Erroneous Thinking: Real Estate Prices Won't Go Up Due to Land Plenty?

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When people talk about real estate prospects in China, many think that prices will not go up as "there is plenty of land". While not disagreeing with this view entirely (as statistically one needs just one case to prove its possibility), the author is inclined NOT to embrace it for the following reasons:

a) **Many people who hold this real estate (prices not going up) view also think that China's economy and GDP per capita will continue to grow and improve = this is ILLOGICAL**. Real estate in the long run reflects the economy and its performance, though whether the economic and the real estate cycles move in exact tandem is another question. If the economy does grow while real estate prices remain the same (or even go down), then one would have to assume either a highly inefficient real estate information distribution system, or highly incompetent real estate participants, or both. Or perhaps some form of market policy diversions. Otherwise, in the long run, such situations do not exist in a market economy. When was the last time you came across an economy / country / city where its typical / average residents can easily afford 10 or more properties, i.e. properties there are not considered a big ticket item?

b) **Land needs to be "serviced" before they become useful** = such as being accessed by roads and with water and electrical connections etc. Even farmlands nowadays are serviced in this sense, let alone lots required for buildings. This means two things. First, there is a limit to land supply as "servicing" them requires resources including capital, though this limit may be at a relatively high level depending on the scale of the economy / city etc. Second, this limit is limited perhaps not so much by technologies (in developing and servicing land) but by economics. Conceptually, however far-reaching the "urban sprawl", it will stop at boundaries where the land value created after servicing the land is less than the expenses / costs (plus land developer's required profit) needed to develop it. As economies grow, the costs of opening up more land also increase.

c) **Land of "Good Location(s)" are always limited in supply** = irrespective of how large the urban sprawl or even for a growing city, good locations in established areas are limited in supply and as such command a premium over other properties at any one time. Furthermore, it takes quite some time to develop and create alternative good competing locations in the newer areas.

d) **Proof: USA** = she has more land than China and yet with only around 1/4 of the population (300M versus China's 1300M). IF the "Land Plenty" theory is correct, THEN USA real estate prices are 10 or more times way over what they are worth. Naturally, this is NOT the way to look at the issue. Real estate prices are influenced / affected / manipulated / controlled by a range of factors, some economic, some social-cultural, and some political-administrative. Earning power is one of these factors. The GDP per capita for the USA is around US$28,000 while top cities such as Shanghai's GDP is only around US$4,000. It should not be a surprise if real estate prices in the USA are still several times higher than those in China.

Please note we are NOT saying that real estate prices in China will definitely rise or will only go up, it is just that <u>having plenty of land alone is not a sufficient condition to contain price increases, just as having little land is not a sufficient condition to guarantee price increases</u>. Supply is just one aspect.