue. Backed by China Life—a major shareholder—and together with Emeritus from the US, Sino-Ocean has committed to building the elder care brand “Senior Living L’Amore,” and has begun operating apartments for the elderly in Yizhuang, Beijing. Meanwhile, apartments for the elderly built by a well-known real estate developer have been opened for occupants in Hangzhou. The developer has also invested in the construction of senior housing projects, such as Yada International Health and Ecology Industry Park in Wuzhen.

Sensing the vast market potential, many real estate developers have decided upon senior housing construction as their strategic development aim, as well as an opportunity for business transformation, revenue restructuring and change in their growth model. Nonetheless, senior housing presents developers with higher requirements than traditional housing. First of all, developers need to strengthen their ability to integrate their resources relative to their needs in elder care such as medical treatment, health care, and entertainment etc. Secondly, the huge investment in senior housing and a relatively longer payback period require developers to enhance their ability to secure long-term financing at reasonable cost. Meanwhile, senior housing development puts developers’ abilities for long-term project operations and management to the test.

Figure 2:Investors show enthusiasm in senior housing market

Sources: Deloitte Analytics
Table 1: Ongoing Senior Housing Projects by China’s Leading Real Estate Developers

<table>
<thead>
<tr>
<th>Developer</th>
<th>Senior Housing Projects</th>
</tr>
</thead>
</table>
| Vanke           | • Elder care products are incorporated in projects such as Fun City of COFCO Vanke and Beijing Huangqincheng of Minmetals Vanke  
                  • Vanke Xingfuhui in Fangshan of Beijing, which owns 146 pilot elder care service apartments that provide services to energetic and senior intellectuals  
                  • Offers about 60 apartments for the elderly in Xianghe, Hebei  
                  • Built 60 apartments for the elderly in northern Qingdao to provide services to mid to high-end seniors over 60.  
                  • Vanke Suiyuanjiashu (Dignified Life) located at Liangzhu Culture Village in Hangzhou is a high-end elder care apartment complex building  
                  • Invested RMB 12 billion in the construction of a health and elder care residential neighborhood and a cultural and creative industry project in Changchun. |
| Poly            | • Poly Hexihui which is located inside West Hill Imagination, covers a construction area of more than 20,000 square meters with a capacity of 400 beds, serving the semi-disabled elderly.  
                  • Offers elder care service within Poly Xitangyue project in Zhejiang. |
| Greentown       | • The Bluepatio Project in Linping of Hangzhou is planned to have 86 apartments for the elderly and 60 beds in its nursing home with supporting facility such as university for the elderly, health center, entertainment center, community hospital, and nursing home.  
                  • Yada International Health and Ecology Industry Park in Tongxiang, Zhejiang encompasses 6,000 apartments for the elderly under the themes of leisure, health and elder care to provide all-round service. |
| Sino-Ocean      | • Joining hands with Emeritus, the largest senior living service company in the US to build Senior Living L’Amore in Ocean Palace at Yizhuang, Beijing, which covers a construction area of nearly 6,000 square meters and offers 89 apartments to provide high-end elder care service. |
| Fosun Group     | • The Starcastle Zhonghuan Elder Care Community jointly developed with Fortress Investment Group opened to tenants in May of 2013. |
| Greenland Group | • Introduced Xiaoxianfang in 21 cities as early as 2004; it is an all-inclusive elder care project. |
| Shanghai Industrial Investment | • Invested RMB 10 billion to build “Elderly Community” in Dongtan of Chongming, Shanghai, which provides continuous care to over 10,000 seniors. |
| Fantasia        | • Launched two pilot elder care service stations in Yueliangwan, Shenzhen that provide medical, living, catering, and spiritual care services.  
                  • Acquired the plot originally assigned for the TCL project in Nanshan, Shenzhen to build senior housing—a health-related industry park that offers medical inspection, sports, athletic training, and physical therapy services to the elderly. |
| Shangyou        | • Developed and operates the Oriental Sun City in Shunyi, Beijing. The community is mature now and Shangyou is planning to expand by chain projects in places like Shandong and Hainan. |
| Taiyangcheng   | • Developd and operates Taiyangcheng community in Xiaotangshan of Changping, Beijing. The community is equipped with a hospital, Chinese medicine hospital, cultural center, shopping center, housekeeping service center, holiday hotels, hot spring club and other elder care facilities. |

Source: Deloitte analysis (compiled based on open information and company website)
Poly Real Estate – integrating three modes into one to build the elder care industry

Among all the senior housing developers, Poly Real Estate (Group) Co. Ltd. is no doubt one of the leaders. So far, the company has made plans or constructed seven senior housing projects in five cities including Beijing, Shanghai, Guangzhou, Chengdu, and Sanya, one of which—Hexihui at Beijing West Hill - has been operating since the end of 2012.

As part of the West Hill Imagination project at Beijing by Poly Real Estate, Hexihui was originally built as a support facility for a rated hotel. It later underwent a RMB 30m transformation and was turned into an apartment for the elderly covering 7,000 square meters with a construction area of approximately 20,000 square meters. The complex has 200 rooms, 400 beds and is equipped with a clinical building in the west, a 999 ambulance station, and a physical treatment and rehabilitation center on the second floor. By the end of 2013, 110 seniors, most of them aged or semi-disabled, were in residence there. Presently, Hexihui offers differentiated discounts on monthly fees for its beds, meals, treatment and care based on three levels of membership fees (RMB 50,000, RMB 100,000 or RMB 200,000). After over one year of operation, Hexihui is still struggling to make ends meet. Despite the high costs of construction on the project, the promised subsidies and preferential policies have not yet been put in place. In addition, its services are not covered by medical insurance due to a lack of strong support from the government, which affects its occupation rate.

Poly Real Estate selects to pilot its first senior housing project in Beijing for the following reasons: First of all, unlike other welfare elder care organizations, Hexihui serves seniors with middle to high net worth. Beijing outnumbers other cities in terms of high income and senior intellectuals. Secondly, Beijing is equipped with abundant medical resources of the highest quality in China, which ensures that the medical and health needs of these customers are met. Therefore, Beijing Hexihui is charged by Poly Real Estate with the responsibility of testing the commercialization of the senior housing development. As a window of Poly Group, Poly Anping was established to specifically provide elder care service for the entire group, build and promote Hexihui as an elder care brand, and be responsible for its operations and management.

Poly Real Estate has developed a strategy to achieve profitability for its senior housing development. In the short term, it will invest in senior housing construction and operations. The revenue from the sale of elderly-friendly housing will be used for the research and development of other elderly-friendly products and in transforming other products into elderly-friendly supporting facilities. In the medium term, Poly Real Estate expects to spend three to five years to transition to a stage where their facilities are operated smoothly and a break-even is achieved. In the long term, it plans to bring its senior housing and service product development up to the same profitability level as in Western countries. Meanwhile, it plans to clear up the financial channel and to pave the way for Real Estate Investment and Trust Funds ("REITs") to eventually go public.
In the future, Poly Real Estate will be present across the entire elder care business sector, aiming to create a Chinese elder care business model that “integrates three modes into one” – institutional, community, and home care. Poly Real Estate plans to build 50 elder care institutions within ten years that have the capacity of 200–300 beds each. Meanwhile, in each newly built community of 500,000 square meters or more, it plans to build apartments of 10,000 or 8,000 square meters as homes for the elderly. Over the next two to three years, it plans to invest RMB 300m to 500m in the renovation of older neighborhoods to make them more elderly-friendly, with more options for care and services. In addition, Poly is planning to leverage its current project resources and customer base to test launch senior housing projects in the form of senior tourism, timeshare or other “migratory bird” types in cities such as Sanya, Chengdu, and Lijiang that boast beautiful scenery and pleasant climates.

In July, 2014, China International Silver Industry Exhibition jointly sponsored by Poly Real Estate and China National Committee on Ageing was held at the Poly World Trade Center in Guangzhou. The exhibition served as a platform for establishing the Alliance of Elder Care and Elderly-Friendly Industries in China, streamlining the elder care industry chains, ensuring the quality of elder care and elderly-friendly products and promoting the sound development of elder care industry.

Sources: company websites, interviews and analysis by Deloitte
In addition to providing housing that suits the elderly and the care and treatment that satisfy their daily needs, senior housing providers should also be capable of meeting the desires of those elderly pursuing a high-quality lifestyle. Therefore, it is desirable for the developers of senior housing to build, maintain and operate supporting facilities for elder education, culture, sports, entertainment, tourism, as well as those that meet the more basic needs for nourishment, health management, medical treatment, and healthcare. The elder care service institutions that provide these products and facilities are at the leading edge of the senior housing market.

Although China’s elder care service is in its infancy, we have observed that more and more investors are being drawn to the market. Table 2 reveals that the majority of China’s elder care industry offers aid or long-term elder care service in physical elder care facilities such as apartments for the elderly, service centers, and nursing homes, supplemented by professional home care and treatment services.

Many foreign elder care agencies have begun to enter the Chinese domestic market by forming joint ventures with Chinese counterparts, or by setting up independent elder care service companies in the hopes of capturing market share in the Chinese elder care service market. Unlike the strategy employed by those real estate developers who are focusing on senior housing development, the elder care institutions currently operating in China, especially the foreign-owned ones, mainly offer elder care services from the facilities they rent and renovate in residential neighborhoods inside the cities.

