

## INDICATOR OF HOUSING AFFORDABILITY IN MALAYSIA

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### ABSTRACT

There are many indicator of housing affordability in Malaysia such as household income, household expenditure, house prices and others. If the income is adequate to pay for a house and other household expenditure, then the individual concerned can be described as having home affordability. The objective of this paper is to discuss the indicator of housing affordability in Malaysia and variables that affect housing affordability amongst the low-income group in Malaysia. From the experience of developed countries, the indicators of housing affordability in Malaysia that affecting housing affordability are mainly house price and housing finance. The finding of this paper conducted on low-cost housing at Kuala Lumpur is there are two main indicator affecting housing affordability i.e. household income and household expenditure. In conclusion, the understanding of indicator of housing affordability in Malaysia are important as input to improve our housing policy.

**Keywords:** *Housing Affordability, Affordable, Indicator.*

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### INTRODUCTION

Housing affordability is not a simple matter to determine and identified. Various approaches and methods have been adopted by earlier researchers in their efforts to determine housing affordability. Housing affordability is the financial capacity to pay off the costs involved to be able to occupy a housing unit. From the earlier studies, there are four main indicators have been identified influencing housing affordability i.e. house price, housing finance (interest rate of housing loan), household income and household expenditure. To determine whether some one could afford to own a house is by looking at their expenses whereby after paying a certain amount and there is still a residual income to purchase other necessary things, then they are considered as capable to own the house (Whitehead, 1991). On the other hand, if they are unable to pay for the monthly housing instalment and have no sufficient money to purchase other necessary things, then they are considered as not capable to own the house.

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## CONCEPT OF HOUSING AFFORDABILITY

The concept of housing affordability refers to the ability of a household to pay for a house. Hulchanski (1995) observed that the housing affordability concept pertains to the amount of income needed to pay for a house and other household expenditures (Hancock, 1993). This concept was used in the United Kingdom and United States in 1960 and 1980 respectively with different policy objectives (Hui, 2001). Affordability is concerned with securing some given standard of housing (or different standards) at a price or a rent, which does not impose, in the eyes of some third party (usually the government) an unreasonable burden on household incomes (Maclennan and Williams, 1990). Bramley (1990) defines housing affordability as the capacity of a household to be able to occupy a housing unit that meets well-established (social sector) norms of adequacy (given household type and size) at a net rent which leaves the household concerned with enough income to live on without falling below some poverty standard. Thus, it can be summarize that the housing affordability can be define as being able pay the mortgage and having residual income to buy other things.

Housing affordability is not easy to determine and measure. Previous researchers have used many approaches and methods in an effort to determine and to define housing affordability. Owning affordability is the financial ability to pay the costs of acquiring a house. In other words, if a family, after paying a certain amount to own a house, still has residual income to buy other items it means that they can afford to own a house (Whitehead, 1991). Household income constitutes the primary source of information needed to determine housing affordability. Household income refers to the combination of both the husband and wife's incomes if both of them are working. If only the husband or wife is working, the income of the individual who is working is considered the household income. There are many methods to measure housing affordability. The familiar methods commonly used by previous researchers are the Price to Income Ratio (PIR) measure, the Housing Expenditure to Income Ratio measure and the Residual Income Measure.

Apart from these measures, the Conventional Measure or Ratio Measure has also been used to determine housing affordability. These measures are based on the premise that only 20% to 30% of earned income is used to pay for the house. If the percentage exceeds this range, it means that the household concerned cannot afford to own a house. Although this measurement is used internationally, it is not a precise method to determine housing affordability as the percentage range cited maybe appropriate only for low-income group who have limited income, but would not significantly affect the financial status of high or medium income groups. However, this measurement is unsatisfactory for low-income group because they will have insufficient residual income no matter how little they spend on housing. While high or medium income groups are likely to have more than adequate residual income even if they spend more than the specified percentage of income on housing.

#### **INDICATOR OF HOUSING AFFORDABILITY**

Previous researchers have different opinions regarding the actual indicator that determine housing affordability. In fact, more than one indicator determines housing affordability. Clark et al. (1994) mentioned that people buy a house due to an increase in household size, adequate disposable income, both spouses being employed, strategic location, the house price, the interest rate and marriage. Many researchers note that the house price variable is the main cause of the housing affordability problem (Peattie, 1987; Linneman and Megbolugbe, 1992; Hancock, 1993; Lau and Li, 2006). In the United States, housing affordability is largely affected by the house price, household income, interest rates, mortgage instruments and underwriting, real property taxes and insurance, expenditure and debt, rent control and housing subsidies (Whitehead, 1991).

