

# FACTORS INFLUENCING HOUSING AFFORDABILITY STRESS VERSUS ALTERNATIVE FINANCING SCHEMES FOR HOME BUYERS IN KLANG VALLEY MALAYSIA

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**ABSTRACT. Objective:** The massive uncontrolled development of residential properties especially in the Klang valley has resulted in a supply glut. According to economic theory, when supply exceeds demand, the price product price should decrease. However, due to the increased cost of construction materials and labour, house prices have not decreased. Consequently many in the Klang valley cannot afford to buy residential property causing financial stress to families with a household income below the average level. At the 19<sup>th</sup> National Housing and Property Summit 2016, Tan Sri Noh Omar the then Minister for Urban Wellbeing, Housing and Local Government Housing, announced an alternative home financing scheme offered through eligible housing developers licensed under the Money Lenders Act 1951 and Pawnbrokers Act 1972. The paper therefore explores factors influencing housing affordability stress and alternative schemes that could be offered by developers without unduly burdening the home buyer and ensuring a balance between the interests of the public and the developer.

**Methodology:** The writers apply the method of documentary studies, historical archives, public record and interview to arrive at the findings.

**Results:** The loan tenure would be between 10 to 20 years with the interest rate being fixed at 12% per annum for borrowers with collateral, and 18% for those without. It is noted that the section of public applying for such a scheme would be those whose monthly income and expenditure disqualify them from a 100% conventional loan. Consequently, one of the immediate issues for the borrower would be coping with the very high interest rates under this scheme. If a borrower were to apply under this scheme as a top-up to a conventional bank loan, there would be two monthly loan repayments to manage. Further if the second loan

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is without security he would be charged 18% interest leading to a real danger of potential insolvency. Further, no eligibility criteria has been set for developers to qualify for a licence. There is also the issue of a conflict of interest when a developer also acts as a financier.

**Implication:** This research presents a conceptually yet empirically supported framework to describe the factors influencing housing affordability stress and alternative schemes that could be offered by developers by taking into consideration of the legal impact when the developers act as home loan financier to the borrowers. The study is particularly useful for housing industry by identifying the legal implication when the developers act as home loan financier to the borrowers. This paper gives valuable reference to law markers to consider whether this alternative is one of the solutions to solve housing affordability stress in Klang Valley area.

**Keywords:** *Alternative schemes, developer, housing affordability stress, Klang Valley.*

**JEL classification:** H31

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## INTRODUCTION

A home provides man with a sense of security and belonging where he can raise a family and become a part of a community and society. It takes on a central role as a haven of peace, love strength and psychological support. It is a sanctuary where one can retire to, for rest and privacy. Home ownership therefore is an important target for achievement and also represents a considerable economic investment. In fact, in many countries, private homeownership is given priority as otherwise the cost of housing the homeless would fall on the State. In recent years affordable housing has become an increasingly important social issue as the gap between available housing and the financial capacity of buyers widens.

The massive uncontrolled development of residential properties especially in the Klang valley resulted in a housing over supply. However, this situation is contrary to economic theory, which states that when supply exceeds demand, the price of the product should decrease. In reality, when the supply of the houses increase, prices have not dropped. This is attributed by increased cost construction materials and labour, costs leading to increased house prices. Consequently, not everyone in Klang valley can afford to buy a house. This, has in turn caused financial stress to families whose household income is below the average level. In other words, it means that there is imbalance allocation between the number of housing and population in Klang valley.

There is no statutory definition for the term 'affordable housing'. Wendy Wilson and Cassie Barton (2018), define it as "what is judged to be affordable to a particular household or group by analysis of housing costs, income levels and other factors". Another definition is "housing which is sufficient in quality and location, and is not so costly that it prevents its occupants from satisfying other basic living needs". The McKinsey Global Institute in 2014 gave a broader definition in terms of not only to affordability, but extends to 'housing which meets minimum decent standards of living (basic amenities, floor-space, sanitation, without structural building defects) and is not located too far away from centres of employment, usually one hour away' The United Nations Declaration of Human Rights recognises housing as a basic human right in Article 25 on 'Right to an adequate standard of living':