Table 2: Projects administered by privately-owned Chinese or foreign elder care service institutions

<table>
<thead>
<tr>
<th>Company</th>
<th>Senior housing &amp; service items</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cherish Yearn Co. Ltd.</td>
<td>• Owns and operates Qinhe Apartments for the Elderly, Qinhe Nursing Hospital, and other physical elder care institutions supported by daily life and professional care and medical facilities.</td>
</tr>
<tr>
<td>Aixin Elder Care Group</td>
<td>• Owns and operates eight large-scale physical elder care institutions including Taiwanese Apartments for the Elderly, Riverside Apartments for the Elderly, Wanghuzhai Apartments for the Elderly, Housekeeping Center, and Sun City Elderly Service Center.</td>
</tr>
<tr>
<td>Huichen Elder Care Institution Management</td>
<td>• Is building apartments for the elderly at Beiqijia, Beiyuan, and Wangjing in Beijing; conducts training for nursing certifications; and develops, manufactures and sells products for the elderly.</td>
</tr>
<tr>
<td>Yanda International Medical Investment Management</td>
<td>• Operates Yanda Golden Age Health Nursing Center and other elder care Institutions that provide medical, rehabilitation, health management, daily care and nursing services.</td>
</tr>
<tr>
<td>Pinetree Senior Care</td>
<td>• Provides professional home care to the seniors in Beijing who suffer from being bedridden, senile dementia, diabetes, and stroke, etc.</td>
</tr>
<tr>
<td>Haiyang Elderly Development and Service Center</td>
<td>• Provides professional daily home care and rehabilitative care, community life service, and community security services.</td>
</tr>
<tr>
<td>Kajian Huazhan Elder Care (US)</td>
<td>• Provides professional elder care services in Shanghai and Beijing including rehabilitation, nursing homes, apartments for the elderly, centers for elders with dementia, and continuous care communities.</td>
</tr>
<tr>
<td>Ciaijia Elder Care Service (US)</td>
<td>• Provides professional and specialized nursing and accompanying services to seniors, patients, the disabled, and other people who need nursing service, such as people in post-operation or terminal care at Beijing, Jilin, Sichuan, Hubei and Zhejiang.</td>
</tr>
<tr>
<td>Starcastle Elderly Service (Sino-US joint venture)</td>
<td>• Operates high-end senior life communities that provide daily care and nursing, and medical services in Shanghai.</td>
</tr>
<tr>
<td>Weisifuzhi Business Consulting (Sino-Japan joint venture)</td>
<td>• Has established Lai Nursing Home in Shanghai to provide self-care, semi self-care, full care, Alzheimer’s disease (senile dementia) care, postoperative rehabilitation and short-term care and rehabilitation, and family villa-style vacation service.</td>
</tr>
<tr>
<td>Liai Enterprise Management Consulting (Sino-Japan joint venture)</td>
<td>• Establishes Liai Nursing Home in Shanghai to provide self-care, semi self-care, full care, Alzheimer’s disease (senile dementia) care, postoperative rehabilitation and short-term care and rehabilitation, family villa style vacation service etc.</td>
</tr>
</tbody>
</table>

Sources: Everbright Securities resources, Deloitte analysis
US Fortress Investment Group – building an urban elder care community with a local partner

In August 2012, Fortress Investment Group, an experienced operator in the elder care business, established Starcastle Elderly Service Co. Ltd. as a joint venture in partnership with Fosun Group. Starcastle’s first flagship community—Starcastle Zhonghuan Elder Care Community—launched operations in May 2013. Fosun Group is China’s largest private enterprise, engaging in a wide range of businesses such as medical service, real estate operations, tourism, pensions, insurance, and financial investment.

Located in Baoshan, a suburb of Shanghai, the Starcastle Zhonghuan Elder Care Community covers a total area of 18,000 square meters. It employs a fee model that differs from those of any other senior housing projects or social elder care centers. In addition to residential space, its all-inclusive monthly fee also covers three meals a day, public utilities and maintenance, housekeeping, 24-hour emergency medical response, and an in-community medical clinic. The senior residents who live there spend from RMB 5,000–30,000 on a monthly basis, depending on their floor plan. In addition, a RMB 50,000 down payment is required before moving in to cover the internal furnishings, electrical appliances, an evaluation of the condition of the prospective resident’s health, and preparation of an individual care plan.

The community has a total of 150 individual units that offer various room types from one-bedroom to large two-bedroom apartments. It also has room for public activities such as a dining room, a cafeteria, an elder-friendly fitness center, a room to play mahjong and cards, an art room, a classroom, a library, a teahouse, a computer room, and a clinic that provides both Western and Chinese medicine and treatment. In addition, it has the capacity for 50 people to live individually or as couples who need aid while living there, such as assistance in bathing, administration of medications, dining, and clothing. It also provides care to dementia patients, onsite medical treatment, occupational and language treatment services. Starcastle Zhonghuan Elder Care Community operates from a rented facility. In the future, it will invest in more such communities in Shanghai or even throughout China.

Sources: company website, telephone surveys and analysis by Deloitte
1.3 Insurance institutions – long-term capital provider

Thanks to the vast amount of long-term capital accumulated over an extended period of time, insurers have a unique competitive edge in the market. On the other hand, elder care communities are good investments for life insurance companies due to the large investment required, long investment cycle, steady capital inflow toward the middle or the end of the projects, higher long-term comprehensive return on investment, and stronger resistance to risk. To invest the premium income from life insurance policies in the elder care industry not only opens up new investment opportunities for life insurance capital, but also eases the difficulty of implementing the elder care industry’s long-term plan, as well as solves the problem of insufficient capital in elder care communities.

The rapid accumulation of life insurance funds makes it possible for their investment in elder care. In recent years, China’s insurance institutions have absorbed high volumes of life insurance capital. By 2013, life insurance premiums collected in China had reached RMB 1.0741 trillion, a figure that had grown at a compound rate of 13.6% over the preceding ten years. Meanwhile, legislation and policies have paved the way for investing life insurance capital in elder care enterprises. In 2008, The Guidelines on the Current Financial and Promoting Economic Development issued by the General Office of the State Council clearly specifies to “support related insurance institutions to invest in medical institutions and physical elder care organizations”. The new Insurance Law that came into effect on 1 October 2009 explicitly states that earnings from insurance premiums may be invested in real estate, paving the way for insurance capital to be invested in the elder care industry and in the development of elder care communities. In addition, Article 11 of The Outline of “Twelfth Five-Year” Plan on the Development of Insurance Industry in China issued in 2011 specifies to “support the investment in the life insurance service industry by insurance institutions that meet the requirements.” Article 34 states, to “drive the research on tax policies in support of investment in the elder care industry and involvement in the reform of the medical and health system by means of insurance capital.”

In fact, a few insurance companies have made the move. Taikang Life has acquired a 329-acre (133-hectare) “pilot zone” in Wenquanxiang at Xiaotangshan where it will invest RMB 4 billion in the development of an elder care community. Union Life is building “Union Health Valley,” a project in Wuhan that is designed to be a modern high-end service industry platform that provides functions such as nourishment, elder care, tourism and vacationing, rehabilitation, and medical services. Other companies, including Taiping Life and Ping An Group have all launched their own projects. (See Table 3 for details.)

Table 3: Current senior housing projects invested by leading insurance institutions in China

<table>
<thead>
<tr>
<th>Company</th>
<th>Senior housing projects</th>
</tr>
</thead>
</table>
| Taikang Life  | • Taikang Elder Care Community is located at Xiaotangshan in the district of Changping, Beijing. It covers a construction area of 300,000 square meters with 3,000 households, and offers a community park, a recreational farm, a fitness center, a school, a hospital for rehabilitation, other support facilities. It also offers 24-hour housekeeping service.  
• Taikang Life plans to establish a chain of elder care communities nationwide. |
| Union Life    | • Is building “Union Health Valley” in Wuhan, Hubei. Encompassing a five-square-kilometer tract, the project has cost a total of over RMB 20 billion and is divided into two parts: Tongji Health Community and Union Life Health Community. It integrates many functions such as medical treatment, rehabilitation, recuperation, physical examination, fitness, nourishment, elder care and vacationing. Phase I is an elderly home care with a capacity to serve 50,000 seniors. |
| NCI           | • “Xinhuaijia yuan” in Yangqin, Beijing, is under construction. The project in Miyun has been approved by the Board of Directors.  
• NCI has established health management centers at Xian and Wuhan. |
| Taiping Life  | • Has spent RMB 2 billion in building Zhoupu Elder Care Community in Shanghai.                                                                 |
The availability of long-term capital enables insurance companies to build and operate elder care communities that offer all-round continuous service and to build a nationwide blanket brand name in chain operations. Meanwhile, insurance companies may bind-sell their insurance wealth management services with the services they provide to their current customers to ensure that the operation of the elder care service facility receives steady cash funding.

### 1.4 Other investors – important supplements in the market

In addition to real estate developers, elder care service, and insurance institutions, other investors in China’s senior housing market have included enterprise groups, trust companies, and investment funds. Tables 4 and 5 reveal that enterprise groups such as Hiking Group, Clifford Group, Baosteel Construction and Bright Food have been involving in the development and operations of elder care facilities, while trust institutions have been financing trust schemes for senior housing projects.

### Table 5: Senior housing trust schemes issued in recent years

<table>
<thead>
<tr>
<th>Trust company</th>
<th>Trust scheme</th>
<th>Year of issuance</th>
<th>Duration</th>
<th>Amount</th>
<th>Expected ROI</th>
<th>Investment areas</th>
</tr>
</thead>
<tbody>
<tr>
<td>China Railway Trust</td>
<td>“Shangjinnanfu Hospital – Elder Care Center” collective fund trust scheme</td>
<td>2010</td>
<td>18 months</td>
<td>RMB 110 million</td>
<td>7.30%</td>
<td>Specifically used for development of “Shangjinnanfu Hospital- Elder Care Center”</td>
</tr>
<tr>
<td>Anxin Trust</td>
<td>Care Series “Sunshine II- Care” collective fund trust scheme</td>
<td>2010</td>
<td>One year</td>
<td>RMB 200 million</td>
<td>6%</td>
<td>Elder care service industry and livelihood projects</td>
</tr>
<tr>
<td>CITIC Trust</td>
<td>Juxihuixing Senior Housing Xingyao Health City I collective fund trust scheme</td>
<td>2011</td>
<td>2-4 years</td>
<td>RMB 1.024 billion</td>
<td>2 years: 10-19%, 3 years: 10-21%, 4 years: 10-23%</td>
<td>Xingyao Health City</td>
</tr>
</tbody>
</table>

**Table 4: Senior Housing Projects by other enterprise groups**

<table>
<thead>
<tr>
<th>Company</th>
<th>Senior housing projects</th>
</tr>
</thead>
<tbody>
<tr>
<td>Hiking Group</td>
<td>• Partners with Long Life Group of Japan to spend RMB 300 million in developing and operating a high-end elder care institution in Laoshan, Qingdao—Hiking (Qingdao) Long Life Care Service Center.</td>
</tr>
<tr>
<td>Clifford Group</td>
<td>• Owns Guangzhou Clifford Elder Care Apartment, the first hotel-style apartment for the elderly that has attracted seniors from Hong Kong, Guangzhou, and Shenzhen.</td>
</tr>
<tr>
<td>Baosteel Construction</td>
<td>• Joins with Design Investment in spending RMB 15 billion to build China Leling City in Mianyang—the first innovative urban complex that houses seniors as well as headquarters of enterprises run by “elite seniors.”</td>
</tr>
<tr>
<td>Bright Food</td>
<td>• NGS Real Estate, a subsidiary of Bright Food, is partnering with Chang Jiang Corp to develop the Bright Chongming Health Manor project. The project is expected to be launched at the end of 2015 to early 2016 with the first-phase of investment reaching RMB 2 billion. It is planned to occupy a 329-acre (133-hectare) trace, of which 115 acres (46 hectares) are to be used in real estate development, and 214 acres (87 hectares) are to be used for vacation, tourism, and ecological construction purposes.</td>
</tr>
</tbody>
</table>

Sources: open information, Deloitte analysis. This table does not list all projects; these are examples only.
The lack of maturity in China’s elder care industry has cooled the enthusiasm of many investors who are waiting for the business environment to improve. However, statistics from ChinaVenture indicate that some private equity funds specializing in the Chinese elder care industry have started or finished raising funds. With the market potential continuing to be released from the acceleration of ageing, industry policies getting clearer and business models becoming more mature, we expect that more capital will be funneled into this market.

