SINGAPORE (INCLUSIVE OF GST) S$3.80

OTHER HIGHLIGHTS

To Afiniti and beyond
CITY & COUNTRY

Emerging-market bargains
PERSONAL WEALTH

THE ASCOTT INTERVIEW
Louis Vuitton's time to shine
OPTIONS

THE EDGE SINGAPORE

www.theedgesingapore.com

BUSINESS & INVESTMENT WEEKLY

THE WEEK OF JUNE 10 — JUNE 16, 2013 578

MCI (P) 064/03/2013 PPS 1519/09/2012 (022805)

NOTEWORTHY

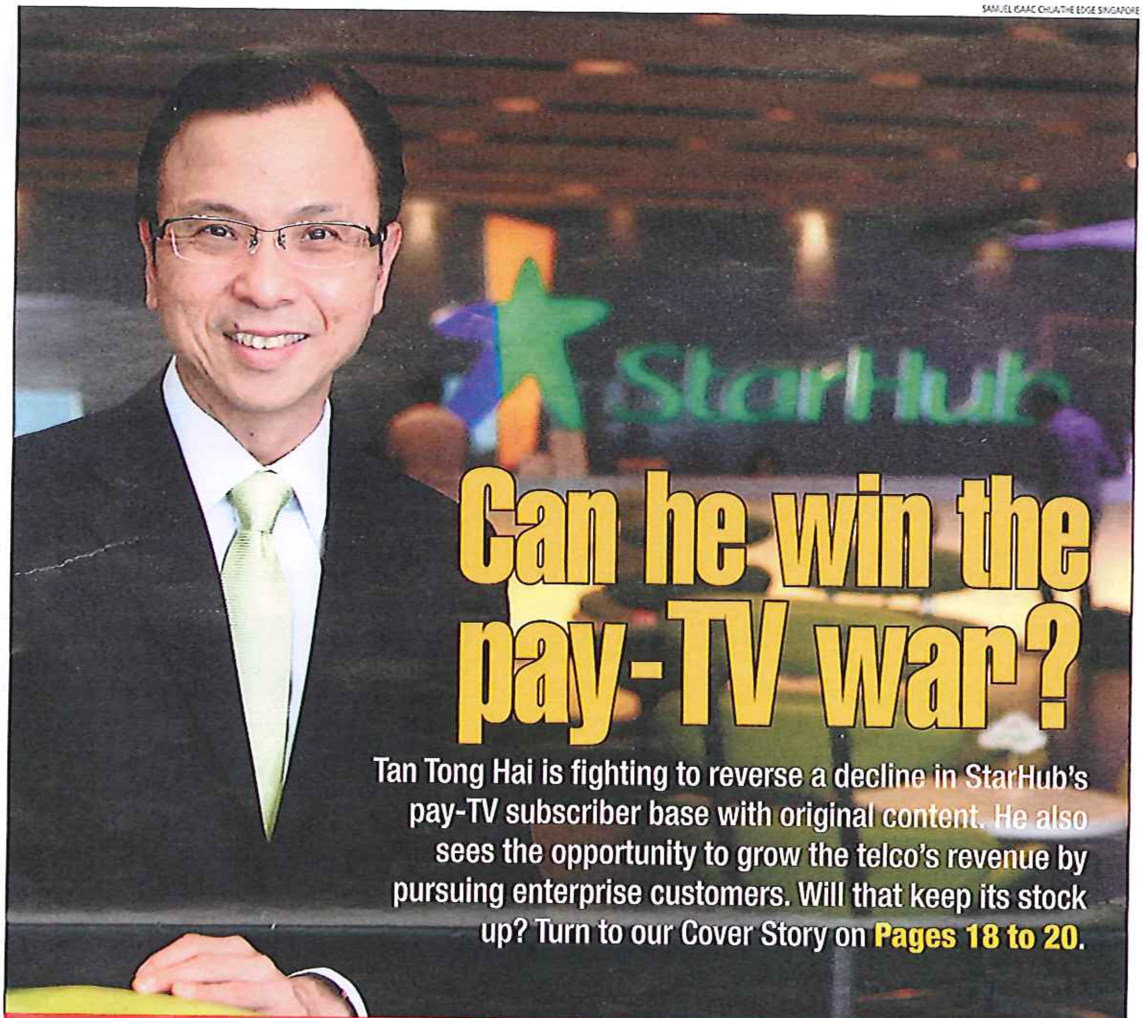
PATRICK LECOMTE: A European perspective on China's urbanisation and property speculation PG6

Diverging fortunes for bank stocks and REITs as US Fed mulls QE 'tapering' PG10

LIM YIN FOONG: London transformed by new developments PG22

8 885002 090004 >

SAMUEL ISAAC CHUA/THE EDGE SINGAPORE



Can he win the pay-TV war?

Tan Tong Hai is fighting to reverse a decline in StarHub's pay-TV subscriber base with original content. He also sees the opportunity to grow the telco's revenue by pursuing enterprise customers. Will that keep its stock up? Turn to our Cover Story on **Pages 18 to 20.**

PLUS: **ISP ViewQwest rocks the boat with its own TV offering**

A European perspective on China's urbanisation and property speculation

| BY PATRICK LECOMTE |

In recent months, China's Prime Minister Li Keqiang and the new Chinese leadership have targeted urbanisation as a priority for the Chinese economy. Urbanisation will boost economic growth and create a better living environment for all. In addition to the building process, which generates economic activities in the short to medium terms, cities are opportunity creators, by enabling the aggregation of skills, talents and resources conducive to innovation and growth.