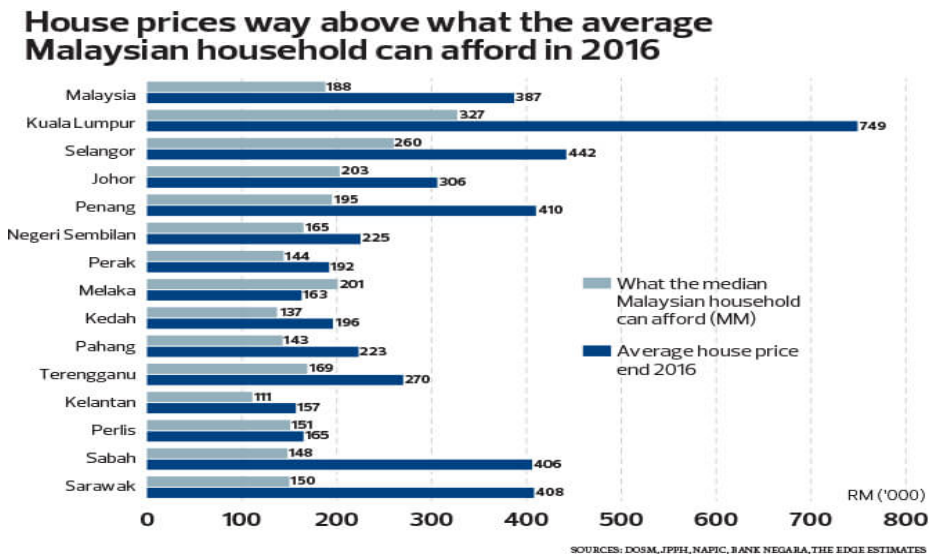
*"Everyone has the standard of living adequate for the health and well-being of himself and of his family, including food, clothing, housing and medical care and necessary social services ..."*

According to Dr. Suraya Ismail et al, 'affordable housing' would be achieved when the 'median price for the housing market is three times the gross annual household income'. BNM recommends that the monthly payment for the house should not be more than 30% of the income. Anything more than that would be a burden to the household. Meanwhile, housing affordability can be defined as a person's ability and capacity to save their income towards both housing costs as well as other consumption (Anirban et al., 2006). Based on Bujang (2006) and United States Department of Housing and Urban Development, when a family has to allocate more than 30 percent of their income just to pay for the cost of

housing, there is a cost burden and they will face difficulties in providing for basic needs such as food, clothing, transportation and medical care. Rawley and Ong (2012) concluded that the housing affordability stress is the financial hardship faced by owners of housing. Thus, if a household spends more than 30 percent of the income for housing, this household would be a suitable candidate for measuring the level of housing affordability.

According to the survey done by the Household Income and Basic Amenities Survey 2016, it shows that Malaysia's median monthly income continued to grow from 2014 until 2016 but in a small pace.

Malaysia's median monthly household income grew from RM4,585 in 2014 to RM5,228 in 2016, up 6.6% per year at nominal value and 4.4% in real terms, according to the Department of Statistics Malaysia's (DoSM) report on the 2016 Household Income and Basic Amenities Survey. The bottom 40% (B40) households can only afford homes priced up to RM108,000 each while the middle 40% (M40) households can afford up to RM225,900, based on the B40 and M40's median monthly household income of RM3,000 and RM6,275 respectively. The Graph 1 below shows the house prices way above what the average Malaysian household can afford in 2016.



Source: DOSM, JPPH, NAPIC, Bank Negara Malaysia.

**Graph 1.** House prices way above what the average Malaysian household can afford in 2016.

The residential property market in Malaysia saw a general decline in 2016 due to various factors including high home loan rejection rates by Banks.<sup>3</sup> Bank Negara Malaysia (BNM) introduced stricter lending guidelines with mortgage eligibility assessments based on net income.<sup>4</sup> BNM in its Financial Stability and Payment Systems Report (2016) stated that its Financial Services Committee (FSC) would continue monitoring all finance providers for potential unintended consequences.<sup>5</sup> Malaysia already has a household debt of 89.1% or RM1.03 trillion, one of the highest in the region, which has led BNM to maintain its prudent measures.<sup>6</sup> These are specifically: “(i) curb excessive speculative activity in the housing market; and (ii) deter over-borrowing”. The maximum loan-to-value ratio (LTV) of 70% introduced in 2010 is imposed only on borrowers with three or more outstanding housing loans.<sup>7</sup> However it noted that risks from household lending currently remained stable as households generally reduced borrowings in line with loan affordability.<sup>8</sup>

The National Property Information Centre statistics show that less than 30% of new housing launches between 2015 and 2016 were for houses priced at less than RM250,000, compared to 70% during 2008 – 2009.<sup>9</sup> The number of unsold properties is due to the mismatch

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<sup>3</sup> Global Property Guide Malaysia, ‘Subdued house price rises in Malaysia’(14 Feb. 2017), available at <<https://www.globalpropertyguide.com/Asia/Malaysia/Price-History>> accessed on 24 Feb. 2018.

