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BUY OR RENT: living in singapore

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The Wong family—comprising Mr. Wong, aged 40, Mrs. Wong, aged 38, and their three young children— relocated to Singapore in 2010 when Mr. Wong received a job offer from a leading investment banking giant. For the next six years, they rented a three-bedroom condominium for US$4,000 in Singapore dollars[[1]](#footnote-2) per month, which included parking and condominium fees but not the maintenance cost, which was borne by the owner.

While renting made life easy, the Wong family began weighing the pros and cons of purchasing a larger unit, in the same building, that became available in June 2016. In the past three years, the real estate market had softened somewhat and the cost of the unit had declined from $1.6 million to $1.5 million. The idea of home ownership as a form of pension investment appealed to the couple. The monthly rents could be used for mortgage payments instead.

Home ownership as a form of investment

Some years back, the Wongs had made the decision to settle down in Singapore. They were ecstatic to receive Singaporean citizenship in January 2016. They understood that Singapore had a pay-as-you-go pension system that placed the responsibility of retirement planning on the individual instead of the state. All citizens were required to put a percentage of their monthly income into their own account in the Central Provident Fund (CPF),[[2]](#footnote-3) which was managed by the Singapore government.

On reaching the retirement age of 55, all Singaporeans could choose to receive a lump sum from the CPF after setting aside a minimum sum. The minimum sum would be kept untouched until age 65, at which time monthly payouts would be made to the retiree until he or she passed away (see Exhibit 1).

The savings in the CPF alone might not be sufficient for a citizen to maintain the same standard of living after retirement. For stay-at-home spouses, the problem was very real. Since Mrs. Wong was a housewife, Mr. Wong would need to have additional savings to provide for himself as well as his wife.

The Singapore government strongly encouraged home ownership as a form of savings. After retirement, if the need arose, the retiree could unlock savings by moving to a smaller unit or consider a reverse mortgage. First-timer buyers (only citizens with monthly income below $12,000 qualified as first-time buyers) of public housing could obtain subsidies from the government. First-time buyers of private property, such as condominiums, would not qualify for subsidies.

Singapore citizens who purchased properties could pay part of the down payment using their CPF funds. Specifically, for a $1.5 million property, the Wongs had to put down a minimum of $75,000 in cash and withdraw $225,000 from the Ordinary Account of their CPF accounts. They could borrow up to 80 per cent loan-to-value or $1,200,000, assuming they qualified for the loan.

singapore property market

Between 2009 and 2013, property prices rallied 70 per cent. Exhibit 2 shows that the residential price index reached a level of 170 in the third quarter (Q3) of 2013 while it was at a level of 100 in Q1/2009. During the same period, the average nominal wages increased by only 30 per cent.[[3]](#footnote-4)

Since 2013, the Singapore property market had softened on the back of sluggish economic growth, various newly adopted property cooling measures[[4]](#footnote-5) (see Exhibit 3), and a large supply of newly built private residential units. According to Augustine Tan, president of the Real Estate Developers’ Association of Singapore, there were 57,597 new private residential units and 12,077 executive condominiums available as of May 2016. These numbers were significant in view of the prevailing weak demand.[[5]](#footnote-6) Exhibit 4 shows that the supply of new units in the pipeline had dropped from Q1 to Q2 in 2016.

Property home prices had dropped for 11 straight quarters at the end of June 2016.[[6]](#footnote-7) Prices were 9.4 per cent below the peak of Q3 in 2013.

At the central bank annual briefing on July 25, 2016, Ravi Menon, the managing director of the central bank—the Monetary Authority of Singapore (MAS)—said that MAS was “quite happy” with the way the property sector was evolving.

It’s a gradual softening of prices, unwinding some of the sharp run-up that you saw earlier. The household debt situation has improved and the debt servicing ratio for new loans is very good. Banks’ non-performing loans for property are very low. So we don’t have concerns for the property market as such. I think things are playing out in a good manner.[[7]](#footnote-8)

Menon said it was too early to lift the cooling measures, as “we want to make sure the gains we have made painstakingly over the last one to two years are entrenched, that we are on a sustainable path for the property market, and that the household balance sheets become stronger still to withstand (interest rate and income) shocks.”[[8]](#footnote-9)

financial considerations

While the Wongs really liked their rental unit and its surroundings, their children preferred to have their own rooms. The larger unit, with four bedrooms, would be just right for them.

If the Wongs made the purchase, they would need to pay a maintenance fee of $250 monthly to the condominium management committee, property tax of $100 per month to government authorities, and the cost of repairs and general maintenance within the unit of $100 per month.

The initial cash payments included a down payment of 20 per cent of the purchase price, 3 per cent stamp duty, 1 per cent agent fee, $4,000 in legal transfer fees, and $4,000 in other closing fees.

The Wongs planned to take a 30-year tenure loan with monthly instalment payments. The bank officer informed them that the current mortgage rate was a 3 per cent annual percentage rate. While the market conditions for borrowing had been favourable in recent years with the low interest rate environment, the Wongs worried that the interest rate might increase in the near term, making borrowing more expensive.

