Buying landed is like buying art

Like scarce art works, they do not yield significant recurrent cash flow but offers capital appreciation. By **ALAN CHEONG**

INVESTING in real estate has never been an easy decision. This has been made even more difficult in a climate filled with a multitude of cooling measures, seven rounds to be precise, since September 2009. To top that, a Total Debt Servicing Ratio (TDSR) limitation was imposed in late June.

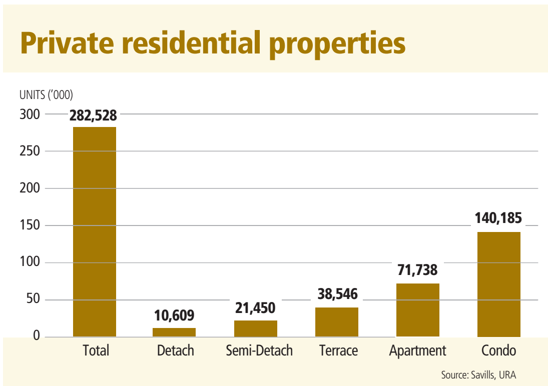
For landed homes, the decision became even weightier because the quantum of investment is significantly larger than for a typical non-landed home, thereby posing greater financial risk to the buyer.

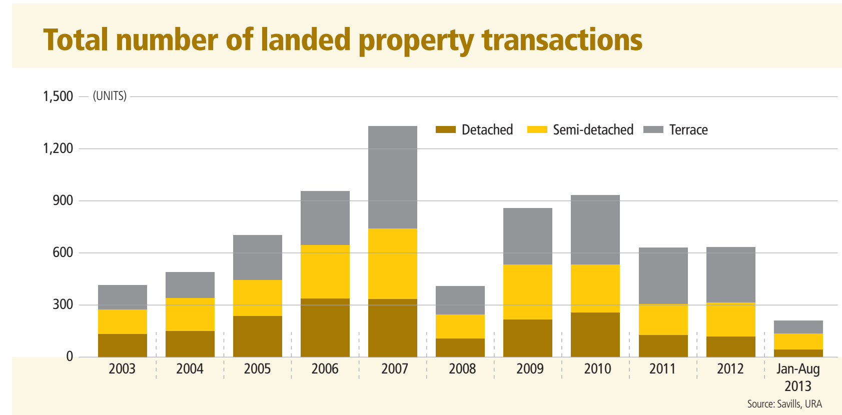
This article highlights some of the historical facts about local landed properties (landed homes and landed properties will be used interchangeably) in terms of price performance, volume of transaction and quantum involved.

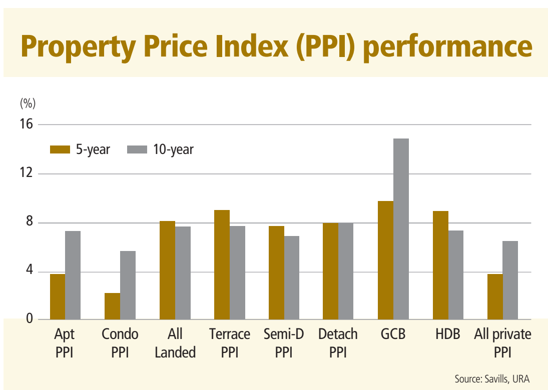
From this, it is hoped that readers can make a more informed decision when confronted with the option of buying a landed property or non-landed one.

A statistic worth remembering is that as at the second quarter of 2013, we have a total completed supply of 282,528 private residential units, of which 211,923 units are non-landed and 70,605 are landed. This means 25 per cent of the total housing stock is landed.

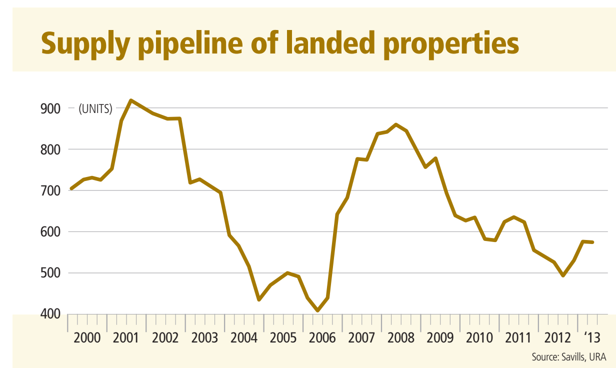
For Good Class Bungalows (GCBs), there are approximately 2,500 of them, representing just 0.9 per cent of the total housing stock or 3.5 per cent of landed stock. Of the 94,773 residential units in the future supply pipeline, only 3,825 are landed or just 4 per cent.







The number of landed properties here will remain below 75,000 units, due to the lack of available land.



Price performance

From the perspective of price performance, using data taken from two periods, one being a five-year and the other a 10-year time horizon, landed properties have provided superior returns over their non-landed cousins.