<sup>4</sup> *Ibid.*

<sup>5</sup> Bank Negara Malaysia, ‘Managing Risks Arising From Household Indebtedness’ The Financial Stability and Payment Systems Report (2016)12, available at <[http://www.bnm.gov.my/files/publication/fsp/en/2016/fs2016\\_book.pdf](http://www.bnm.gov.my/files/publication/fsp/en/2016/fs2016_book.pdf)> accessed on 24 Feb. 2018.

<sup>6</sup> Emmanuel Surendra, ‘The New PR1MA Financing Plan: A Step Up Or Step Down?’ iMoney.my Learning Centre (15 Feb.2017), available at <<https://www.imoney.my/articles/pr1ma-step-up-end-financing-home-malaysia>> accessed on 24 Feb. 2018.

<sup>7</sup> Lim Le Sze, ‘Debunking the Myth: Property Measures Have Led to Higher Loan Rejection Rates’ BNM Quarterly Bulletin, 1st. Quarter, 33, available at <[https://www.bnm.gov.my/files/publication/qb/2017/Q1/p5\\_ba1.pdf](https://www.bnm.gov.my/files/publication/qb/2017/Q1/p5_ba1.pdf)> accessed 26 Feb. 2018.

<sup>8</sup> *Supra* n 4.

<sup>9</sup> Ng Min Shin, ‘BNM defends strict housing loans criteria’ (19 July 2017) *Malaysian Reserve*, available at <<https://themalaysianreserve.com/2017/07/19/bnm-defends-strict-housing-loans-criteria/>> accessed on 24 Feb. 2018.

between the prices of new launches and households' affordability.<sup>10</sup> Generally, first time home buyers, especially the young and those in the lower income group experience difficulties in obtaining home loans. In response thereto, the Malaysian government introduced the Malaysia People's Housing (PR1MA) with various fiscal incentives.<sup>11</sup> However there were issues of availability and location. Subsequently, at the 19th National Housing & Property Summit 2016 on 8 September, Tan Sri Noh Omar the then Minister for Urban Wellbeing, Housing and Local Government Housing (the Ministry), announced a novel scheme enabling housing developers to provide home buyers with financing for their home loans.<sup>12</sup> The requisite licence would be issued under the Money Lenders Act 1951 and Pawnbrokers Act 1972 which do not come under the purview of Bank Negara Malaysia (BNM).<sup>13</sup> The objective is to assist home buyers who are unable to secure home financing to obtain up to 100% financing or just a top-up to assist with their differential financing problems. The loan tenure would be between 10 to 20 years while the interest rate would be capped at 12% per annum for borrowers with collateral, and 18% for those without.<sup>14</sup>

Currently 54 property developers in Peninsular Malaysia have money-lending licences issued by the Ministry, to provide bridging loans to secure end financing especially to first time home buyers.<sup>15</sup> However eligibility is not automatic as the developers also perform a risk assessment of the potential borrower. According to the Real Estate and Housing Developers' Association Malaysia, developers would be

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<sup>10</sup> Cheah Su Ling, Stefanie Almeida, Muhamad Shukri, Lim Le Sze, *Imbalances in the Property Market*, *BNM Quarterly Review* (Third Quarter 2017) 26, available at <[https://www.bnm.gov.my/files/publication/qb/2017/Q3/p3\\_ba2.pdf](https://www.bnm.gov.my/files/publication/qb/2017/Q3/p3_ba2.pdf)> accessed on 24 Feb. 2018.

<sup>11</sup> See n 1.

<sup>12</sup> Shawn Ng, 'Update:Housing Ministry to issue money lending licences to property developers' *Malaysia Property News* (8 Sept. 2016), available at <<https://www.edgeprop.my/content/877948/housing-ministry-issue-money-lending-licences-property-developers>> accessed on 24 Feb. 2018.

<sup>13</sup> *Ibid.*

<sup>14</sup> *Ibid.*

<sup>15</sup> The Malaysian Reserve, '54 developers have money-lending licences' (3 April 2017), available at <<https://themalaysianreserve.com/2017/04/03/54-developers-have-money-lending-licences/>> accessed on 24 Feb. 2018.

willing to provide financing of between 10% and 15% of property prices for units priced RM500,000 and below, for first-and second-time home buyers.<sup>16</sup>

The big difference between the affordability and the house price has forced them to live in a low quality and uncomfortable residents, as well as lack of amenities hence putting stress on housing affordability.