Table 6: Samples of private equity funds specialized in China’s elder care industry

<table>
<thead>
<tr>
<th>Name</th>
<th>Size</th>
<th>Nature</th>
<th>Status</th>
<th>Detailed description</th>
</tr>
</thead>
<tbody>
<tr>
<td>Denmark – China Elder Care Industry Investment Fund</td>
<td>RMB 100 million</td>
<td>Sino/Foreign JV</td>
<td>Fund raising completed</td>
<td>The government has provided initial funding to the Denmark – China Elder Care Industry Investment Fund and will primarily invest in three areas: firstly, high-quality projects in the elder care industry; secondly, projects in the elder care industry that have promising growth potential, are preferably treated by policies, of the science and technology type, and have resource advantage; thirdly, projects leading to the integration of the industry.</td>
</tr>
<tr>
<td>Qing Geng Elder Care Industry Investment Fund</td>
<td>N/A</td>
<td>Chinese</td>
<td>Started raising funds</td>
<td>Qing Geng Elder Care Industry Investment Fund is the first investment fund in China that focuses on elder care industry investment. It was jointly established by China Chengtong Asset Management Co. Ltd – a central enterprise owned and managed by the State Assets Supervision and Administration Commission, and Beijing Qing Geng Investment Management Co. Ltd. It is operated by a management team consisting of senior experts from China ChengTong, Beijing University and Oxford University.</td>
</tr>
<tr>
<td>Hong Fu Elder Care Industry Investment Fund</td>
<td>N/A</td>
<td>Chinese</td>
<td>Fund raising completed</td>
<td>Hongfu Elder Care Industry Investment Fund was established by Tianjin Hongfu Equity Investment Fund Management Co. Ltd. It specializes in the investment of elderly-friendly communities, institutions for the elderly, and an elder care industry science and technology park.</td>
</tr>
<tr>
<td>China Health and Elder Care Industry Development Equity Investment Fund</td>
<td>RMB 1.5 billion</td>
<td>Chinese</td>
<td>First-round fund raising</td>
<td>China Health and Elder Care Industry Development Equity Investment Fund is a remanibi fund managed by Yinhong (Tianjin) Equity Investment Fund. It has a size of RMB 1.5 billion and was established particularly to gain from the great potential of China’s health and elder care industry.</td>
</tr>
<tr>
<td>Ping An Elder Care Industry Equity Investment Fund</td>
<td>RMB 10 billion, RMB 2.5 billion in Phase I</td>
<td>Chinese</td>
<td>First-round fund raising</td>
<td>Ping An Elder Care Industry Equity Investment Fund was established on 29 December 2012 by Shenzhen Ping An Real Estate Co. Ltd. China Ping An Insurance (Group) Co. Ltd. has contributed 30% and the Social Security Fund has contributed 40% to the total investment.</td>
</tr>
<tr>
<td>Hai Fan Elder Care Industry Phase II Fund</td>
<td>RMB 500 million</td>
<td>Chinese</td>
<td>First round fund raising</td>
<td>Hai Fan Elder Care Industry Phase II fund specifically invests in elder care industry in the combined form of equity and debt investment.</td>
</tr>
</tbody>
</table>

Sources: ChinaVenture, Deloitte analysis
2. Structure of products is getting elaborate but not to scale yet
Although China’s senior housing industry is still in its infancy, the number and sophistication of its ongoing and planned projects indicate that a preliminary structure has been put in place with products that can meet different needs of the elderly at different ages and different conditions of health (Fig. 3). The current senior housing in China may be classified into permanent or transient housing based on the duration of stay. In terms of functions, they can be classified among elderly-adapted housing, housing for all-round living, continuous care retirement housing, and apartments for the elderly.

- **Current ordinary residential communities** - Today, most of the elderly in China own their housing directly or indirectly and wish to live in a familiar community. They have not shown a strong interest in living in elder care institutions such as an elder care community or apartment for the elderly. Therefore, some real estate companies have invested in their current residential real estate projects to renovate and transform the facilities, living environment, and supporting services to adapt them to the aging society. Others choose to establish elder care service centers to provide meal service, housekeeping, medical aid, and organization of entertainment activities.

- **Newly-constructed all-round residential communities** - These are communities with both young and old residents. Generally, each of these communities is large and is located outside the inner city, accessible by a gradually improving public transportation system. Developers usually hold and operate a small area for elder care purposes and rely on the revenue from selling other properties from the ensuing development and operations. Meanwhile, living together with their children makes it possible for the elderly and their children to take care of each other while avoiding conflicts which result from different habits in life. The elder care facilities in these communities include both the basic community elder care service as well as more professional and long-term services such as aided-living, care, and nourishment.

- **Continuous care retirement community** - This is a community established specifically to meet the needs of the elderly. It offers facility and services such as self-care, assisted care and assisted housekeeping to senior residents of different ages and different levels of health in the community, which enables the senior residents to spend most of their elderly lives in a familiar community. It not only requires that the continuous care retirement community be developed with the living and spiritual demands of the elderly in mind, but also that these be customized and specify the subsequent care services, which puts a higher demand on the comprehensive ability of the developer and managers of the project.

Sources: Deloitte analysis

Figure 3: Structure of China’s current senior housing products

- Permanent senior housing
- Migratory senior housing
- Elderly-adaptation renovation
- Community elder care service center
- Elder care facility by proportion
- Aided-living, care, nursing
- Elder care, health and vacation centers
- City A
- City B
- City C
- ……
- Tourism and vacation
- Health and nourishing

Specifically, each type of senior housing has its own characteristics and functions.

- **Current ordinary residential communities**
  - Today, most of the elderly in China own their housing directly or indirectly and wish to live in a familiar community. They have not shown a strong interest in living in elder care institutions such as an elder care community or apartment for the elderly. Therefore, some real
• **Stand-alone apartment for the elderly** - This is more of a professional elder care facility that usually relies on the medical resources of the city and are more likely to be located within the city. As a result, most of these apartments are smaller, with fewer than 500 beds for housing and delivery of professional care services to very old, chronic-disease-suffering, semi-disabled or fully-disabled seniors. So far, most of these apartments available on the market are designed with high-end customers in mind. Meanwhile, compared with other products, this kind of project is more likely to be funded by Sino-foreign joint-venture institutions.

• **Elder care, health and vacation center** - In essence, vacation-type elder care housing is built to promote leisure and vacation service in the name of elder care. These can be single buildings as well as branded chains funded by a large real estate developer, and are usually located in cities with beautiful scenery and a pleasant climate. They often serve the most healthy and energetic seniors and are equipped with medical treatment, other healthcare services, physical rehabilitation services, and dietary education facilities and services. However, the actual elder care function in this type of senior housing is much weaker than its other supporting functions. They are often operated in the timeshare/hotel model and are often used by the developers to integrate and re-use their current real estate projects. Whether they can be classified as senior housing and thus benefit from the relevant preferential policies remains to be seen.

Although the infrastructure and basic product structure that consists of varied and multi-level senior housing products have been built in China, the construction of the core function in senior housing and services lags far behind, reflecting the lack of actual operating experience as well as the need to grow the market and the need for more comprehensive support from government policies.

3. **Current profit models demonstrate pros and cons**

Currently, China’s senior housing market is characterized with many market participants, gradually improving product structure and a diversified profit model. Four major profit models in China’s senior housing market are tabulated below.

### Table 7: Major profit models in China’s senior housing market

<table>
<thead>
<tr>
<th>Mode</th>
<th>Characteristics</th>
<th>Typical project</th>
</tr>
</thead>
<tbody>
<tr>
<td>Sale</td>
<td>Sale of residential housing products allows the rapid recoupment of funds and transfers ownership to the resident. This method of real estate development under the name of senior housing has the benefit of a shorter capital turnover period and lower risk, therefore it is a common profit model in the current market.</td>
<td>Poly Xitangyue, Greentown Wuzhen Yayuan, Vanke Suiyuanjiashu (“Dignified Life”)</td>
</tr>
<tr>
<td>Sale+ Buy-back</td>
<td>The ownership of the property is first sold and then bought back by the developer, with the buy-back funds used to cover the elder care and medical treatment costs. After the death of the senior, the remaining principal, if any, will be transferred to the successor and the ownership of the property will be transferred to the developer.</td>
<td>Beijing Oriental Sun City</td>
</tr>
<tr>
<td>Rent + Sale</td>
<td>This model is often seen in the newly constructed all-round residential community where elderly-adapted housing is sold on the market and the elder care service center built as a supporting commercial facility will be held and operated by the developer.</td>
<td>Beijing Vanke Xingfuhui</td>
</tr>
<tr>
<td>Rent to members</td>
<td>Members secure their beds by paying deposits or one-time membership fees. They may be given a certain discount when making annual payment on rent, daily necessities, or care.</td>
<td>Poly Hexihui, Qinheyuan Apartment of the Elderly, Senior Living L’Amore, Kaijian, Starcastle Zhonghuan Elder Care Community, Taikang Elder Care Community</td>
</tr>
</tbody>
</table>

Sources: Deloitte analysis
Different profit models have their own characteristics and pros and cons (Table 7).

- **Sale of senior housing** - This is a profit model employed by many real estate developers at present, which allows rapid recoupment of cash and shortens the investment cycle. However, it does not differ much from the sale of ordinary residential housing and is therefore not covered by the senior housing preferential policies. Developers may be regarded as intending “land enclosure” under this model. Meanwhile, as developers are not responsible for the subsequent management of the properties; they may not understand the real needs of their customers, which may impact the design, development, and sale of the project.

- **Sale + Buy-back** - Sales of properties enable developers to recoup cash quickly, which effectively eases the short-term cash flow restraint. However, the buy-back price caps the living and service cost and therefore restrains the variety and level of the service provided. As a result, this model has the same problem of constraining customers (who are mainly energetic seniors able to care for themselves) as well as invite possible disputes around property ownership.

