Urbanisation and Housing in China

April 2012

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Executive Summary

In 2011, for the first time ever, more than half of China’s citizens were living in cities. Against the background of rapid urbanisation, it has become increasingly difficult to provide affordable housing for lower-income families. A hike in property prices has also exacerbated the problem by making housing unattainable for even middle-income groups.

Urbanisation in China is largely driven by rural-to-urban migration. The strategic approach to urbanisation in the 12th Five Year Programme (2011-15) is to channel rural migrants away from megacities and big cities and into small and medium-sized cities. Yet in marked contrast to this approach by the Chinese government, it is the megacities and big cities that rural migrants are primarily attracted to. The influx of migrants into urban metropolises remains an ongoing and increasing trend despite the various measures and policies instigated by the Chinese government to try and control it.

There are two main scenarios for promoting urbanisation reform: the first scenario would target the administrative hierarchy for cities, redirecting more resources to small and medium-sized cities to enable them to provide more and better services (including housing) and to attract more investment and migrant workers. This approach could turn out to be very costly and time-consuming. The second scenario would open up the megacities and big cities to the migrants who already reside there. This would require the provision of affordable housing and essential public services. Both scenarios imply a redistribution of resources from urban hukou (housing registration) holders in first-tier cities, either to smaller cities or to migrants within the megacities who would thus become classified as urban citizens. The need for a more inclusive approach toward migrants in the city becomes even more urgent in view of recent development strategies that place a priority on expanding the domestic market and strengthening domestic consumption as part of a structural reorientation of the Chinese economy.

Due to internal migration, there has been a marked increase in the demand for low-rent urban housing. This demand has been reinforced by the following factors: 1) a growing tendency for entire families to migrate; 2) greater expectations by second-generation migrants to stay in the cities; 3) a growing number of young graduates from colleges and universities who wish to stay in big cities even with meagre incomes; and 4) a growing number of former peasants who have lost their land. Despite being seen as an important attempt toward solving the problems for low and middle-income families in urban areas, the government’s affordable housing programme (outlined in the 12th Five Year Programme) has raised concerns regarding its potential negative impact on affordability in general. Informal housing units will be replaced by fewer affordable-housing units that might still be out of reach for most migrants in urban areas either because they are ineligible for the programme or because they lack sufficient financial means to pay the higher rent (compared with the costs of informal housing). Other concerns include the fiscal risk for local governments, eligibility criteria and fair distribution for different types of affordable housing, and the quality of construction.

Since 2010 the Chinese government has introduced various policies to curb speculation and excessive gains from property transactions, which have led to lower prices for most players. Controls on the housing market conflict with the interests of most players at the local level such as early buyers, potential home buyers, developers and local governments, but they nevertheless help to promote widespread construction of affordable housing. They thus have the potential to meet the essential needs of lower and middle-income citizens and migrants if – and only if - the many challenges associated with implementing the programme are mastered.
To ensure the effectiveness and fairness of the affordable housing programme, it is crucial to have clearly defined targets and eligibility criteria. For this purpose, a comprehensive social assessment of the government’s affordable housing programme is needed that focuses on different groups of migrants and their respective housing needs. It should also cover questions of household registration as well as access to public services and social security.

With increasing numbers of people moving from rural to urban areas in search of a better life, China and Europe face the common challenge of ensuring sustainable urbanisation. National and local governments have to provide better public services, including affordable housing, to a growing number of city residents. An exchange on the challenges, experiences and prospects of affordable housing programmes and on redevelopment in the context of urbanisation and migration could help facilitate and deepen the dialogue between China and the EU on sustainable urbanisation and its economic, social and environmental implications.
Main points

- While the Chinese government is seeking to channel rural migrants into small and medium-sized cities, rural migrants themselves are primarily attracted to megacities and big cities.

- Due to internal migration there has been a marked increase in the demand for low-rent urban housing.

- The Chinese government has launched an ambitious affordable housing programme to build 36 million units of affordable housing over the five-year period, 2011-15.

- It is feared that the programme may have a negative impact on affordability because some informal housing units will be replaced by fewer affordable housing units that might still be out of reach for most migrants.

- Government housing interventions will probably have a limited effect on the rate of urbanisation in China because only a very small part of the affordable housing programme targets low-income families.