## **RESEARCH QUESTIONS**

This paper represents the first stage of research on the topic and consequently is a literature review that examines four research questions related to factors influencing housing affordability stress in Klang Valley area and subsequently to examine the alternative financing schemes for home buyers to overcome the housing affordability stress. What are the:

- (i) factors influencing housing affordability stress?
- (ii) currently available home loan financing schemes?
- (iii) eligibility criteria and problems encountered in qualifying for home loans.
- (iv) resulting legal financial implications?
- (v) possible alternative home financing schemes?

## **RESEARCH METHODOLOGY**

The study adopts a qualitative method based on documentary studies, historical archives and public records to arrive at the findings. Interviews have also been conducted with selected households in Klang Valley area. The data reveals that there are three major factors influencing housing affordability stress in Klang Valley area and particularly in Petaling Jaya, Subang Jaya and Jalan Old Klang, namely economy factors, property market and demography.

Structured interview method was used in the research to ten interviewers. Questions are prepared before hand and the categories of answers/responses predetermined. Open ended questions often used and each respondent received same questions with same methods. Selection criteria and results were as follows:

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<sup>16</sup> *Ibid.*

No.	Gender	Age	Monthly income (RM)	Do you own at least a house in Klang Valley area? If not, please state the reason.
1	M	22	2500	No. Not afford to buy.
2	M	25	3000	No. Staying with family.
3	M	24	2800	No. Not afford to buy.
4	M	32	4200	Yes, apartment with 750 square feet.
5	M	45	6500	Yes, single storey house.
6	F	35	3500	No. Not afford to buy.
7	F	48	3800	No. Staying with family.
8	F	21	1800	No. Not afford to buy.
9	F	38	4500	No. Not afford to buy.
10	F	37	4000	No. Not afford to buy.

*Source: Interview conducted by author between 10 respondents in Klang Valley conducted from June 2018 until September 2018.*

For the abovesaid result, it shows that most of the people staying in Klang valley area are not afford to buy the house due to insufficient income and the price of the properties is too high.

## **FINDINGS**

### ***Economy***

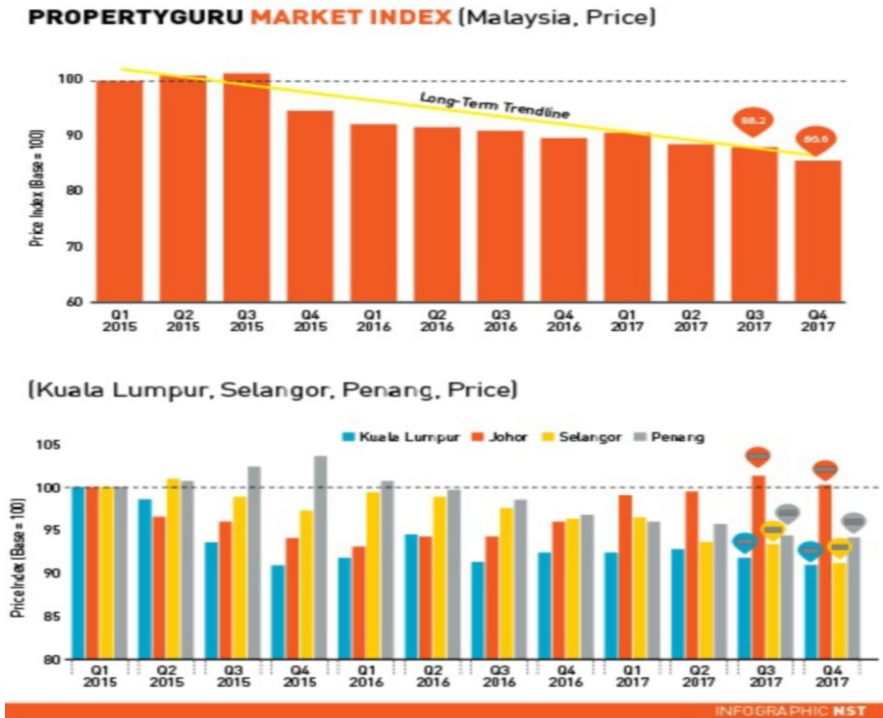
Most of the households are unable to own a house because of high house price. Most of the stratified properties or landed properties start from RM300,000 minimum, (especially in Klang valley area) and above. An additional factors to be budgeted for in the housing cost are the high legal professional fee and stamp duty for the sale and purchase and loan transactions. The higher the price of the property, the higher the professional fee according to the Solicitors' Remuneration Order 2005<sup>17</sup> and stamp duty pursuant to Stamp Act 1949.<sup>18</sup> Renovation costs is another burden for most of the households. Graph 2 belows show that the house pricing in Kuala Lumpur, Selangor and Penang area.

