



## Monitor

with Tom Holland  
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## Delving into the history books to see property market's future

As usual, everyone is arguing about the Hong Kong property market, and as usual there is a bitter division over the outlook.

With prices now up by around 70 per cent from the depths of the crisis, thanks to the wave of financial liquidity which swept into Hong Kong's asset markets, no one can agree on where prices are likely to go next.

On the one hand, you have the gloomy camp. They point to rising loan-to-deposit ratios at the city's banks and to the recent increases in premiums on new mortgages as evidence that the great tide of liquidity may now be starting to ebb.

Market conditions will only get tighter from here, they argue, forecasting that rising interest rates and declining affordability will inevitably trigger a deep correction in prices over the coming months.

Nonsense, comes the retort from those on the sunny side of the street. They point out that Hong Kong's monetary base is still close to record highs – more than triple its level before the crisis – and insist that the city remains awash with liquidity.

With the interest rates on new mortgages still below 2 per cent, and monthly repayment costs low by historical standards, they argue that powerful economic forces will continue to drive prices higher.

Deciding which side is right is not easy. But Pierre Gave at independent research house GaveKal has dug up an old indicator that might just help.

He has delved into the economic history books to come up with a measure called Marshallian K. Developed by a 19th-century Cambridge University professor called Alfred Marshall, this is the ratio of money supply growth to the growth in nominal gross domestic product (in other words, before adjusting for inflation).

Marshallian K is used to gauge the degree of excess liquidity in an economy. The higher the ratio, the more excess liquidity there is, and the faster asset prices can be expected to rise.

As you can see from the first chart below, this works pretty well as a predictor of Hong Kong property prices.

The red line here represents Marshallian K, while the blue line is the year-on-year change in home prices. As Marshallian K rises, so does the Hong Kong property market. And as Marshallian K falls, so the market runs out of puff.

Ominously, according to Gave, Hong Kong's

Marshallian K measure has started to decline over recent months. That doesn't necessarily mean prices are going to fall in the near term, but it does mean we are unlikely to see the sort of rapid gains in price that buyers have enjoyed over the last couple of years. As Gave puts it: "We would not be surprised to see Hong Kong property face a tougher time over the near future."

When I was a wee lad, my schoolmasters used to tell me that money can't buy happiness. Noting that they really weren't in a position to know, I always used to doubt their certainty.

Now a study by the Asian Development Bank into the rise of China's middle class appears to support my schoolboy scepticism. On the mainland at least it seems that increasing wealth does indeed go hand in hand with greater happiness.

The study surveyed different income groups, asking people whether they were happy or unhappy. Not surprisingly the proportion of

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unhappy people was far greater among the poorest members of society. As the chart below illustrates, more than a third of the urban poor earning less than US\$2 a day said they were unhappy, with their low income and the prospect of unemployment being the biggest causes of complaint.

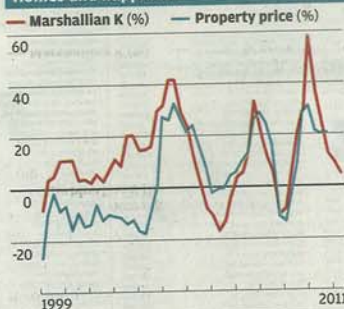
The upper middle class also complained about low income, but gripes about poor health and personal problems were far more common. Poor people, it seems, cannot afford personal problems.

But although wealth and happiness are obviously correlated, the picture isn't completely clear cut. Most of China's very poor live in the countryside, but far fewer country people than city-dwellers admitted being unhappy, and those that did said they were less unhappy.

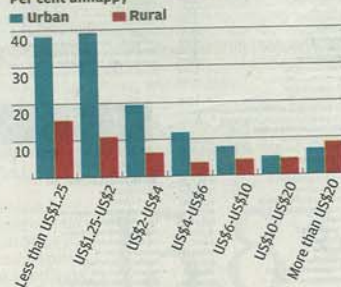
So there is a contradiction here: city people are wealthier, which makes them happier. But living in cities makes people miserable.

Perhaps those old schoolmasters were on to something after all.

Homes and happiness



Per cent unhappy



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SOURCES: GAVEKAL, ADB