- The two scenarios for promoting urbanisation focus on either big/megacities, or on small/medium-sized cities. Both scenarios imply a redistribution of resources away from urban hukou holders in first-tier cities, with the latter scenario probably more costly and more difficult to put into practice.

- Central government control conflicts with the interests of most players at the local level such as early buyers, potential home buyers, developers and local governments, but is promoting widespread construction of affordable housing.

Recommendations:

- An exchange on the challenges, experiences and prospects of affordable housing programmes and on redevelopment in the context of urbanisation and migration could help facilitate and deepen the ongoing dialogue between China and the EU on sustainable urbanisation and its economic, social and environmental implications.

- To ensure the effectiveness and fairness of the affordable housing programme, it is crucial to have clearly defined targets and eligibility criteria. A comprehensive social assessment of the government’s affordable housing programme is recommended as a precondition for greater dialogue.
**Introduction**

In 2011, for the first time ever, more than half of China’s citizens were living in cities.\(^1\) According to projections from the Centre of Development Research under the State Council, in 2020 the urbanisation rate will be as high as 60 percent. A further 325 million more people are expected to move to urban areas within one generation. Against the background of rapid urbanisation it has become increasingly difficult to provide affordable housing\(^2\) to lower-income families, particularly since a hike in property prices from 2003 to 2008 exacerbated the situation by making housing unattainable even for middle-income families.

In light of the commitment by the 12th Five Year Programme (12FYP, 2011-15) to increase the rate of urbanisation in China, this paper will examine the effects of China’s rapid urbanisation on the domestic demand for housing, with particular reference to affordable government housing. It will examine how government housing interventions will impact the rate of urbanisation in China, and consider alternatives ways of achieving this. It will also consider how central government control of the housing market conflicts with local demand.

1. **China’s rapid urbanisation and the strategic approach of the 12FYP**

Urbanisation in China is largely driven by migration processes. This consists primarily of internal rural-to-urban migration. According to the 2010 population census, the total population of 1.34 billion people consisted of 665.57 million urban and 674.15 million rural residents, or 49.68% and 50.32%, respectively. The total number of migrants, who were defined in 2010 as persons staying for more than six months in locations other than the towns (townships or streets) listed on their household registrations (*hukou*), was 261.39 million. Of this number, 39.96 million had a current residence different from the location on their household registrations but in the same city. This leaves 221.43 million people who can be classified as belonging to the migrant population.\(^3\) This figure is 83 percent higher than that in the 2000 population census, which recorded 117 million persons at different locations from their household registrations.

The strategic approach to urbanisation in the 12FYP aims to channel rural migrants away from megacities and big cities toward small and medium-sized cities. While it argues the case for steadily allowing rural migrant workers to become urban residents, it repeats the mantra of urban development espoused in China since the 1990s: ‘Megacities need to keep their population within reasonable bounds; large and medium-sized cities need to strengthen and improve population management and continue to make full use of their important role in absorbing the migrant population; and small and medium-sized cities and small towns should relax conditions for outsiders to become residents based on their particular condition.’

In marked contrast to the Chinese government’s approach to urbanisation, rural migrants are primarily attracted to the megacities (特大城市) and big cities (大城市). Despite the government measures and policies to control migrant flows, the influx of migrants into the urban metropolises represents an ongoing and increasing trend. In 2009, 63.3% of the migrant workers in China were employed in big and medium-sized cities of prefecture level (地级市) or greater, with 9.1 percent in

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\(^2\) Affordable housing can be defined as a purchase price that is less than three times the annual household income or a rent that is less than 30 percent of monthly household income. Price-to-income ratio is the basic affordability measure for housing in urban areas.

\(^3\) Nearly 80% of the migrant population have a rural background (Liudong 2010:38)
municipalities (直辖市), 19.8 percent in capital cities (province level 省会城市), and 34.4 percent in prefecture-level cities. These data show that China’s urbanisation process is dominated by megacities and big cities, with the fastest population growth being seen in cities with more than 2 million inhabitants. When considering the impact of urbanisation on Chinese domestic demand for housing, it is necessary to differentiate between the real urbanisation process of migrants voting ‘by their feet’ (based on spontaneous and largely market-driven factors) and the government’s strategic approach of channelling migrants into smaller cities (which emerged and were shaped in reaction to this spontaneous development).