- **Rent + Sale** - This is the model taken by many senior housing pilot projects which are developed by real estate developers. The needs of the elderly are given a thorough consideration in the design, planning and construction stages of the housing. Development cost is recouped by revenue from the sale. The supporting service center is owned by developers who hire professional elder care service institutions to manage and operate the service center. Such a profit model partially solves the cost problem but depends on the quality of the partners and their service. The efficiency of such a model remains to be seen.

- **Rent to members** - the lump-sum membership fee or deposit may cover part of the cost in facility renovation and fixed assets acquisition as well as the expenses in rent, consumption and maintenance. The projects that are currently operating using such a model indicate that the majority of customers are high-end customers who are wealthier but limited in total number. In addition, if the apartments are owned with full property rights by the residents, the costly membership fee may significantly affect the occupancy rate. It may be more acceptable on the market and therefore easier for continuous operation if preferential land policies are granted and the total costs are lowered.

In addition, insurance companies such as Taikang Life and Union Life subsidize the elder care communities they have invested in by selling pension products along with the properties. Such a model may lock in the customers shared under the same brand and may make it possible to have a rational plan on the community based on the future cash flow forecast. However, the actual elder care need of the customers may not materialize for another 10-15 years, which may cause some uncertainty.

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**Zhang Liang, Vice General Manager of Poly Real Estate Development Research Institute**

China’s senior housing market is in a preliminary development state at the stage where stakeholders are still exploring different profit models. In the future, each profit model is going to be improved as the market further develops and the industry becomes more regulated. Based on the characteristics of each individual project, we will see a situation where different models co-exist and new models will likely emerge.
4. Industry stakeholders bring different strengths to the cooperation

As industry stakeholders bring with them different characteristics and strengths to play different or overlapping roles in the market, we have observed that they have engaged in different forms of cooperation that are going deeper and wider. The elder care industry chain relates to three levels of participants, namely senior housing providers, consumers, and elder care funding providers. Important institutions include the government, real estate developers, elder care service institutions, insurance institutions, other investors and the elderly who need care. The government plays a role in regulation, guidance and initial funding support while each physical institution provides related elder care products for the elderly in need of care (Figure 4).

Specifically, the government performs the following three functions - formulating and implementing policies regarding elder care, building public welfare elder care infrastructure, and providing service, regulating and supporting commercial facilities and service providers. The problems, that the industry currently faces includes unclear industry definitions, a lack of unified standards, insufficient implementation of relevant policies on land, tax, and subsidies, required improvement from the government.
As mentioned above, although China’s senior housing industry has many participants which have been launching new products, the products available on the market and business models are all at the pilot and testing stage. Different participants have their own strengths and characteristics: Real estate developers are strong in facility development; elderly service institutions have experience in facility management and operation; Insurance institutions have access to long-term capital and bind selling financial wealth management products with elder care properties. Other players provide capital support and additional services. As a result, these physical institutions are related to each other by competition as well as cooperation. This is clearly shown in some of the senior housing projects which are a result of multi-party cooperation (Table 8). In these projects, real estate developers usually are facility builders or renovators. Domestic or foreign professional elder care institutions are responsible for the operation and management of the facilities while these projects are funded by investors, insurance companies, trust institutions, and industrial groups.

Overall, China’s senior housing development is at a preliminary stage and all the participating institutions are exploring the market. However, in terms of the market need, availability of products and services or degree of maturity of the business model, we have not seen a duplicable project model, neither have we seen a player that dominates the market.

Table 8: A partial list of elder care projects with multiple participants

<table>
<thead>
<tr>
<th>Project name</th>
<th>Facility building, renovation</th>
<th>Management and operation cooperation</th>
<th>Capital support</th>
</tr>
</thead>
<tbody>
<tr>
<td>Vanke Xingfuhui</td>
<td>Vanke</td>
<td>Shanghai Qinheyuan</td>
<td></td>
</tr>
<tr>
<td>Vanke Suiyuanjianshu (Dignified Life)</td>
<td>Vanke</td>
<td>Taiwan Cardinal Tien Hospital</td>
<td></td>
</tr>
<tr>
<td>Senior Living L’Amore Kaijian</td>
<td>Sino-Ocean</td>
<td>Emeritus</td>
<td>Columbia Pacific Capital Management, China Life</td>
</tr>
<tr>
<td>Starcastle Zhonghua Elder Care Community</td>
<td>Fosun</td>
<td>Fortress Investment Group</td>
<td>Fortress Investment Group</td>
</tr>
<tr>
<td>Dalian Weisifuji</td>
<td>Japan Weisifuji</td>
<td>Japan Weisifuji</td>
<td>Dalian Shipbuilding Industry Co. Ltd</td>
</tr>
<tr>
<td>Shanghai Lai Elder Care Center</td>
<td>Japan RIEI</td>
<td>Japan RIEI</td>
<td>Shanghai Sieton Group</td>
</tr>
<tr>
<td>Shangjinnanfu Hospital· Elder Care Center</td>
<td>Guiky</td>
<td></td>
<td>China Railway Trust Co. Ltd.</td>
</tr>
<tr>
<td>Jialize International Health Island</td>
<td>Leading foreign medical and elder care industry operator (to be determined)</td>
<td></td>
<td>China Railway Trust Co. Ltd.</td>
</tr>
</tbody>
</table>

Sources: open information, Deloitte analysis. The list of projects is not exhaustive and should be used as samples only.
Challenges that China’s Senior Housing Market is Facing

In terms of the overall elder care market and implementation of current projects, the senior housing market in China is facing many challenges. First, despite the gradual changes that are taking place in China’s elderly culture, the senior housing market will not reach maturity in the near future. Moreover, the traditional culture embodying values such as “family” and “piety” should be considered in the development and operation of the future senior housing. Second, the extreme insufficiency in both quality and quantity of elder care practitioners, scarcity of mature talents and the high turnover rate make it difficult to establish professional teams that can provide steady and high-quality service. In addition, the lack of nation-wide senior housing facilities and service and fee standards has blurred the boundary between senior housing and ordinary residential projects. The absence of supporting policies and detailed implementation rules has prevented the mode of development and operation of senior housing from getting mature rapidly. Finally, the huge amount of investment, long cycle of return and low capital liquidity have made it difficult to achieve economies of scale and maintain sustainable operations without long-term capital support.

1. The effective demand in China’s senior housing market needs to be developed

The Chinese society is getting old before getting rich. Developed countries have generally not become “ageing societies” until their average GDP reaches USD 10,000. By contrast, China became an ageing society in 2011 when its average GDP was only USD 5,416 per person. Today, the elderly in China rely on pension, family care, and income from work. The survey carried out in 2012 on elderly population reveals that social security covers 84.7% and 34.6% of the population in cities and rural areas with average income of 17,892 Yuan and 4,756 Yuan respectively. Getting old before getting rich has intensified the shortage in pension funds. According to the World Bank, the shortage in China’s pension coverage is going to reach 151 billion and will continue to grow, reaching 1.4 trillion in 2050.

In the meantime, the conflict between a modern family structure and the traditional elder care culture has become more apparent. Families in China have been playing a fundamental and leading role in elder care and the “family culture” and “piety culture” have been passed down to the present day. According to the Institute on Ageing of Renmin University of China, 40.7% of the elderly rely on their families for care compared to 24.1% who live on their retirement money or pension. Since the 1990s, Chinese families have become smaller and the family’s elder care function has weakened due to the erosion of the “four-two-one” family structure. A number of factors have combined to weaken the traditional family structure. First, implementation of the one-child policy over the last 35 years has reduced the number of young Chinese. Second, there is an increasing number of “empty-nest families” as a result of frequent labor migration across huge areas due to urbanization, industrialization and modernization. Third, a changing viewpoint in young people on elder care and an intensifying conflict between young Chinese and their parents regarding their obligations to care for their parents. Therefore, the elderly have unwillingly changed their care philosophy which in turn requires an increase in social elder care facilities and services.

However, due to the way of passing down family heritage in traditional Chinese society and the frugal life habit of most seniors, their actual willingness to purchase commercialized elder care facilities and services remains to be seen. Besides, 90.5% of the elderly in cities and 97.7% in rural areas own houses of their own or live in the homes of their children. Surveys indicate that only 3% of the elderly wish to move into professional elder care facilities. Most of these seniors are not able to take care of themselves and have to rely on long-term medical aid. Therefore, the providers of elder care facilities and services must better understand the needs of their potential customers to precisely position themselves in the market, effectively reduce investment risks, and achieve their expected strategic and business targets.
2. Elder care facilities and service supply do not match market needs

The mismatch between the facilities, service supply and market demand in the senior housing market is mainly reflected in the following aspects:

Firstly, most of the current elder care facilities are designed to serve middle to high net worth customers. A satisfactory elder care function costs the elderly themselves or their families a huge amount of money either in the form of sale or membership fees plus rent, which far exceeds their consumption willingness and the ability of the elderly. As a result, a majority of mid to high-end elder care facilities have a low occupancy rate of less than 50%.

Secondly, both the disabled or healthy seniors and their family members favor a convenient and easily accessible elder care facility that enables them to provide care to each other. Therefore, the facilities in the sphere of cities are in much higher demand than those in the suburbs or remote locations. However, most of the newly built facilities are located in suburbs or remote areas to save investment cost, creating a regional imbalance in supplies.

Moreover, most of the elder care facilities currently available on the market only provide basic living or care service with a limited number of other services. By contrast, the development of society and uplift of standard of living have significantly changed the mentality of elder care. We are seeing the trend of a diversified demand by the elderly in their elder care service, which requires that the market not only provides the service of basic necessities of life but also the capacity of offering opportunities for the elderly to enrich their educational, cultural, sports, and entertainment life as well as providing specific medical, health care, nursing and a complete senior-focused medial service network.

Mr. Fu, Executive General Manager of a large-scale real estate group

Senior housing customers may be classified into three types according to their health condition and the status of their spouses. The first type of customers refer to the healthy couples who focus on medical check-ups, sports, entertainment, tourism and other similar activities; The second type of customers include those who have lost his/her spouse but are healthy and mainly require spiritual consolation; the disabled elderly fall into the third type who require the care of professional centers. In the meantime, communities, families or professional elder care facilities and services must be built and operated by a unified and advanced standard.

In addition, the market lacks a high-quality and professional elder care service team. According to statistics from surveys, the elderly over 60 years of age in China spend on average one fourth of their time with insufficiently functioning body parts or organs and therefore are in need of care and nursing services. This infers that approximately 32.5 million seniors in China need a certain kind of long-term care while more service personnel capable of meeting other psychological or spiritual needs by the elderly are needed. As a matter of fact, the service personnel currently working in this industry are characterized by a general low quality and a high mobility, damaging the service quality and long-term operation of elder care facilities.

