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3-2015

### Managing superstar cities

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#### Citation

Singapore Management University. Managing superstar cities. (2015).

Available at: <https://ink.library.smu.edu.sg/pers/212>

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# MANAGING SUPERSTAR CITIES

Published:

25 Mar 2015



*Attractive cities draw people from around the world. Comprehensive and decisive urban planning is needed to deal with the resulting property price surge*

In his paper “Superstar Cities”, economist Joseph Gyourko documented differences in house prices and income growth rates between 1950 and 2000 across various U.S. cities. Gyourko explained how the “ever-widening gap in housing values and incomes between the typical and highest-priced locations” within each city can be partially attributed to “inelastic land supply in some places combined with growth in the high-income population”.

“The whole thing about superstar cities is that there is a supply constraint,” explains Phang Sock Yong, Celia Moh Professor and Professor of Economics at the SMU School of Economics (SOE). “Superstar cities are attractive locations, and people are attracted to the city. Companies are also attracted to such cities because of agglomeration economies, and that somehow by locating to these cities productivity is higher and costs are lower. Therefore they are willing to pay higher rent.

“These cities have to deal with the problems of success, which is that everybody wants to be there. How each city deals with these problems will determine the property prices that arise.”

## “We must make land common property”

Speaking to *Perspectives@SMU* on the sidelines of the recent SMU SOE Celia Moh Professorial Chair Public Lecture, “*Superstar Cities, Inequality and Housing Policy*”, Phang highlighted the reasons for increasing disparity in income and property prices.

“For example, in New York, the pay for the global elite and CEOs justifies whatever these people are paying for rent. The lower income folks are also drawn there because the jobs, and service sector jobs in particular, are more plentiful. For them, it’s better to be in the superstar city than to be in smaller city or the rural areas.”

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She adds, “As for the middle income, there is some sorting. The upper middle class might go, ‘For the same job, I can get a better deal elsewhere,’ and they might go to another city. This has been happening, and it also drives income inequality in superstar cities.”

To deal with these problems, it would help to look at the principles espoused by 19<sup>th</sup> century economist, Henry George. In his 1879 book, “*Progress and Poverty*”, George argued: “We must make land common property” to limit the unearned income – and social advantages – that accrue to landlords.

In that respect, Singapore is a good example in the application of George's ideas. The 1966 Land Acquisition Act was passed to meet the government's need for "an adequate supply of land to carry out its developmental projects, especially those concerning resettlement and industrialisation"<sup>[i]</sup>. In the words of Singapore's founding Prime Minister, the late Lee Kuan Yew:

*"First, that no private landowner should benefit from development which had taken place at public expense; and, secondly, that the price paid on the acquisition for public purposes should not be higher than what the land would have been worth had the Government not contemplated development generally in the area."*

The act was amended in 1973 to curb land speculation, fixing the compensation amount for acquired land "at market value as at 30 November 1973 or at the date of gazette notification, whichever was lower"<sup>[ii]</sup>. That stayed on the books until 2007 when compensation was determined as the market value of the land as at the date of its acquisition.

"You need the government to intervene in the markets," Phang argues. "There are so many sources of market failure in cities. You need urban planners to have the power to amalgamate land for redevelopment. To be able to plan on a sufficiently large scale, in order to generate the kinds of positive externalities and overcome the problems of fragmented ownership, and also the unearned increments accrued to landlords, careful urban planning is necessary."

## Singapore as a blueprint

Having the power and authority to acquire and amalgamate land is one thing, using it in the best way to increase housing supply is another. Whereas Singapore is committed to high-rise and high-density housing, cities with policies against either high-density or high-rise housing end up with a more acute housing shortage, and thereby more expensive housing.

"The Singaporean government plays a big part in the supply equation, releasing land in Government Land Sales," Phang explains. "It has gone for high-density housing. The housing price premium in some cities is a reflection of a policy to not allow high-density development."

Paris is a prime example of such building policies. Until 2010, buildings in inner Paris cannot be built beyond 37 metres in height. Phang attributes part of the city's infamously high property prices to such policies that limit the supply of housing units, thereby driving up prices and rent. Phang also points out the need to balance the interests of global investors betting money on property in superstar cities and those who live in them.

"Housing is a consumption good, and that impacts the way it is treated as an investment good," Phang explains. "When you buy a bond or a stock, there is no other externality than the fact that you are financing capitalism, which is a good thing. When it comes to housing, people invest in housing and property, and it can drive up the price of consumption for the rest of society, especially for the lower income groups who cannot afford the rising rent or price as a result."

"In global superstar cities, you have to watch that consumption/investment demand quite carefully. You must make sure that investment demand doesn't lead to inequality in housing outcomes in terms of affordability for the rest of the population."

For cities that are on the verge of becoming superstar cities, how should housing matters be handled? Could Singapore be used as a blueprint to successfully manage the inevitable tensions?

"Singapore has succeeded because of its very deliberate land use," says Phang. "Many cities that are on the verge of becoming superstar cities don't have that same framework that Singapore has. Some countries still have rent control issues, as well as whether there is enough government capacity to deal with the need to resettle. These are issues cities have to deal with as they grow."