2. Impact of China’s rapid urbanisation on domestic demand for housing

Due to the continuous rise in rural-to-urban migration, there has been a marked increase in demand for low-rent urban housing. Demand by migrants in the city for different types of housing is determined to a large degree by the types of jobs they obtain. Migrants and their housing can be roughly divided into the following categories:

- construction workers, who make up a large proportion of male migrant workers and who generally sleep in barracks at the construction sites;
- factory workers, both male and female, who are usually housed in company-owned dormitories;
- and household workers who are accommodated in private households.

For many other types of migrant labourer, their place of work is also where they live (see Figure 1). Only a certain number of rural-urban migrants, therefore, rent their flats on their own. Migrants with privately rented housing frequently live in urban villages—often they are employed or self-employed in small shops, small-scale production enterprises, the restaurant and service sectors, or they are employed in cleaning, peddling or similar occupations. In other words, they usually hold informal jobs. As evident in figures from the Ministry of Public Security, demand by migrants for private housing has shown a continuous increase in recent years.5

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5 In contrast to the criteria used by the State Statistical Bureau which defines migrants as persons staying for more than six months in locations other than the towns (townships or streets) of their household registrations, the Ministry of Public Security counts the number of temporary resident permit holders registered at local police stations. People have to register when staying more than three days at a location different from their place of permanent registration. Due to these different criteria, figures from the Ministry of Public Security generally show a smaller number of migrants than those from the State Statistical Bureau.
Figure 1: Types of housing for migrants with residence permits in Chinese cities in 1998, 2003, and 2008 (migrant numbers in millions)

Note: These figures refer to the entire municipal administrative area, not just to the city districts.

Between 1998 and 2008 the number of migrants who lived in independently rented housing rose from 11.35 million to 57.2 million. In percentage terms, this represents a rise from 28% to 49%. These figures clearly show the rapid increase in low-priced accommodation for migrant workers in the cities. Based on urbanisation tendencies and the distribution of migrants in cities of different size, the demand for affordable housing will be particularly strong in megacities and big cities.

Growing demand for inexpensive housing is expected to be amplified by at least four developmental tendencies:

1) the increasing and normal tendency for entire families to migrate as migration periods lengthen; 6
2) higher expectations by second-generation migrants (born in the 1980s) to stay in the cities and become permanent urban citizens compared with first-generation migrants; 7
3) a growing number of young graduates from colleges and universities who (often from a rural background) have difficulty in finding a decent job after graduation, but want to stay in the big cities and therefore also seek minimum-rent housing; 8 and
4) a growing number of ‘land-less peasants’ (失地农民), namely those who have lost their land due to acquisition of a number of investment projects.

Without an effective means to integrate these newer groups of migrants, social tendencies toward polarisation and alienation in urban centres can very easily. Affordable housing programmes could help with such problems, but only if implemented in a prudent manner.

6 The propensity to buy housing increases with the duration of the migration period and the income and educational level of rural migrants.
7 According to Chinese marriage customs the bridegroom’s family should provide housing for the newly married couple. This increases the demand for urban home ownership among younger generation male migrants, but is generally difficult to attain for migrants-in-the city due to low wages, the household registration system and a lack of mortgage schemes.
8 Some of these “floating graduates” will also buy housing in the long run.
3. Housing reform and the affordable housing programme

China’s housing reform started during the 1980s when a few cities began liberalising their housing markets by removing rental subsidies and selling public housing on the open market. In 1988 these new housing measures were taken up at the national level, which effectively shifted the responsibility for providing housing from the government to the market. In 1994 and 1998, the State Council strengthened the housing reform by introducing two directives, one on a market-based housing rental system and the other on a housing provident fund (住房公积金, compulsory housing savings system providing subsidised loans to employed homebuyers). These reforms led to a significant increase in the level of privately owned housing, but created problems in providing housing for lower-income families. Local governments neglected the supply of low-rental housing, and fewer than 3 percent of lower-income families were living in low-rental housing before 2006.