Consequently, before investors venture into China’s senior housing market, they should fully understand the needs of their customers and the important economic and cultural changes in Chinese society. By adjusting the structure of products available on the market, enriching services and focusing on the training of service personnel to ensure the quality of service they can better address these challenges. We anticipate that in the future, standardized facilities and services will be the cornerstone of the industry while customized products and services will determine who will win.
3. Unsatisfactory implementation of industry policy at the micro level

Compared to the countries with a wealth of elder care industry experience such as Japan, China is lagging far behind in legal development as well as participation of both the government and private capital in the industry. The government has introduced supporting policies in recent years. For instance, on September 17th, 2011, the State Council issued the “Twelfth Five-Year” Plan on the Development of Elder Care Industry in China to deal with the tendency of an ageing population. It lays out the main future tasks in an effort to tackle ageing including elderly social security, medical and health care, elderly services and elderly industry development. In 2012, the civil administration departments and land management departments of many local governments incorporated policies regarding “house-for-pension” schemes, land supply and preferential tax treatment in the plans on elderly-related work, or the land supply plans for 2013.

In 2013, government departments announced related policies with regards to lifting the restraints on granting access to foreign investors to China’s medical, healthcare, and elder care service industry. The Administrative Measures on Granting Permission for the Establishment of Elder Care Institutions and the Administrative Measures on Elder Care Institutions that entered into force on June 1st, 2013 give permission to foreign investors to establish elder care institutions in the Chinese market in the form of wholly-owned subsidiaries, joint ventures or cooperative operations. On September 6th, 2013, the State Council issued the Opinions of the State Council on Expediting the Development of Elder Care Service Industry (Guofa [2013] No.35, mentioned as “Document No.35” later in the report) that introduced a series of preferential policies regarding the investment by private investors in the for-profit and not-for-profit elder care institutions including land supply preferential policies, tax incentives, and supporting subsidies.

Generally speaking, however, the lack of laws and policies further supporting these plans has obscured the development of China’s elder care industry. For example, independent land supply will serve as an important foundation for the development of the elder care industry in the future. Fiscal and land supply policies may play a supporting role to attract more attention from foreign capital to this area and drive more projects in developing senior housing in real terms.

Unfortunately, the current policy support is limited to “not-for-profit” welfare institutions which rarely benefit the high-end elder care projects. As elder care service institutions survive on minimal profits or no profit at all and nearly all the apartments for the elderly are not making profit, it dims the hope of more capital flowing into the market. In addition, China’s elder care industry is suffering from insufficient regulation and supervision. Relevant government departments are not up to expectations in regulating and supervising market access, providing industry guidance or operational supervision, leaving the entire industry in the state of unguarded development as a result of a lack of unified industry standards or norms. Meanwhile, how to effectively interpret and utilize the complicated preferential tax policies (see attachment for detail), is a complex tax forcing participants to rely on professional institutions and services for advice.
Table 9: Laws and policies on elder care issued recently in China

<table>
<thead>
<tr>
<th>Time</th>
<th>Laws &amp; Policies</th>
<th>Main Content</th>
</tr>
</thead>
<tbody>
<tr>
<td>2011.12</td>
<td>“Plan on Constructing an Elder Care Service Social System (2011-2015)”</td>
<td>An elder care social service system will be mostly completed by 2015 that has a sound system, integrated organization, moderate size, good operation and service, effective regulation and supervision and sustainable development. The number of beds for every one-thousand seniors for elder care purposes will reach 30. The number of beds for day-care purposes and that in elder care institutions combined will be increased over 3.4 million during the period of the twelfth five-year plan, doubling the current total number of elder care beds; 30% of current beds will be renovated to meet the construction standards.</td>
</tr>
<tr>
<td>2012.12</td>
<td>The Law of the People’s Republic of China on Protecting the Lawful Rights and Interests of the Elderly (Revised)</td>
<td>It made revisions to the law in 1996 to make it more adapted to the current situation and clarified on the direction of future development.</td>
</tr>
<tr>
<td>2013</td>
<td>Detailed rules on elder care</td>
<td>Provinces and cities such as Hubei, Shandong, Zhejiang and Shenzhen introduced detailed rules on building elder care system and services.</td>
</tr>
<tr>
<td>2013.6</td>
<td>The Administrative Measures on Granting Permission for the Establishment of Elder Care Institutions and the Administrative Measures on Elder Care Institutions</td>
<td>Foreign investors are permitted to establish elder care institutions in the Chinese market in the form of wholly-owned subsidiaries, joint ventures or cooperative operations; In addition, foreign enterprises are allowed to establish medial institutions in the form of wholly-owned subsidiaries within Shanghai Pilot Free Trade Zone.</td>
</tr>
<tr>
<td>2013.9</td>
<td>The Opinions of the State Council on Expediting the Development of Elder Care Service Industry</td>
<td>A moderate sized elder care service system with complete functions covering both cities and rural areas will be built by 2020 on the basis of residential homes, dependent on communities and supported by institutions. It proposes to integrate small and medium enterprises into the elderly service industry cluster, develop elder care service websites and elder care service consumption market.</td>
</tr>
</tbody>
</table>

Sources: China National Committee on Ageing, Everbright Securities Research Institute, Deloitte analysis
4. Financing channels restrain the healthy development of senior housing market

Despite the entry of many investors into the senior housing market, until now only the pilot projects by a few companies such as Vanke, Poly Real Estate, Sino-Ocean, Greentown and Union Life have been implemented. Senior housing communities require large investments which they will not recover quickly. This weak capital liquidity makes it hard for the senior housing industry to achieve economies of scale or sustain a long-term operation without continuous capital support. Profit models have been the bottleneck that are difficult to break by developers or operators. Therefore, most of the senior housing projects are still at the stage of “selling houses to the elderly” and the investments in senior housing are often questioned as “enclosure movement”.

Limited financing channels have long restrained the overall real estate development in China. Due to the suspension of the IPO and re-financing markets in China, real estate companies have to fund most of their projects by their own capital, bank loans, or cash generated from sale to support project development and operation. For example, in January through April of 2014, over 95% of the capital used in real estate development came from the above three sources. In other countries, however, on top of government investment and policy support in the senior housing market, innovation in other financial instruments have played a vital role – for instance reverse mortgages and REITs. But these two financing channels have provided little assistance for China’s senior housing market.

In a reverse mortgage, the owner of a house mortgages his/her house to a financial institution in return for cash payments on a regular basis. When the owner of the house sells the house or dies, the loan will be repaid with the money received from selling the house. Such a model enables the borrower to finance the house while living in the house. The concept of “house-for-pension scheme” was first brought up in China in 2003 and was later tested in cities like Nanjing, Beijing and Shanghai. However these pilot projects were of a small scale and have produced unsatisfactory results. Factors such as the 70-year land-use right, the difference in expected value of houses, and the traditional notion of raising sons to support parents in old age have hindered the development of reverse mortgages. On June 23, 2014, the China Insurance Regulatory Commission issued guiding opinions stating that in the two years starting from July 1st, reverse mortgage pension insurance tests will be officially launched in Beijing, Shanghai, Guangzhou and Wuhan, which has innovated pension insurance by combining “house mortgage” and “lifetime pension insurance” and may drive the implementation of “house-for-pension” scheme to some degree in China. However, the lack of international experience on emerging products like this has resulted in a strict requirement on the qualification and minimum capital of insurance companies, which cause many insurance companies to be cautious before making moves.
REITs, namely Real Estate Investment Trusts, provide an innovative financing mechanism for real estate enterprises. They first appeared in the United States in the 1960s and are a widely held company, trust, contract or trust agreement. It seeks to gain from long-term real estate (housing) investment and returns a majority of yields to the beneficiaries without paying any tax. Although the Central Bank, China Securities Regulatory Commission and China Banking Regulatory Commission launched REIT pilot programs as early as 2004, they have not been extended to the domestic market due to the global financial crisis in 2008 and the absence of supporting domestic measures including tax, registration system, public trading and exit mechanism and etc.

As a result, some real estate companies choose to seek financing in the overseas market. New Century Hotel and Resort Group packaged five self-held properties and releases it in the Hong Kong Securities market in the form of REITs; the Beijing Oriental Plaza owned by Li Ka-Shing started to issue REITs for financing (for details please see Appendix II). In 2013, UBS SDIC partnered with UBS Global Asset group to establish an investment fund that only makes investments in public rental housing and holds the ownership—a quasi REITs real estate fund. It liquidizes fixed assets by innovative products and creates cash flow, signaling a possible new mode in the development of REITs in China.

However, the financing function of innovative financial instruments must be established on the foundation of a developed industry, i.e. a steady and attractive return to the investors through sound project operation. Therefore, participants in the senior housing market should, at the same time of exploring new financing channels, focus on building high-quality long-term projects that produce steady return to ensure the healthy development of the industry.

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1 OCED; Deloitte, China Real Estate Investment Handbook 2014;
China’s elder care industry, including both senior housing and service, is at a preliminary stage. We have selected some elder care models from the developed countries in Europe and America such as the UK and US as well as those that have a similar culture as China including Japan, Hong Kong and Singapore to learn from their experiences.