In Singapore, loans from commercial mortgages were generally in the form of hybrid adjustable-rate mortgages; the interest rate would be fixed for the first three years and adjusted thereafter based on the local one-month or three-month Singapore Interbank Offered Rates. Since 2015, the one-month and three-month Singapore Interbank Offered Rates had been increasing. In June 2016, they stood at 0.76 and 1.00 per cent respectively, more than double the average levels from 2009 to 2014 at 0.35 and 0.47 per cent respectively (see Exhibit 5).

possible scenarios

The Wongs had been advised that if they were buying to stay, it did not matter when they entered the market. This sounded rather counterintuitive to them. How could it not matter if they had to put out more money? It would definitely affect the size of their gains/losses if they were to sell the property in, say, 10 years’ time. They decided to conduct an analysis of the net gain or loss on the purchase based on several scenarios:

* In scenario 1, the selling price of the condominium unit remained unchanged at $1.5 million at the end of 10 years.
* In scenario 2, the selling price was up 10 per cent.
* In scenario 3, both the rent and the selling price increased by 0.15 per cent per month for the next 10 years.
* In scenario 4, the annual mortgage rate would be increased by 0.5 per cent from the first year onward and would be constant for the next 10 years.

For their analysis, they assumed that when they eventually sold the condominium unit they would need to pay the principal still outstanding on the loan and a 1.00 per cent agent fee on the selling price.

other considerations

The property purchase would be a huge investment for the Wongs. Mrs. Wong felt uneasy. Mr Wong, however, was worried that the property market might rebound soon and they might miss this golden opportunity.

Apart from their quantitative computations, they had to consider certain qualitative factors. For example, property transactions played a key role in the life of many families in Singapore as primary school districts were closely tied to residential addresses. Thus, properties sited close to popular schools would invariably command a premium.

Exhibit 1: Types of CPF Accounts and Retirement Sum

|  |  |  |  |
| --- | --- | --- | --- |
|  | **Ordinary Account**  **(to be used for**  **home purchase**  **and insurance)** | **Special Account and Medisave Account**  **(for investment and health care)** | **Retirement Account**  **(in SG$)** |
| Interest rate at June 2016 | 2.50% | 4.00% | 4.00% |
| At age 55 | Transfer to  Retirement Account |  | Automatically opened |
| **Retirement sum** |  |  |  |
| Basic retirement sum for age 55 in 2016 |  |  | 80,500 |
| Full retirement sum for age 55 in 2016 |  |  | 161,000 |
| Enhanced retirement sum for age 55 in 2016 |  |  | 241,500 |
| Basic retirement sum for age 55 in 2020 |  |  | 90,500 |
| Full retirement sum for age 55 in 2020 |  |  | 181,000 |
| Enhanced retirement sum for age 55 in 2020 |  |  | 271,500 |

Source: Central Provident Board Fund, accessed April 11, 2017, www.cpf.gov.sg/Members/Schemes/schemes/retirement/retirement-sum-scheme.

**Exhibit 2: Housing Price Index in Singapore**

Note: Q = quarter

Source: Price Index: Urban Redevelopment Authority, accessed December 15, 2016, www.ura.gov.sg/uol/-/media/User%20Defined/URA%20Online/media-room/2016/jul/pr16-49a2.pdf?la=en; Rent Index: Urban Redevelopment Authority, accessed December 15, 2016, www.ura.gov.sg/uol/-/media/User%20Defined/URA%20Online/media-room/2016/jul/pr16-49a4.pdf?la=en.

**Exhibit 3: Property Cooling Measures**

Additional Buyer Stamp Duty (ABSD)

|  |  |  |  |
| --- | --- | --- | --- |
| **Citizenship** | **ABSD Rate on Primary Home** | **ABSD Rate on Secondary Home** | **ABSD Rate on Tertiary and Subsequent Homes** |
|
| Singapore citizens | N/A | 0% revised to 7% | 3% revised to 10% |
| Permanent residents | 0% revised to 5% | 3% revised to 10% | 3% revised to 10% |
| Foreigners and non‑individuals | 10% revised to 15% | 10% revised to 15% | 10% revised to 15% |

Additional Seller Stamp Duty (SSD)

|  |  |  |  |  |
| --- | --- | --- | --- | --- |
| **Residential Property** | **Sold in Year 1** | **Sold in Year 2** | **Sold in Year 3** | **Sold in Year 4** |
| SSD rate since February 2010 | Same as basic buyer stamp duty | N/A | N/A | N/A |
| SSD rate since August 2010 | Same as basic buyer stamp duty | 2/3 of basic buyer stamp duty | 1/3 of basic buyer stamp duty | N/A |
| SSD rate since January 2011 | 16% | 12% | 8% | 4% |