Housing prices in most Chinese cities rose rapidly and created a large group of urban residents in the ‘sandwich stratum’ (夹心层), i.e. those who are neither able to afford private housing nor eligible to apply for public housing (公共住房). One of the reasons behind the property boom was the introduction of an open tender system for residential and commercial land sales in 2002. To generate higher returns, local governments favoured the sale of land to private over public residential developers. These actions were supported by an evaluation system for measuring the performance of local officials that was based on local GDP growth rates. This in turn resulted in a climate that allowed speculators to drive property prices upwards. In response, the State Council established a general framework for a new public housing system in 2007, including fund-raising recommendations for local governments other than land sales, such as acquiring funds from local budgets, collecting rent from lower-rental housing and deriving income from the housing provident fund. That same year the home ownership rate reached 82.3 percent in urban China. However, housing affordability has become a major issue, particularly in large cities.

Against the background of the global financial crisis in 2008/09 and the continuous rise in housing costs, the Chinese government allocated 10% of China’s 4 trillion-yuan (US$ 486 billion) economic stimulus package to the construction of low-income housing, the modernisation of dilapidated housing and other measures to improve housing conditions. Building on this (and again as an economic stimulus), the Chinese government has launched an ambitious programme to provide affordable housing to qualified families. This programme calls for 36 million units of affordable housing to be built within five years (2011-15). When completed, the programme is expected to cover 20 percent of the country’s urban housing supply. In 2010 China started to construct 5.9 million government subsidised flats, and in 2011 some 10 million affordable-housing units should have been built, including 4 million for people in rundown areas, 2.2 million public-housing rental units and 2 million limited-price houses (the latter two options for middle-income earners who cannot afford to buy on the commercial market), and 1.6 million government subsidised low-rental units. Central government funding for building affordable houses has increased from 5.1 billion yuan in 2007 to 16.8 billion in 2008, 47 billion in 2009, 80.2 billion in 2010, and 152.2 million yuan in 2011.

Different cities have created different policies to navigate the central government’s social housing policy. While, for example. Chengdu has launched a pioneering reform of its household registration system that allows tens of thousands of migrant workers living in the city to enjoy the same social benefits (including housing benefits) as their urban counterparts, megacities such as Beijing and Guangzhou are opening up public housing to migrants without a substantial reform of their household registration systems. In Beijing where 7 million migrants make up a third of the capital’s population of 19.6 million (2010), as of December 2011, non-hukou holders may now also apply for public rental housing. But while very clear criteria are in place for applications by Beijing hukou
holders,\(^9\) the criteria for applicants without *hukou* remain vague, and individual district and county governments will stipulate additional requirements based on their specific situations and housing availability. In Guangzhou there are two public housing options: government-administered for *hukou* holders, or society-based (without the *hukou* restrictions). The government is responsible for the ‘sandwich stratum’ as their main target group; for these *hukou* holders the rent should be at least 40% of the market price. For public housing without *hukou* restrictions for which migrants can also apply (certain restrictions such as a specified period of previous city residence, stable employment etc. are still held under consideration), the rent should not be higher than 80% of the market price. In both cities, non-*hukou* holders seeking to apply for public rental housing, cannot own property in the city.

4. Concerns about the affordable housing programme

A variety of concerns have been raised regarding the government’s affordable housing programme. These include:

1) the fiscal risk for local governments;
2) the eligibility criteria for different kinds of affordable housing and a just distribution system;
3) the quality of construction; and
4) rent inflation caused by enforced upgrades following large-scale demolition of urban villages.

4.1 Fiscal risks for local governments

With only 152.2 billion yuan invested by the central government, local governments will have to contribute most of the estimated 1.3 trillion yuan (149 billion euros) for financing the 10 million low and middle-income housing units. This will entail a high fiscal risk for local governments, which will have to borrow and might face difficulties in paying off their debts. This is because they will have to provide developers of affordable housing projects with land essentially free of charge, i.e. they cannot use the auction of land use rights which is normally their main source of income. In addition, the governments will bear an ongoing obligation to pay for property maintenance and repairs.

4.2 The eligibility criteria for different kinds of affordable housing and a just distribution system

As confirmed by the Minister of Housing and Urban-Rural Development, Jiang Weixing, there are loopholes in the programme’s management - illustrated, for example, by the fact that some well-off residents of affordable housing units can be seen driving around in luxury cars. One suggestion is to establish a national information system covering personal housing assets in order to lay the foundation for a fairer distribution system. The lottery system used previously should be replaced by a waiting list of eligible people. Each city – and sometimes even each city district – is establishing its own eligibility criteria for affordable housing. The question of how to integrate migrants into the programme poses particular difficulties, affecting both the balance between the low-income urban population and the rural migrants in the city, and the question of institutional responsibility for the programme’s different target groups.

