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Deciding between freehold and leasehold

by Png Poh Soon and Jing Tang

Why are freehold properties preferred to leasehold properties? Given that the current median life span in Singapore stands at 81.4 years, a 99-year leasehold property, whose ownership reverts to the State after this period, offers a more than adequate home for any one generation.

But setting aside owner-occupation, if you expect your property to be an investment for wealth preservation or a legacy for future generations, then a freehold home, which allows you to hold the property in perpetuity, makes more economic sense.

This argument holds even for 999-year leasehold properties, which effectively function like freehold properties, although technically and legally they are in effect still leasehold properties.

Against this backdrop, the preference for freehold property over leasehold property is simple economics - if supply is limited and demand increases, prices go up. We studied resale prices of freehold versus leasehold properties and found that the difference was between 10 and 15 per cent.

There are many factors that can affect resale prices over time. Location, proximity and unit types are among the variables.

Admittedly, it is quite difficult to find freehold land and leasehold developments in close proximity. Nonetheless, there are still some locations that fit our selection criteria. Also, in arriving at our 10- to 15-per-cent figure, we categorised transactions by floor area, to eliminate discounts of larger units.

But this differential between freehold and leasehold properties is also affected by market conditions. During a downturn, both freehold and leasehold properties slide in tandem with the broader market.

At times, the price differences narrow. This then becomes a window of opportunity to buy that coveted freehold property.

Interestingly, when the broader market recovers, freehold properties, in particular those with significant en-bloc potential were observed to appreciate faster than leasehold properties. In some cases, the price premium reached more than 25 per cent.

But before you splurge on that dream freehold property, there are a few points to note. The first is that despite the property being freehold - age matters. Older developments command

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lower prices and also have a slower rate of capital appreciation. This is because of a variety of factors. Among them: The greater cost of maintenance and a general preference among Singaporeans for newer properties with fancy fixtures and fittings.

But when it comes to buying property, whether for consumption or investment, it is important to understand your budget, needs and holding horizon. For example, when the market sees a short-term spike, the tenure of the property does not really matter especially if you're looking for a quick gain and price momentum is all that matters. In the longer run, however, freehold properties are less risky in terms of returns and volatility.

This is not to say that leasehold properties are always poor cousins to freehold.

In fact, we noted that some new leasehold properties have seen their prices rise faster than new freehold properties. And if rental yields are what you are concerned with, leasehold properties are able to give a better return compared to their freehold counterparts, all things being equal. After all, why would a tenant care if the property was leasehold or freehold?

But again, even for leasehold properties - age is a factor. Once the tenure of a leasehold property goes below 30 years, its value declines sharply as prospective buyers will not be able to withdraw funds from their Central Provident Fund account or secure a loan for the property purchase.

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