The high house price has resulted in the purchasing power for middle-income group in the United States to decrease. This is because they have started offering the house at a good price to the low-income group who want to buy a house because house price have increased consistently with the rise in quality of housing. These rise in house prices has cause a problem especially to low-income group (Linneman and Megbolugbe, 1992). The outcome of the research by Lau and Li (2006) for higher house price based on the low level of housing affordability for the

period 1992 to 2002, found that when Price to Income Ratio (PIR) is high, people in Beijing will not buy houses, in fact they will depend on housing subsidies those given by the government to own the houses. If they do not obtain these housing subsidies, then they would continue as a tenant.

Linneman and Megbolugbe (1992) also said that because of high house price and insufficient income, household are unable to own the house. Further, they said the issue of the housing affordability are also encountered by middle-income group because of high house price and slow rise in income since the year 1970. High house price is because of increase in quality of housing to meet individual taste on better and more comfortable houses. High house price for low-cost houses foment a problem to the low-income group to own the house particularly in urban area. Low-income household and high house price prevent low-income group to buy the house because of their limited finances (Izeogu, 1993).

This rise in house price is because of the increased in property market value which makes a developer increased the house prices. Apart from that, building material costs and labour cost had also caused the price of low-cost houses to increase. All this obviously shows that there were many aspects that contribute to the rise of house prices in a market. Due to the varying house price in the local market, the level of housing affordability also varies as in United States and in United Kingdom. The relationship between house price and household income has an effect in housing affordability. (Weicher, 1977; Anthony, 2000). So, high income household will stay in high cost housing while low-income household will stay in low-cost housing.

This means that housing affordability is dependable on income level (Whitehead, 1991). Any strategy to control house price and efforts to promote low-income group to own a house required attention by all parties and this was done by the Ministry of Housing and Government of Malaysia in discussions on ways to tackle the problems of the rise in house prices since 1995. These efforts were very important in handling the housing problems in Malaysia (Mohd. Razali, 2001). High house price and competition in housing supply for low quality housing foment a problem to the low-income group to own a low-cost house (Linneman and Megbolugbe, 1992). The high house price has caused the people in United States to

face a problem to purchase the house. Furthermore, if the household do not give their item and information of their real income and enhance the taste for quality housing, they must pay more to own a house. This situation has caused them to face a problem to own a house (Linneman And Megbolugbe, 1992).

Apart from high house price, interest rate of housing loan also affects the ability to own a house. This was stated in the research finding by Weicher (1977) study over interest rate percentage of housing loan where the increase of percentage in interest rate of housing loan from 6% in the year 1965 to 9% in the year 1975 and 1976, had caused people in United States to face difficulties to own a house. Weicher (1977) mentioned that individuals face a housing affordability problem when they have to pay high interest rates on their mortgages. Other than that, it has also increased other costs such as maintenance cost and home ownership cost. It means that, interest rate percentage of housing loan influence the ability to own a house.

The other indicator that influences housing affordability is household income (Deurloo et al., 1988; Moore, 1991; Clark et al., 1997; Norazmawati, 2007). The *National Association of Realtors* (1990) reported that 93 percent of house buyers use their income to buy a house. The calculation of household income varies. For example for married household with or without children, their income will be calculated from the husband and wife income if both of them are working.

Beyer (1958) pointed that household income is the main indicator affecting the decision to buy a house. This is because of the household income being influenced by work opportunity and the type of work. If only husband or wife is working, then only the stated income are taken into account. For household with live-in adult children, then only the husband and wife income are taken into account as household income. Children income are not taken into account as household income because the children would leave home at one time and will not stay long with their parents especially after they married. Income is the main indicator in a decision to own a house especially for married couple and family (Clark et al., 1997). Gyourko, Linneman and Wachter (1999) also agreed with this factor that determined a decision to own a house.

The next indicators that effect housing affordability are household expenditure. Hancock (1993) said that to determine the housing affordability, all information about their household expenditure such as housing monthly instalment and other expenditures that are required, must be informed to make easier calculation. The household can afford to own a house if his income is adequate to pay for the monthly instalment and he is able to purchase other necessities things. Maclennan and Williams (1990) and Bramley (1990) acknowledged that information about other expenses must be informed to determine housing affordability. Hulchanski (1995) study about housing affordability in the 19th century from the aspect of household expenditure also said that 'one week's pay for one month's rent'. This means that household can afford to pay the monthly instalment from only about a quarter of their income. If their spending exceeds the ratio to pay for the monthly instalment, it means that they can not afford to own a house.