4.3 The quality of construction

The poor quality of building construction has led to complaints by people who have been resettled due to redevelopment. Several reasons lie behind the concern that the quality of affordable housing

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\(^9\) Beijing *hukou* holders whose current accommodation provides less than 15 square metres of living space per person and whose annual income is below 100,000 yuan for a three-member household are eligible to apply.
might be poor. Because the developers of affordable housing are only permitted a 3% profit margin, quality may suffer as a result of efforts to save money during construction. Another factor is the time pressure facing contractors to finish their work. Moreover, insufficient numbers of skilled workers might be involved in the project, due either to financial restrictions or a shortage of these workers. Either eventuality could lead to poor quality of construction. However, it should be noted that poor quality of construction is also a problem for the construction of commercial sector properties due to the speed and scale at which buildings are built.

4.4 Rent inflation
As part of the affordable housing programme, residents of dilapidated urban housing will be resettled in public rental housing. This may have an unintended negative impact on affordability. As in most urban renewal projects, demolition of this (mainly informal) housing will mean losing the majority of lowest-rent housing stock. Rural migrants often live in the urban villages which have become targets of demolition and renewal. In contrast to the local urban hukou population, they do not receive any compensation when forced to move out. Most of them will probably not be eligible for the affordable housing programme, either because they do not meet the criteria or because they lack sufficient means for the rent. This means that the affordable housing programme would have the effect of enormously increasing the demand for affordable housing by the lowest income groups.

5. Government housing interventions and their impact on the rate of urbanisation

Government housing interventions will probably have a limited impact on the rate of urbanisation in China. For one thing, only a very small part of the affordable housing programme targets low-income families (in 2011 no more than 1.6 million affordable-housing units out of a package of 10 million units) and this will have to be shared among poor urban hukou residents and migrant non-hukou residents. In addition, the megacities and big cities which are the preferred destinations for rural migrants all have strict regulations in place that control and restrict the influx of migrants (even if they are not very effective). Under these conditions, the formulation of eligibility criteria for migrants seeking to participate in the affordable housing programme might turn out to be another instrument for channelling them to the small and medium-sized cities.

The incongruity between official Chinese urbanisation policy that attempts to channel migration streams into small and medium-sized cities and the economic incentives that attract ever greater numbers of rural migrants to mega-urban areas is, to some extent, related to the role of the cities in the Chinese administrative hierarchy. In the course of the reform process, ever more cities received extensive right of autonomy. This has doubtless contributed substantially to China’s economic rise. Yet despite considerable decentralisation, the hierarchical nature of the top-down polity remains. Only first-tier cities are in a position to provide the best public services. Because of their higher rank these cities can gain more resources through administrative means. With more resources, public welfare benefits increase for urban hukou holders. The urban elite might worry that their living environment and access to public welfare benefits will erode as migrants in the city are granted full citizenship rights. The same economic mechanisms attracting rural migrants to megacities are causing their exclusion from costly public services. This has resulted in the emergence of a predominantly informal migration regime including informal housing, employment, schooling and health care.

10 The Chinese administrative hierarchy comprises the following levels: central, provincial, prefectural, county, and town and township governments. This structure basically also determines the configuration of the country’s urban administration: provincial-level cities, deputy-provincial cities, provincial capitals, prefecture-level cities, county-level cities, and towns
6. Two scenarios for promoting urbanisation

Given this situation there are two main scenarios for promoting urbanisation reform: the first scenario would target the administrative hierarchy of Chinese cities and redirect more resources to small and medium-sized cities, enabling them to provide more and better services (including housing) and to attract more investment and migrant workers. That would mean adjusting the existing administrative and management system of cities in line with priorities of the government’s urbanisation strategy. This approach could turn out to be not only very costly, but would also require a considerable amount of time, basic changes to the existing city management system and, if successful, would probably result in rapid growth by these small and medium-sized cities.