Over a five-year period, the Urban Redevelopment Authority (URA) All-Landed Property Price Index rose by a compounded 8.2 per cent per annum while condominiums only rose by 2.2 per cent per annum. Over the same period, the URA All-Property Price Index rose by 3.8 per cent.

Over a 10-year period, the URA All-Landed Property Price Index rose by 7.6 per cent versus a lower 5.7 per cent for condominiums and 6.5 per cent for All-Property.

It is clear that landed properties outperformed the other residential asset classes with the exception of HDB resale prices which only marginally bested landed property price growth over a five-year period.

However, over a 10-year time frame, the tables turned, with landed properties outperforming HDB resale prices, also by a whisker.

On a sensitivity basis, the landed property segment shows greater leverage. For the period Q1 1990 to Q2 2013, the price movement of landed properties is more than that for the All-Property Price Index.

Using the concept of beta where a reading of greater than 1 means more movement of the subject asset class than the benchmark (URA All Property Price Index) and a reading less than 1 signifies otherwise, the beta for All Landed Properties was 1.09. In fact, all sub-types of landed properties exhibited a beta of more than 1.

What does that mean? Well, for one, it means that price appreciation for landed property is superior to that of non-landed ones.

Unfortunately, what goes up fast can similarly come down fast. This is the major negative of landed properties because in a down market, values of landed properties can also depreciate faster than condominiums.

Therefore, with regard to downward price movement, investors who purchase landed properties must have ample store of wealth to overcome the vicissitudes of the market.

In a downturn, not only may their prices decline more than other housing types, but they may become illiquid, which may result in distressed prices when a forced sale occurs.

Sales volume

Transaction volume for the landed property segment has been low. This is no surprise because of the twin reasons of having a relatively low number of units available for sale and the absolute quantum required, which weeds out a large audience of buyers.

As a proportion of total transactions from January to August this year, the total number of landed home transactions amounted to just 1.5 per cent of the market.

This is a key factor to be cognizant of as the liquidity factor – or to be more precise, the lack of it – can hamper one's ability to raise cash quickly when it is needed.

When under pressure, because of illiquidity, sellers who wish to raise cash fast may end up having to offer steep discounts.

Turning to examples of landed properties transacted in districts 9, 10, 11, 21 and 23, we find that prices for various sub-types of landed properties have performed well over a 10-year period.

Of late, prices, when measured on a dollar per square foot (psf) basis, have started to taper although on an absolute quantum measurement, they are still rising.

Limited supply: *As at the second quarter of 2013, there was a total completed supply of 282,528 private residential units, of which 211,923 units are non-landed and 70,605 are landed. This means 25 per cent of the total housing stock is landed.* FILE PHOTO

Why buy landed

Limited stock: Given that the pipeline of supply in this segment of the housing market makes up only 4 per cent of the total future supply, it offers assurance that it is less likely to face an oversupply situation.

Very likely, for the foreseeable future, the number of landed properties here will remain below 75,000 units, due to the lack of available land for such low density developments. Also, even if there is land from the government, this type of development does not usually reap the highest and best return, monetarily speaking.

Also helping long-term price appreciation is the fact that most of the landed properties are on freehold or on 999-year leasehold land.

The relative scarcity of landed homes makes them behave a little like art works and antiquities, which do not yield recurrent cash flow but may offer capital appreciation.

Landed properties have the benefit of both – rental yield, (although at a low a sub-3 per cent level compared with the 3 to 3.5 per cent range for non-landed properties), and capital appreciation.

Moving up the social class: Over a longer term, as landed property tends to rise more than the All-Property Price Index, it has the effect of securing and augmenting one's socio-economic standing.

Using the analogy of an expanding universe, the further galaxies are from us, the faster they move away.

Hence as each landed property sub-type represents a higher order of housing, it tends to pull away from the lower order housing classes.

Over the longer term, it may become more difficult for one to purchase landed properties due to this reason.

Based on historical data, it therefore pays to be positioned in the landed housing category.

Retirement and inheritance planning: Given the expected largesse from selling a landed property after a long-term holding period, this asset class provides the owner the luxury of cashing out of the property and downgrading to a smaller or non-landed abode to realise cash for his/her retirement.

Alternatively, it may serve as a store of wealth to transfer to the next generation who may find it difficult to keep up with the widening income disparity if they are purely mainstream economic performers.

Risks

Buying landed property is, however, not without risks.

Although prices for such properties tend to move up more than other classes of residential properties, they can also come off faster.

The issue of timing then becomes more crucial vis-a-vis one's financial status.

If one's financial resources are stretched, entering the landed property market when prices look toppish exposes one to downside risks should one's ability to service the mortgage be hampered by a high correlation to a declining property and other complementary markets.

In a way, the seven rounds of cooling measures plus the TDSR guideline acts as a preventive gantry for over-adventurous risk taking.

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