There has never been in human history such an ambitious plan as the one proposed by the Chinese central government to spur urbanisation. The World Bank estimates that by 2030, two-thirds of Chinese will live in cities, which means that 14 million people will move to newly built cities every year over the next two decades. In terms of both geographic scope and size of population concerned, the process undertaken in China will break records. What could be the consequences of this plan on real-estate markets? Can there be urbanisation on such a large scale without potentially harmful speculation in residential-property markets at the city level?

Industrial Revolution and speculative urbanisation

Notwithstanding very different situations in China and Europe, European history provides a few examples illustrative of the great benefits to be expected from a massive urbanisation push as well as a few pitfalls to be avoided. During the second half of the 19th century, while Europe was rapidly modernising under the Industrial Revolution, major urbanisation programmes were carried out in many European cities to accommodate the massive inflows of rural migrants.

For instance, Paris was totally redesigned by urban planner Baron Haussmann who turned a medieval city into a cosmopolitan metropolis catering to a rapidly growing middle class. The process, which lasted more than 30 years, involved many speculative excesses, leading to blatant hardships in the poorer parts of society. Speculators of all kinds intervened in the property market, turning land acquisition and development into a game of Monopoly. Similar speculative phenomena on other continental property markets (for example, Germany and Austria) led to the Vienna Stock Exchange crash in May 1873, which triggered a major banking crisis and a global recession. If history can teach us anything, how can China avoid the mistakes made in Europe?

Space market versus asset market

In effect, in a market economy, there are two groups of people intervening in the housing market: people who actually need the space to live in (space users) and people who buy and sell the space for investment and ultimately profit-making (investors). This is a unique characteristic of properties to be exchanged on two parallel markets: the market for space occupied by genuine users and the asset market occupied by investors. For urbanisation to be beneficial to all, both markets should function properly, that is, there should not be permanent imbalances between a property as a place to live and the same property as an investment asset. When speculators intervene in the asset market, the space market might get disrupted so that people in genuine need of housing might not be able to find or afford it.

So, what can be the way forward for a harmonious urbanisation in China? There are no miracle solutions to ensure that all parties involved in the real-estate process incorporate the greater good into their decision-making. However, several measures have been successfully implemented in Europe in order to accommodate both genuine users in need of space and investors, from long-term property owners to short-term speculators.

Four successful measures implemented in Europe

First, the power of the markets can be harnessed to tame speculative pressures on property prices. One way to do so is to encourage securitisation of private properties on stock markets through specific investment vehicles such as real estate investment trusts (REITs), which do exist in most European countries. When prices in the asset market become inflated and disconnected from the levels supported by the actual interplay between demand and supply in the space market, then rational equity investors will signal that real-estate investors are getting ahead of themselves by selling stocks of such property trusts. In that sense, stock markets can provide a system of checks and balances to control speculation in real-estate markets, if only by fostering greater disclosure. This process should be accompanied with a series of measures promoting consistent guidelines for property valuation and transparent indices of real-estate prices.

Second, developers should be incentivised to build affordable housing in good locations. Such measures exist in the UK, where the Town and Country Planning Act allows developers and local authorities to enter into legally binding agreements about issues such as infrastructures, community facilities, transport improvements and affordable housing. All over the UK, more than half of all new affordable housing is developed under such agreements. In the Greater London region, over 75% of residential developments of more than 10 units are subject to agreements between local planning authorities and developers. Policies in place have to be robust and clear.

Third, the focus should be on the quality, rather than the quantity, of the newly built environment. A short-term approach tends to forgo quality over volume of space created. Interestingly, in economic theory, the pricing of a dwelling is dependent on its qualitative attributes affecting space users' perception of the property's benefits rather than its size alone. Externalities, such as pollution and the environment, are important attributes, and will probably increasingly matter to the Chinese middle class. One of the main problems with the speculative urbanisation in 19th century Paris was that in many areas of the French capital, developers did not take into account the needs of the neighbourhoods and built without paying any attention to the quality of life for people ultimately using the space. As a result, when property prices did eventually adjust down, low occupancy rates made the crisis worse. Hence, there should be controls in place to make sure that developers don't build too much or too little, or the wrong types of properties, given each neighbourhood's needs.

Fourth, investors who need to have access to a wide range of sound investment alternatives should be incentivised to become long-term holders of properties rather than short-term speculators. Long-term investors tend to rely more on the rental returns of their properties rather than on the more volatile and speculative capital returns. One way to do so is to inversely link capital gains taxes on property sale to the owners' holding periods, at least for secondary residences. For instance, in France, the substantial capital gains tax on secondary residences (34.5% in 2013) decreases by 2% after six years and falls to 0% after 30 years. Comparable tax regimes, albeit oftentimes less stringent, are in place in most European countries. This eases pressures on short-term prices, thereby allowing for sounder and more sustainable real-estate markets.

Beyond its economic and social consequences, urbanisation is a process with a durable impact on a country's geography. What is at stake for China today is the definition, on a scale unheard of in human history, of urban landscapes that should provide good quality of life to its citizens while contributing to the country's long-term positioning as one of the world's leading economies. This is possibly the most exciting challenge ever faced by a single country since the Industrial Revolution swept through Europe 200 years ago. E

Patrick Lecomte is executive director at ESSEC Asia-Pacific.