The second scenario would open up megacities and big cities to the migrants who already reside there and enable them to become urban citizens without excessively high hurdles. In this case it would be necessary to build on and carefully upgrade the existing informal economy and infrastructure and to provide affordable housing and essential public services. Both scenarios imply a redistribution of resources away from urban hukou holders in first-tier cities - either to smaller cities or to rural migrants living in megacities and big cities who would thus be classified as urban citizens and consumers. The need for a more inclusive approach to migrants in the city becomes even more urgent in view of recent development strategies that place priority on expanding the domestic market and strengthening domestic consumption as part of a structural reorientation of the Chinese economy. A precondition for enabling migrants to settle in the cities, including the big and megacities, consists of greater attention to securing the wages of migrant workers, as well as their social welfare and housing. The main question then would not be how to prevent migrant workers from placing a strain on the urban infrastructure, but how to prepare the physical and social infrastructure needed to receive them as new urban citizens.

7. How central government control of the housing market conflicts with local demand

Since 2010 the Chinese government has introduced various policies to curb speculation and excessive gains from property transactions. Measures include rules that prohibit residents from buying more than a certain number of properties, higher transaction taxes, and an increase in the supply of flats for poor people. Shanghai and Chongqing have launched a trial property taxation system with the aim of cooling down the housing market. The central government’s property market policies are leading to lower prices for most players.

The importance of cooling the property market was reiterated by Premier Wen Jiabao in early February 2012. The main aims here include 1) returning housing prices to a reasonable level; and 2) promoting long-term, steady and sound development of the property market (thus avoiding a burst in the housing bubble). The recent decline in house prices confirms that the policies are working. But at the local level there are various protests and attempts to reverse them. Early buyers in Beijing and Shanghai have been protesting and asking for refunds. Potential home buyers are anticipating further price drops and delaying their plans to purchase a flat. Local governments of third-tier cities are trying to ease or even break the state’s tightening policies. For example, in October 2011 the third-tier city of Foshan in Guangdong province allowed families to buy an additional dwelling and to trade houses that had been owned for more than five years. But the policy was halted within 12 hours after it was announced. The city of Wuhu in Anhui province announced in February 2012 that home purchasers would receive subsidies for an entire year if these homes were smaller than 90 square metres, purchasers of smaller homes would receive an even higher subsidy and all buyers would be exempt from deed tax. This policy was suspended within three days, and the central government seems unlikely to loosen its rigorous real estate policies in the short run.
8. Conclusion and recommendations

- Whereas the Chinese government is seeking to channel rural migrants into small and medium-sized cities, rural migrants are primarily attracted to megacities and big cities because of the greater economic, social and cultural opportunities there.

- This yields two scenarios for promoting urbanisation which focus on big/megacities or on small/medium-sized cities, respectively. Both scenarios imply a redistribution of resources away from urban *hukou* holders in first-tier cities, with the latter scenario probably more costly and difficult to put into practice.

- Due to internal migration there has been a marked increase in the demand for low-rent urban housing, which has been reinforced by a growing tendency toward migration by entire families, higher expectations by second-generation migrants to stay in the cities, a growing number of young graduates from colleges and universities who (even with meagre incomes) wish to stay in the big cities, and a growing number of former peasants who have lost their land.

- It is feared that the housing programme will have a negative impact on affordability due to the replacement of informal housing units with fewer affordable housing units that might still be out of reach for most migrants.

- Government housing interventions will probably have a limited effect on the *rate* of urbanisation in China because only a very small part of the affordable housing programme targets low-income families, and this small part will have to be shared among poor urban *hukou* residents and migrant non-*hukou* residents. In addition, those megacities and big cities which are the preferred destinations of rural migrants all have strict regulations in place controlling and restricting the influx of migrants (even if they are not very effective).

- Central government control of the housing market conflicts with the interests of most players at the local level such as early buyers, potential home buyers, developers and local governments, but is promoting widespread construction of affordable housing and thus could meet the essential needs of lower and middle-income citizens and migrants if – and only if - the many challenges associated with implementing this programme are mastered.

- To ensure the effectiveness and fairness of the affordable housing programme, it is crucial to have clearly defined targets and eligibility criteria. For this purpose a comprehensive social assessment of the government’s affordable housing programme is recommended.

- An exchange on the challenges, experiences and prospects of affordable housing programmes and on redevelopment in the context of urbanisation and migration could help facilitate and deepen the dialogue between China and the EU on sustainable urbanisation and its economic, social and environmental implications.