### Table 10: Comparison of elder care models in major foreign countries and territories

<table>
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<tr>
<th>Country</th>
<th>Model</th>
<th>Characteristics</th>
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| UK      | Government-driven | • The UK’s elder care model has transitioned from a traditional welfare institution to community care; community service centers are established and maintained through investment from local governments to provide services for elders in the communities.  
• About three fourths of seniors above 65 years of age in the UK live in self-owned homes. The government provides elder care services to these seniors and assists in renovating and repairing these self-owned homes through low interest rate loans and subsidies.  
• The government owns, maintains and operates shelter homes, elder care communities and nursing centers that are provided to low-income seniors in the form of public welfare rental homes. They account for over half of the elderly homes. Meanwhile, care and nursing services of different levels are provided to the elderly based on their self-care condition.  
• The market-oriented senior housing market demands a high professional standard and is therefore very centralized with the biggest developer taking 60% of market share. It provides services ranging from public facilities, social activities, housekeeping, catering to nursing and care.  
• “Equity release plan”/reverse mortgage are in place to help the elderly. |
| US      | Market-driven development and operation | • The elder care service in the US is highly market-oriented and industrialized. The government does not operate elder care institutions but performs functions such as management, insurance, and certifying salvation qualification.  
• Most of the elderly choose home care while a lot of service institutions provide routine care, medical care, and service at different levels.  
• Senior housing developments in the US represent a mature industry that is segmented into communities for energetic seniors, independent living, aided living, professional care and continuous care.  
• The senior housing market is open to full competition. Individual projects are usually in moderate size and are run in the way that separates owners from the managers.  
• The development of financial instruments such as mortgage loan default insurance and REITS has driven private capital into senior housing and therefore expedited the industry’s development. |
<table>
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<tr>
<th>Country</th>
<th>Model</th>
<th>Characteristics</th>
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| Japan   | Multi-party cooperation | • The elder care industry in Japan has formed a complete industry chain whose development is critically driven by a complete elder care insurance system and the Care Insurance System introduced in 2000.  
• Home elder care is highly developed. People can choose between “two-generation residence” and a longevity-type of residence which are supported by community and home care services.  
• Senior housing in Japan can be developed by a wide variety of developers such as real estate developers, insurance companies, industrial companies, the government and other institutions. This cooperative model helps reduce operational risks and costs.  
• The majority of the senior housing is rental property. Institutional facilities are usually run on a lump sum move-in fee and monthly fees while residential housing only charges monthly fees, which are, to a large extent, determined by and paid out of local care insurance. |
| Hong Kong | Market-oriented operation | • Hong Kong leads the world in elder care service thanks mainly to the mature atmosphere created by private institutions, systematic government plan, steady investment and the respect over the elderly in the entire society.  
• The elder care policy of the Hong Kong government advocates a “focus on home care and supported by institutional care”, providing support to home elder care through community care service plans. Meanwhile, the percentage of beds in the home for the elderly exceeds that of the average level in the world.  
• Recognition of elder care service people through offering academic diplomas, courses and in society to ensure the training on the professional personnel and the steady service level.  
• In the elder care service system, the government plays a role in planning, guidance, evaluation and resource allocation while the supply and operation of facilities are completed by private institutions.  
• Different types of pensions and salvation welfare policies are in place to meet the different needs of seniors who are in different states of life and require different levels of care.  
• Relevant senior housing funds have emerged in Hong Kong in recent years, contributing positively to the financing and long-term operation of elder care projects. |
The above table clearly shows that the elder care models of these countries are a reflection of their specific social background and local characteristics. China may learn from these countries in the development of its elder care industry while taking consideration of the Chinese cultural background and specific needs to constantly improve its infrastructure and system, encourage all parties to participate in development, proactively drive system reforms including financial innovation, and to ensure the healthy development of the elder care industry in China.

1. **Respect different needs of elder care in different cultures**

Although it seems varied and complicated, the different elder care models in different countries are common in that they are created and improved along with the evolution of the history, culture and economy of the specific country. The family structure and degree of closeness among family members in the western countries determine that the elderly live in a relatively independent state both economically and spiritually. By contrast, Asian countries – which treasure Confucian values – value the philosophy of piety, provide for the elderly in the family, and are comfortable with several generations living together. Although an accelerated ageing society and change in the structure of modern families have shifted the paradigm in elder care, it cannot be overlooked in the development of the elder care industry in China that the elderly are in need of family as well as spiritual care. Consequently, the “9073” principle and percentage allocation among home care, community care and institutional care proposed by the government are a reflection of China’s specific situation and traditional culture, which offers as a principal direction in the construction and development of elder care facilities and service systems in China.

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Zhang Liang, Vice General Manager of Poly Real Estate Development Research Institute

We have a lot to learn from foreign countries about senior housing. However, the development of senior housing in any country, whether in Europe, US or Japan, is closely related to the level of economic development, living standards, culture, and the social security system. China’s senior housing market is unique. Therefore, it cannot fully copy the foreign experience but rather should be developed in consideration of China’s tradition and specifics.
2. The government has intensified investment to improve infrastructure and system
The elder care industry in all the countries was developed as a result of an ageing population. But the development was accelerated by the push of the government and insurance policies. For example, In the 1980s, the development of mortgage loan default insurance encouraged a large amount of private capital to flow into senior housing. In the UK, the shelter homes for rental supported by government funding have been an important part of senior housing; In Japan, the implementation of the Care Insurance System in 2000 has ensured that the elderly are capable of paying for the care and nursing services and have since attracted a large amount of private enterprises in this field. The governments of both Singapore and Hong Kong have constantly increased investment in law, tax, subsidy and other areas in an effort to construct and improve an elder care system that best suits them.

3. Participants of various natures in multiple modes
The participants in the development of senior housing in foreign countries vary dramatically and may include real estate developers, insurance companies, industrial companies, and governments. Different from the ordinary residential housing offered for sale, the senior housing also faces the issue of continuous management. Most of the senior housing projects in foreign countries are managed by professional management companies. Sale plus rent is the major profit mode in foreign senior housing although generally speaking, older customers tend to need more care services and therefore senior housing is often rented to them. In the US, the energetic elderly communities are often for sale with a part of it for rental, while the aided-living and professional care communities that require routine medical aid and care are often operated in the form of rental. In the UK, the majority of institution-managed senior housing that provides more service is run in the form of rental properties while the independent housing, especially the retirement housing that require less care services are mostly for sale. Japan manages most of its senior housing through renting regardless of the “institutional facilities” with care or “residential housing” without care. The difference is that the institutional facilities often collect a lump-sum move-in fee on top of the monthly charge while the residential housing only charges monthly fee.

4. The development of financial instruments has helped grow the industry
Senior housing is the most basic and most important element in the elder care industry. Experience from foreign countries shows that the development of some advanced financial instruments have helped grow the industry. The mortgage loan default insurance introduced by the U.S. Department of Housing and Urban Development in the 1980s further funneled private funds into this area and drove its development. The emergence of REITs and CMBS in the 1990 also widened the financing channels for the senior housing development. Meanwhile, the reverse house mortgage has been launched in the UK, US, and Japan to ensure that the elderly are capable of paying for the elderly facilities and services.

Today, facing the increasing elder care pressure, the Chinese government should make an effort to enhance elder care product offerings of different levels to meet different elder care needs while paying respect to the Chinese elder care tradition. In the meantime, it is imperative that the government intensify its investment in building and improving infrastructure and the overall system, (to include introducing preferential policies and subsidies to construct facilities), strengthen long-term care insurance, expand health insurance, and encouraging the development of innovative financial services.
As mentioned above, China’s great potential in its senior housing market has attracted the participation of many types of investors. However, the entire market is at a preliminary stage and is facing challenges such as insufficient effective demand, a mismatch between supply and demand, unclear micro policies, financing channel restraints, among others. Although the development in elder care models and industry in foreign countries has provided valuable experience for us, the differences in the level of economic development and in elder care traditions are forcing China to find a model that suits its own specific situation.

We expect that China’s senior housing market will demonstrate the following trends:

- **Increasing clarity on government policies and direction.** The development of China’s senior housing market cannot be successful without heavy investment and strong support from the government. From the government’s perspective, although specific policies have not been implemented, the elder care industry has been listed as a strategically important field that is critical to the development of the country. The government needs to set strict standards on the qualification of participants of senior housing and specific projects to separate out promising senior housing projects so that they can receive full policy support. Meanwhile, all the government departments, including the Ministry of Civil Affairs, Ministry of Finance, Land and Resources Bureau, and the Ministry of Health, should work together in making a concerted policy on elder care.

- **Home care is still the main elder care model and elder care service will be the main source of profit.** We anticipate that the “9073” type of elder care service system that is constructed on the foundation of home care, supported by community service and supplemented by institutional service will be the key direction in China’s elder care in the future. Regardless, the senior housing market should not be limited to the 3% institutional elder care facilities, nor should it be restrained to the renovation of the senior living environment. The service and operation of elder care facilities will be at the core of the long-term development of senior housing. It will also be the main contributor of profit when the market turns mature in the future.

- **Efforts will continue to be put in to explore profit models in the mid to long term and a competitive edge will be achieved through differentiation.** The ambiguity in industry entrance mechanism and in regulation and supervision added by the absence of supporting policies have made it impossible to solve the problem of high cost and long investment cycle in the construction and operation of senior housing. In the next five to ten years, China’s senior housing market will continue to test different business models and to seek competitive edge through differentiated operation.

Meanwhile, policies have been introduced to encourage private investment in this industry without completely losing the welfare nature of elder care to many residents. The government should develop strict operational guidelines that govern the access mechanism and criteria, followed by full support to the projects that meet these criteria without any reservation, especially in transfer of land, preferential financial and tax policies and related subsidies. Meanwhile, the government should drive the implementation of the long-term care insurance market and increase the depth and width of social security coverage, further safeguarding the ability to pay for the elderly service.
Deepened competition and cooperation among industry participants.

• The competition and cooperation among industry participants will be deepened. We expect that with regards to the construction of senior housing, the real estate developers and insurance institutions as major players will seek to compete by differentiation. Real estate companies often focus on the elderly-adaptive renovation of current communities and the construction of comprehensive new communities that are mostly for sale or sale plus rental. The insurance institutions will be more specialized in the continuous care communities, allocating long-term capital among different assets combined with elder care or health insurance products that are provided to their customers. They tend to operate the facilities in the form of rental to generate steady cash flow. On the other hand, effective elderly service institutions are the results of cooperation. Although some large-scale real estate developers and insurance institutions have built independent service teams and brands of their own, professional elder care service institutions are the main force in operating elder care facilities. The participation of other investors can effectively bridge the gap caused by insufficient capital and other resources in the senior housing market and, to a certain degree, drive the entire market to be developed toward maturity in the coming future.

• Foreign elder care institutions speed up China’s deployment. The vast elderly service market created by the increasingly rapid ageing of the society and the gradual lifting of the restrictions on the investment in medical and healthcare fields have attracted more foreign elder care institutions into China. They will focus on developing the high-end market with primary businesses in providing aid to life and long-term care service. Although wholly-owned foreign institutions are permitted to enter this market, they tend to actively seek domestic partners to jointly develop and operate elder care facilities in China.

• Financing channels are expected to be further broadened. The development of the industry itself coupled with the introduction of innovative financial instruments has diversified financing channels. While the domestic financial market is being improved at present, overseas capital markets such as Hong Kong and Singapore will become the main source for the senior housing investors to seek financing.

• Elder care fund planning helps expedite the development of elder care wealth management products. China’s elder care tradition will undergo rapid change as a result of increasing pressure from the modern family structure in the coming 10 to 15 years. Therefore, elder care fund planning will become increasingly important and standardized. This will significantly improve the ability to make use of care facilities in the society and of purchasing elder care service, thus benefiting the entire industry and expediting the development in elder care wealth management products.