Restrictions on Loan-to-Value (LTV) Ratios

|  |  |
| --- | --- |
| February 2010 | For all loans, the LTV values are revised down from 90% to 80%, to reduce speculative buys in the market. |
| August 2010 | For the first loan, the LTV remains at 80% and for the second loan is revised down to 70%. |
| January 2011 | For the second loan, the LTV is further reduced to 60%. An additional new restriction is introduced for non-individuals, requiring maximum 50% LTV. |
| October 2012 | For the first loan, the LTV is revised down to 80% and for second loan is revised down to 60%. For non-individuals, it is revised down to 40%. |
| January 2013 | For the first loan, the LTV is revised down to 80%, for the second loan down to 50%, and for third loan down to 40%. For non-individuals, it is revised down to 20%. |

Note: N/A = not available

Source: “Singapore Property Market Cooling Measures,” Singapore Real Estate Exchange, accessed December 15, 2016, www.srx.com.sg/cooling-measures.

**Exhibit 4: Available Units, Vacant Units, and Future Supply**

**of Private Residential Units**

|  |  |  |  |  |  |
| --- | --- | --- | --- | --- | --- |
|  |  |  | Q1/2016 | Q2/2016 | Change |
| Completed units | |  |  |  |  |
|  | Available | (# of units) | 330,303 | 338,728 | 2.60% |
|  | Occupied | (# of units) | 305,384 | 308,418 | 1.00% |
|  | Vacant | (# of units) | 24,919 | 30,310 | 21.60% |
|  | Vacancy rate | (per cent) | 7.50 | 8.90 |  |
|  |  |  |  |  |  |
| Supply in the pipeline | |  |  |  |  |
|  | Under construction | (# of units) | 46,815 | 41,102 | −12.2% |
|  | Planned development | (# of units) | 6,697 | 6,148 | −8.2% |

Note: Q = quarter

Source: Urban Redevelopment Authority, accessed December 15, 2016, www.ura.gov.sg/uol/-/media/User%20Defined/URA%20Online/media-room/2016/jul/pr16-49e1.pdf?la=en.

exhibit 5: historial trend of Short-term Interest Rates and one-year government bond yield

Note: SIBOR = Singapore Interbank Offered Rates; T-bill = Treasury bill

Source: One-year T-bill rate: Singapore government statistics, accessed December 15, 2016, www.sgs.gov.sg/Statistics.aspx; one-month and three-month SIBOR rates (until December 2013): “Domestic Interest Rates,” Monetary Authority of Singapore, accessed December 15, 2016, www.mas.gov.sg/Statistics/Other-Statistics.aspx; the recent SIBOR rates from January 2014 onward is from MoneySmart, accessed February 9, 2017, www.moneysmart.sg/home-loan/sibor-trend.

1. All currency amounts are in SG$ unless otherwise specified; SG$1 = US$0.75 on March 31, 2016. [↑](#footnote-ref-2)
2. The Central Provident Fund (CPF) was a comprehensive social security system that enables working Singapore citizens and permanent residents to set aside funds for retirement. It also addressed health care, home ownership, family protection, and asset enhancement. Both employees and employers made monthly CPF contributions. These contributions went into three accounts: Ordinary Account , Special Account, and Medisave Account, where the contributions from the Ordinary Account could be withdrawn before retirement for housing, insurance, investment, and education purposes for the contributor or for his or her children; “CPF Overview,” Central Provident Fund Board, accessed August 29, 2016, www.cpf.gov.sg/Members/AboutUs/about-us-info/cpf-overview. [↑](#footnote-ref-3)
3. The Business Times, “Property Cooling Measures: Why Cautionary Stance Still Needed,” July 26, 2016, accessed August 4, 2016, https://global-factiva-com.libproxy1.nus.edu.sg/ha/default.aspx. [↑](#footnote-ref-4)
4. “Singapore Property Market Cooling Measures,” Singapore Real Estate Exchange, accessed August 4, 2016, www.srx.com.sg/cooling-measures. [↑](#footnote-ref-5)
5. Geraldine Goh, “Weak Sentiment Still Weighing Down Singapore Property Market, Says Redas Chief Augustine Tan,” *Straits Times,* July 12, 2016, accessed August 4, 2016, https://global-factiva-com.libproxy1.nus.edu.sg/hp/printsavews.aspx. [↑](#footnote-ref-6)
6. Lynette Khoo, “Property Cooling Measures: Why Cautionary Stance Still Needed,” *Business Times,* July 26, 2016, accessed August 4, 2016, www.businesstimes.com.sg/companies-markets/property-cooling-measures-why-cautionary-stance-still-needed. [↑](#footnote-ref-7)
7. Rennie Whang, “‘Too Early’ to Lift Property Cooling Measures: MAS,” *Straights Times,* July 26, 2016, accessed August 4, 2016, https://global-factiva-com.libproxy1.nus.edu.sg/ha/default.aspx. [↑](#footnote-ref-8)
8. Ibid. [↑](#footnote-ref-9)