United States and Canada always use the ratio of housing expenditure with income measure to define the capability of a person to pay for a monthly housing instalment and to show their housing affordability (Hulchanski, 1995). Whitehead (1991) and Hancock (1993) also said that housing affordability included housing expenditure and their income. They decided a standard must be used on income distribution for housing. The standard is the absolute amount of residual income after buying the house. It determined the level the household can pay for a house price and their affordability to buy other necessary things. Problem of housing affordability exist if household spending is more than certain amount from their income, although each individual can spend independently with their choice (Whitehead, 1991). Therefore, the ratio of housing expenditure with income measure effect housing affordability. Definition of housing affordability from conventional aspect is a percentage of income earned to pay for a monthly housing instalment. Housing expenditure which exceeded 30 percent from household income shows they have a housing affordability problem<sup>2</sup>.

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<sup>2</sup> Guideline 25 percent which was established by International Law of Low Cost Housing in the year 1969 has been added to 30 percent in the year 1981. Others analyses including from William Reeder, Office of Policy Development and Research, Housing Department and Urban Development in United States also use 25 percent and 35 percent and pointed out that this percentage need to be maintained (Linneman And Megbolugbe, 1992).

Home ownership affordability made by household. It means that, the household decides whether they can afford to buy a house base on their income and wealth, and will attempt to maximize income to buy a house (Bourassa, 1996). They will attempt to make sure that their income is sufficient to pay for a housing cost and to buy other housing expenditure because housing is a basic need.

Nevertheless, there are certain indicators that can help individuals to buy a house. For example, housing subsidies from governments help people to buy a house (Thalman, 1999; Grigsby and Bourassa, 2003). Research by Whitehead (1991) into the requirement concept and housing affordability in the United Kingdom revealed that low-income groups who were aided by government housing subsidies were able to purchase houses. Chaplin and Freeman (1999) noted that with housing subsidies, tenants could afford to rent a house. Within the Malaysian context, the provision of a RM3,000 discounts on a low-cost housing unit has made house prices more affordable.

### **HOUSING OWNERSHIP**

Norazmawati (2007) in her research carried out the studies on housing affordability mentioned that 6 factors affect housing affordability include household income, household expenditure and the type of occupation, education levels, working household and monthly payment for housing. The research data was obtained through face-to-face interviews conducted in a low-cost housing scheme in Kuala Lumpur. The interview was based on household leader background, others households, family income, family housing expenditure and information about buying a house. 300 respondents were selected utilizing the stratified random sampling method. The respondent consisted of low wage earners who bought their house in year 1987 to 1999. At that time, the house price was RM22,000 to RM25,000 per unit.

Two main indicators affecting housing affordability are household income and household expenditure. This is because from household income and household expenditure, we can measure either some one are afforded to own a house or not. If they spend more then their income for houses and no have sufficient income to buy

other necessities things, mean that they not afford to own a house and subsequently.

### Household Income

Table 1 show that 59.2% of the low-income group has an income of between RM751 to RM1,500 per month. This situation shows that most respondents in the study area have low income. Nevertheless, there were also 19.4% low-income group having an income of less than RM750 per month which is the lowest income. While 18.4% have an income of more then RM1,500 per month.

Table 1: Household Income

Household Income (RM)	Respondents	Percentage
Less then RM750	60	19.4
RM751-RM1,500	183	59.2
More then RM1,500	57	18.4
Total of Respondents	300	97.1
Total of respondents can't detect in a system	9	2.9
<b>TOTAL OF RESPONDENTS</b>	<b>309</b>	<b>100.0</b>

### Household Expenditure

Table 2 shows that the majority of the low-income group i.e.; 59.5% spend RM751 to RM1, 500 per month. It shows that low-income group whose income is between RM751 to RM1,500 per month spend all their income for household expenditure. However about 24.6% of the low-income group spend less than RM750 per month and only 12.9% spend more than RM1,500 per month. Generally the total expenditure that was spent by the low-income group is in line with the total income receivable.



Table 2: Household Expenditure

<b>Household Expenditure (RM)</b>	<b>Respondents</b>	<b>Percentage</b>
Less than RM750	76	24.6
RM751-RM1,500	184	59.5
More than RM1,500	40	12.9
Total of Respondents	300	97.1
Total of respondents can't detect in a system	9	2.9
<b>TOTAL OF RESPONDENTS</b>	<b>309</b>	<b>100.0</b>

## CONCLUSION

Housing affordability is affected by indicator such as house price, interest rate of housing loan, household income and household expenditure. The finding of this paper conducted on low-cost housing at Kuala Lumpur is there are two main indicator affecting housing affordability i.e. household income and household expenditure. It means that, to make sure that each income group can afford to own a house offered in the market, these indicators should be taken into consideration by all parties especially at an early stage of the housing development. There were six variables affecting the affordability of low-incomes groups to own a low-cost house in Kuala Lumpur i.e. household income, household expenditure, types of work, level of education, working household and housing instalment. Apart from that, by doing a proper study we can make sure that there are no surplus in the housing supply and avoid having problems such as abandoned housing prospects.

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