• Related industries will benefit and be developed in concert. As the elder care industry concerns all the aspects of the basic necessities of the elderly life, it generates a huge potential for the related industries to grow in concert. It includes elderly culture, tourism, education, rehabilitation equipment and many other aspects of life. Of all these, the care and nursing service as the key element in senior housing development will dramatically drive the training of medical care personnel in relevant areas.

Nathaniel FAROUZ, Orpea China

As we mainly serve the disabled elderly as our customers and provide comprehensive and professional high-end care service, Orpea will work to carry out joint training programs with medical schools to solve the problem of a medical care personnel shortage.
Appendix I: Overview on China’s Tax Policies on Elder Care Industry

To tackle the issue of ageing population, satisfy the material, spiritual and cultural needs of the senior, and encourage the development of elder care industry, the government has introduced tax policies to provide support to elder care industry. Below is an overview of types of taxes and preferential tax policies concerning the real estate development, service and operation in the elder care industry.

Senior housing development – elder care industry preferential tax treatment not applicable
The Ministry of Civil Affairs has recently clarified that the senior housing development falls into the category of real estate development and is not administered as part of elder care industry. Currently, the senior housing development is not different in essence from ordinary residential development. Therefore, the relevant preferential tax treatments that are granted to elder care industry do not apply to senior housing development. Depending on the role of the participants and the phase of their participation, different taxes apply.

- **Business Tax**
  - At the construction stage, the contractor is subject to business tax at 3% that is in line with the construction industry.
  - At the selling stage, the developer is subject to business tax at 5% as it is in the sale of real estate property. In the event that the property is directly sold by the original developer, business tax is imposed on the gross selling price; In the event that the property sold is previously acquired from the original developer or other owners, business tax is imposed on the appreciation realized from sales. It is worth noticing that if the senior housing property is sold at an unreasonably low price, the tax authority has the right to make adjustments and deem a selling price.
- At the operational stage, the leased senior housing properties are subject to business tax at 5% on total lease income.
- The Chinese government has been driving the reform in transitioning business tax to value-added tax. It is expected that the business tax structures and applications will phase out in the next few years. After the reform, the above business taxes will be governed under value-added tax.

- **Urban Maintenance and Construction Tax, Educational Surcharge, and Local Educational Surcharge**: They are levied on the value-added tax, business tax and consumption tax actually paid by the taxpayers. The Urban Maintenance and Construction Tax is levied from 1% to 7% depending on the different locations of the taxpayers. The Educational Surcharge is levied at 3% across the nation and the Local Educational Surcharge is levied at 2%.

- **Deed Tax**: Deed tax is imposed on, and payable by transferees of the real estate or land use right upon the transfer of such real estate or land use right within the territory of China. Depending on the location, the deed tax is levied at the range of 3% to 5% of the transaction value. Where, provided relevant policies and regulations are followed, certain activities, such as the enterprise and corporate restructuring, transfer of company’s equity (share), merger of companies, division of companies, sale of enterprises, bankruptcy of enterprises and debt-for-equity swap and etc., may be eligible for tax preferential treatment including partial or full tax exemption.

- **Real Estate Tax**: For the properties self-used by the enterprise for elder care purposes, the real estate tax is levied at 1.2% of the adjusted cost of property value (including the value of the land) after a 10% to 30% deduction from the original value. For the elder care properties leased by the enterprise, the real estate tax is levied at 12% of lease income.
Land Value Appreciation Tax: Land value appreciation tax ("LVAT") is levied at any of the four progressive tax rates, i.e. 30%, 40%, 50% or 60%, on the gain from real estate transfer after prescribed deductions specified by laws.

Presale is common in the real estate development (including senior housing development) industry. In order to regulate the real estate and land market and adjust the income generated from appreciation of land properly, the tax authorities are requested to adopt a "provisional collection and final settlement" approach in collecting LVAT. Under this approach, LVAT is usually provisionally collected based on a certain percentage of sales proceeds, followed later final settlement upon competitions of the entire construction project.

The LVAT is an important tax in the development of real estate as well as a critical source of fiscal income for the local government. It is often used by the government as a means of regulating the real estate industry, including adjusting the pre-collection rate, final settlement and special-purpose tax audit etc. Consequently, the senior housing developers must be cautious on Land VAT planning and compliance management.

Urban and Township Land Use Tax: Taxpayers, including enterprises and individuals using land in cities, towns, designated towns, industrial and mining areas, are subject to a fixed amount of Urban and Township Land Use Tax payable on the basis of the area of land actually been used (different tax rates apply in different regions).

Farmland VAT: Taxpayers, including enterprises and individuals using farmland for building houses or other structures for non-agricultural purposes, are subject to the Farmland VAT payable on the basis of the area of farmland actually used and the rate varies from the amount of 5 - 50 Yuan per Mu (different tax rates apply in different regions).

Stamp Duty: Taxpayers, including enterprises and Individuals who concluded or received the following dutiable documents specified by law (such as sales contract, loan contract, real estate leasing contract, transfer of title of properties, rights-License, etc.) are subject to the Stamp Duty. In most cases, all parties of the contract have the obligation to pay Stamp Duty.

Different tax rates apply to different vouchers. For the real estate transfer contract, the transferor and transferee are both subject to a 0.05% Stamp Duty of the total contract value. For the real estate leasing contract, the lessee is subject to a 0.1% Stamp Duty of the total contract value. The Stamp Duty of 5 Yuan is applied to both Real Estate Title Certificate and Land Use Certificate.

Enterprise Income Tax: All enterprises and other income receiving organizations within the Chinese territory are subject to the Enterprise Income Tax on the operation and other kind income. Since January 1st, 2008, a unified 25% rate applies to both Chinese and foreign enterprises.

In addition to the fact that the preferential policies on elder care industry are different from those on the senior housing development, the government strictly controls how the construction land of elder care institutions should be used. The change of the purpose or plot ratio of a land initially approved for elder care facility construction for real estate development is absolutely prohibited. As the senior housing is not different in essence from the ordinary residential housing, it is predicted that the preferential policies supporting the elder care industry will not be expanded to the senior housing development within a certain period.
Elder care service operation – the preferential tax policies are leaning toward not-for-profit elder care institutions

With the possible exception of LVAT, most of the other taxes applicable in the senior housing development are also applicable to the elder care service institutions for the provision of elder care services.

China is the only country in the world with over 100 million senior people and its ageing population is increasing at a much higher rate than that of the other countries. The Chinese government encourages the participation in the elder care service industry by governments, families and the society by introducing a series of preferential tax policies, which leans more toward not-for-profit elder care institutions. The main policies are:

- **Business Tax**: Elder care institutions are exempted from paying business tax on the nursing and care services they provide.

- **Real Estate Tax, Urban and Township Land Use Tax**: The real estate properties used by the elder care service institutions of a welfare and not-for-profit nature are exempt from the Real Estate Tax and the Urban and Township Land Use Tax.

- **Farmland Tax**: The farmland used by elder care institutions is exempt from the Farmland Tax.

- **Enterprise Income Tax**: The welfare and not-for-profit elder care institutions established by government departments, enterprises and institutional organizations, social organizations and individuals are exempt from the enterprise income tax on temporary basis. The donations made to welfare and not-for-profit elder care service institutions by enterprises and institutional organizations, social organizations and individuals are allowed to be fully deducted when paying enterprise income tax or individual income tax.

In addition to the above preferential tax policies, the government also offers preferential policies on local taxes and fees or subsidies. For example, administrative fees are exempted on the construction of not-for-profit elder care institutions; Administrative fees are reduced by half on the construction of for-profit elder care institutions; Administrative fees are reasonably reduced on elder care institutions that provide elder care services; The electricity, water and gas used by elder care institutions will be priced the same as that for residential living purposes.

The Opinions of the State Council on Expediting the Development of Elder care Service Industry (Guofa [2013] No.35) issued by the Chinese government in 2013 clearly specifies that the above preferential policies apply to the elder care institutions established by the Chinese or foreign funding, which will encourage overseas capital, especially the overseas elder care service providers to enter the Chinese elder care industry. Furthermore, the Chinese government is still in the process of initiating and improving preferential tax policies that relate to the investment in the elder care service industry by private capital. Whether more tax benefits will be provided to for-profit elder care institutions as are the not-for-profit institutions remains to be seen.
The term Real Estate Investment Trust ("REIT") may be the most frequently discussed yet the most misunderstood term for real estate financing in China. REITs have actually been a very popular investment vehicle in the United States and are an important element of the American Model (i.e. different sectors of the real estate industry, such as development, operations, sales, financing and investment, are able to reflect specialisation). Real estate assets in China have been packaged as REITs and publicly traded on stock exchanges in regional financial centers such as Singapore and Hong Kong in recent years. In 2011, the first CNH-REIT was listed on the Hong Kong stock exchange ("HKEx").

1. REIT – characteristics and basic structure

The definition of REIT REIT is a specific term used in global capital markets to describe a specific investment vehicle. "A REIT is a widely held company, trust or contractual or fiduciary arrangement that derives its income primarily from long-term investment in immovable property (real estate), distributes most of that income annually and does not pay income tax on income related to immovable property that is so distributed." With the "widely held" characteristic included in the definition, most global REIT regimes are publicly listed and traded on stock exchanges. So far, there have been no REITs that satisfy this definition and that are listed on the stock exchanges in Mainland China. There are, however, REITs containing China’s real estate assets listed in regional financial centers such as Hong Kong and Singapore.

REIT characteristics REITs can invest in one or more properties. Generally the investments will be comprised of established properties which generate a stable rental income stream and potentially long term capital gains for the investors. These might include all asset classes, such as residential apartments, hotels, shopping centers, factories, warehouses, office buildings and hospitals.

Compared with other securities traded in stock exchanges, REITs have some of the characteristics of both debt and equity – for example, the regular income stream makes it debt-like, while the fact that investors are generally exposed to all the risks and rewards of the underlying properties makes it equity-like.

Compared with direct investment in property, REITs provide better liquidity to the investors. Most countries would provide tax neutrality or incentives when designing their REIT regimes, so that the traded REITs would be more tax efficient when compared with the direct investment in property.

The diagram below illustrates the basic structure of REITs:

**Figure 5: REIT basic structure**

Sources: Deloitte Analytics
2. Benefits of developing REITs

The development of REITs will benefit the real estate industry and its investors in the following aspects:

**Improving the real estate business model** One of the key attractions of a REIT regime for the Chinese real estate market is that it will open up an additional source of financing for real estate developers and other property companies, who are currently relying mainly on bank loans for financing. With a REIT regime established, developers will have another ready market for completed properties, making it easier for them to free up capital for new projects. REITs primarily seek good quality assets with a stable income stream and low risk. They therefore provide an exit route for other property investors who have a different risk appetite, for example opportunity funds whose objective is to realise gains through upgrading or reallocating assets; once their work is complete, the asset becomes suitable for a REIT. Other holders of substantial, non-core real estate assets may also benefit from a REIT market in that REITs will increase the pool of potential purchasers for such assets. Meanwhile, the development of REITs should increase the level of capital invested in the sector, thereby increasing liquidity. Overall, it can entirely change the highly leveraged real estate business model.

**Broadening access to real estate investment** In their publicly listed form, REITs allow private individuals and other small scale investors to get exposure to specific real estate assets that would otherwise only be accessible to institutional and wealthy individual investors because of the high cost of the assets, for example shopping centers and office buildings. In the absence of REITs, small investors can only purchase shares in listed property companies, which are not a good proxy for investment in real estate assets, as such companies have a much more complex risk profile than assets typically do on a standalone basis. In addition to enabling retail investors to make a small investment in real estate, REITs are also attractive to investors since shares or units in REITs can be freely traded on the stock exchange, creating an easy exit from their investment with no impact on the underlying property, i.e. the property title remains with the REITs.

**Diversification** REITs divide the ownership of the assets into shares or units. Investors with the same budget can invest into different asset classes through REITs, instead of buying into a particular asset. Fundamentally, REITs provide a different form of real estate investment for investors. For institutions such as insurance companies and pension funds, which require steady returns to match their long-term liabilities, the stable income stream of a REIT provides an alternative holding to bonds.

**Regulated status** As REITs are usually established as a retail investment product, they are typically subject to a range of regulatory requirements, which are designed to prevent them from taking on too much risk. These commonly include investment restrictions limiting the nature of investments that may be held and restrictions on borrowing and valuation requirements. These requirements are in addition to the normal rules applicable to publicly traded securities, such as public disclosure, financial reporting and internal control procedures. All of these measures mean that REITs provide investors with a highly transparent and regulated means for investing in real estate, which gives investors confidence when they are making investment decisions.

**Tax transparency** As noted above, most countries treat a REIT as a tax transparent vehicle, so the income earned by a REIT is not taxed at the REIT level. Instead, a REIT is required to distribute nearly all of its net income to the investors and the income is then subject to tax in their hands. This avoids double taxation of the income, making the tax treatment for investors comparable to the treatment that would apply if they invested directly in real estate rather than through a REIT. In practice, as an incentive to encourage REIT development, the tax imposed on investors by some REIT jurisdictions may even be lower through granting of preferential treatments.
3. Offshore RMB REITs: The supply and demand for funds

Supply of Offshore RMB funds: By using a series of supportive measures to expand RMB trade settlement and allow offshore RMB financial products, China has gradually expanded international use of the RMB. Mr. Li Keqiang, the Chinese Premier, announced a series of supporting policies, including "support Hong Kong to develop into an offshore RMB centre", at a forum focusing on the 12th Five-Year-Plan along with economic, trade and financial cooperation between the Chinese Mainland and Hong Kong on 17 August 2011.

With the RMB going through the process of internationalisation, Hong Kong, which is the settlement centre for offshore RMB, holds RMB from import and export settlements. The CNH deposits in Hong Kong had reportedly reached RMB 1 trillion, the RMB bonds issued overseas has reached RMB 450 billion and the offshore RMB spot and forward trade volume combined has reached USD 8 billion averagely per day. Assume that Hong Kong holds over 50% of offshore RMB, the RMB deposit will reach RMB 6 trillion by 2028. Given the popularity of Chinese properties among investors and the increasing influence of the RMB, investors will probably regard offshore RMB REITs as an investment with unique attraction, leading to a strong demand for such offshore RMB investment instruments in addition to deposit and bonds.

Qualifications of offshore RMB REIT sponsors: Offshore RMB REITs are traded on the HKEx under the Securities and Futures Commission ("SFC")'s supervision. No REIT can be listed on the stock exchange without approval from the SFC. Offshore RMB REITs are governed primarily by both the Code on Real Estate Investment Trusts ("the REIT Code") promulgated by the SFC and listing rules issued by the SEHK.

In addition, Mainland China has issued regulations on the approval and supervision of direct foreign investment in the real estate sector. More specifically, Shang Zi Han (2007) No. 50 specifies that tight control shall be imposed on the merger and acquisition of our investment in local real estate companies in the form of "round-trip" investment structures (including the same effective owner); foreign investors are not permitted to change the effective owner of local real estate companies so as to avoid approval procedures for foreign investment in the real estate sector. Strictly speaking, such regulations restrict the participation of local property developers initiating offshore RMB REIT. Currently the only eligible sponsors for offshore RMB REIT are foreign investment enterprises.

4. Offshore RMB REITs – risks and pricing

Valuation and pricing: In the only offshore RMB REIT case, the majority of the trust-unit interest is still held by the sponsor, with only a minority number of units available for subscription by investors in the open market. As for valuation, an independent asset valuation report is issued by professional valuation firm for reference. In mature REIT markets, pricing in secondary markets is mainly based on investors’ expectations on both the regular rental cash flow and the long-term asset value appreciation, with consideration of macroeconomic factors in general and property management in particular. As for offshore RMB REITs, the investors should also consider policy risk factors directly related to CNH.
Market risks: REITs are usually established as a regulated investment product for retail investors, and hence they are subject to investment restrictions to keep their risk level within acceptable parameters. Consequently, REITs generally do not take development risks but rather invest in mature properties which generate stable rental income. When REITs are initially established, it is necessary to disclose rental market prospects, major lease terms and conditions, related party transactions, the plan for property management, and other major market risk factors.

Policy risks of offshore RMB: RMB is still not a fully convertible currency. There is no assurance that the Chinese government will not issue new laws and regulations in the future that could have an impact on RMB conversion and remittance. There are restrictions imposed by the Chinese government on the cross-border flow of RMB funds which is presently restricted to trade accounts. As a result, RMB availability in the offshore market is still limited. Hence, the ability to raise RMB funds in the future may also be limited. Whether institutional investors have "natural" RMB supply or not will directly influence their enthusiasm for investing in offshore RMB REITs. Individual investors are confined to Hong Kong residents, and there is a quota system on the amount of RMB a Hong Kong resident can convert and remit daily.

"Cash trap": "Cash trap" means the risk of lower distributable profit due to the use of different accounting standards. Offshore RMB REITs allow investors to receive distributions in RMB. Profits available for distribution from the underlying property holding vehicle in China to the offshore RMB REITs will be determined in accordance with Chinese Accounting Standards. Such profits will differ from those determined using Hong Kong Financial Reporting Standards or International Financial Reporting Standards (e.g. in respect of depreciation, amortisation, deferred tax and contributions to statutory reserves) which could give rise to potential cash trap issues.

Risk management: As a type of Hong Kong REIT, offshore RMB REITs are governed by the REIT Code and regulated by the SFC. To reduce investors’ risks, risk management measures include:

- Specific ownership and rights to the assets;
- Restrictions on borrowing by the REIT;
- Distribution of at least 90% from the REIT’s audited net income after tax for each financial year, subject to certain adjustments;
- A corporate governance framework overseen by an independent trustee; and
- A qualified manager licensed and regulated by the SFC.

5. Offshore RMB REITs: tax issues

Offshore RMB REITs would generally involve tax implications in Chinese Mainland, Hong Kong and Singapore.

5.1 Taxes in the Chinese Mainland

In respect of taxes in the Chinese Mainland, offshore RMB REIT sponsors and investors should be aware of the following issues:

- The Chinese Mainland has a relatively complex tax regime for the real estate sector, with high effective tax rates. Different real estate projects or the same project in different periods may be subject to different taxes and tax rates, which will directly influence the estimate of future dividends for offshore RMB REITs;
The pre-listing restructuring caused by the consolidation of real estate projects in the Chinese Mainland for the purpose of establishing offshore RMB REITs will be subject to Enterprise Income Tax, turnover taxes (such as the Business Tax) and other taxes (such as Land Value Appreciation Tax). Particular attention should be paid to the M&A Tax Rules (i.e. the Income Tax Treatment of Enterprise Restructuring (“Circular 59”), as well as the Announcement on Business Tax Issues Concerning Taxpayers’ Asset Restructuring promulgated by the State Administration of Taxation on 29 September 2011;

- A series of regulations on the conditions for entitlement to tax treaty benefits, including regarding the definition for “beneficial owners”, which have been promulgated since the Enterprise Income Tax reform that began in the Mainland China in 2008, will have influence on the design of overseas holding structures for real estate projects in the Chinese Mainland. This will directly influence the future income of offshore RMB REIT investors.

5.2 Taxes in Hong Kong
According to the collective unit trust investment schemes acknowledged by the Securities and Futures Ordinance - Section 104, offshore RMB REITs can be exempt from Hong Kong Profits Tax, reflecting an internationally accepted principle for considering REITs as tax transparent entities. The trading of offshore RMB REITs is subject to stamp duty in Hong Kong.

5.3 Taxes in Singapore
The Singapore government attaches great importance to the development of REIT. They endeavor to make Singapore the most important market for REIT in the region. Therefore, the Inland Revenue Authority of Singapore (IRAS) provides a series of tax incentives, which mainly include:

- A REIT may enjoy tax transparency treatment whereby the trustee of the REIT may not be charged any tax but the beneficiary be subject to tax on the distributions received from the trustee.
- Tax exemption is granted to the individual who received distributions from REIT.
- Distributions received from REIT by a non-resident entity, which is not an individual, can enjoy a reduced withholding tax rate at 10%.
Contacts

For more information, please contact:

Yvonne Wu
Managing Partner
Deloitte China Life Sciences and Health Care
Tel: +86 21 61411570
Email: yvwu@deloitte.com.cn

Richard Ho
Managing Partner
Deloitte China Real Estate
Tel: +852 28521071
Email: richo@deloitte.com.hk

Maria Liang
Tax Managing Partner
Deloitte China Life Sciences and Health Care
Tel: +86 21 61411059
Email: mliang@deloitte.com.cn

Barry Man
Insurance Managing Partner
Deloitte China Global Financial Service
Tel: +86 10 85207386
Email: bman@deloitte.com.cn

Acknowledgements
We wish to thank the following Deloitte people for their contributions to this report.

Lydia Chen
Director
Deloitte China Research and Insight Centre

Vivienne Huang
Manager
Deloitte China Research and Insight Centre
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SH-020ENG-14

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