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<sup>17</sup> Legal Profession Act 1976 (Act 166), Rules & Orders.

<sup>18</sup> A378.





Source: <https://www.nst.com.my/property/2018/04/353364/downtrend-property-prices>

**Graph 2.** The house pricing in Kuala Lumpur, Selangor and Penang area.

CBRE/WTW managing director Foo Gee Jen said, “In January 2018, that the Malaysian property market is expected to be “flattish” this year”. Speaking at the 2018 Asia Pacific Real Estate Market Outlook briefing, he said property developers are restrategising their products to cater to demand.

According to Foo, “the price range that has been deemed acceptable by the public within the Klang Valley is RM500,000 for landed property. For outside the Klang Valley, it is RM300,000 to RM350,000”.<sup>19</sup>

<sup>19</sup> Sharen Kaur, Downtrend in property price (05.04.2018), available at <<https://www.nst.com.my/property/2018/04/353364/downtrend-property-prices>> accessed on 09 October 2018.

On the other hand, according to PropertyGuru, “real estate prices in Malaysia continued to decline in the fourth quarter of last year as the market corrected itself amid a complex scenario of growing oversupply in certain segments and a prevailing lack of consumer affordability”. The PropertyGuru Market Index (PMI), which tracks the asking prices of residential properties in Malaysia, showed a decrease of 1.6 per cent for the quarter compared with the previous quarter.<sup>20</sup>

### ***Property Market***

A contributory factor to high property prices in the Klang valley is foreign buyers who bought the properties for own residential or investment. This has led to speculation in the property market which has resulted in the current mismatch between the demand and supply in the property market as Malaysians are unable to afford the high prices.

### ***Demography***

Another contributory factor to housing affordability stress is the mismatch between the education level of the households and income. This applies to most of the B40 group of households. Meanwhile, the factor that increase the demand for houses would be due to increasing growth in population in Malaysia (Gin & Sandy, 1994). Growth in population would represent the changes of demographic. Buyers’ behavior is likely to be influenced by this factor (Schuler & Adair, 2003; Nayyab et al, 2011), especially when they are in the decision making process in selecting the right unit for their home (Majid, 2010; Lutfi, 2010; Jain & Mandot, 2012).

## **CURRENT HOME LOAN FINANCING SCHEMES**

Bank Negara Malaysia (BNM) in its *Financial Stability and Payment Systems Report 2017* stated that, “The rejection rate of housing applications has declined to below the average rate of about a quarter of all cases”. The report stated that the rejection rate of housing applications currently

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<sup>20</sup> *Ibid.*

stands at 23.1%, below the 2012-2016 average of 26.1%.<sup>21</sup> Half of household debt for Malaysian is housing loan and this scenario reflects affordability issues among the Malaysian.

There are a few traditional home financing options available in Malaysia. These range from conventional bank loans, Islamic home loans, government loans and withdrawals from the Employees Provident Fund (EPF). These are considered below.

### ***My First Home Scheme (SRP)***

This is a government initiative for home buyers who qualify under PRIMA homes eligibility criteria.<sup>22</sup> It offers:

- “100% financing, including the first 10% down payment on a house;
- Single borrower gross income not exceeding RM5,000 per month and joint borrowers’ gross income not exceeding RM10,000 per month (based on gross maximum income of RM5,000 per month per borrower);
- Property value between RM100,000 and RM400,000;
- Must occupy property upon purchase;
- Financing tenure not exceeding 40 years, or not more than 65 years old;
- Installment payable via monthly salary deduction;
- Compulsory fire insurance / Takaful and
- Amortising facility only, without re-drawable features
- Those blacklisted through CCRIS are not eligible for the scheme”.

The scheme is offered in collaboration with BNM, EPF and four local banks, namely Maybank, CIMB, RHB, and AmBank. They provide stepped-up financing with fixed instalment for the first five years of the loan. Thus, for the first five years, borrowers will only be paying the

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<sup>21</sup> Natalie Khoo, Rejection rate of housing loan applications drops below average, says Bank Negara (28.03.2018), available at <<http://www.theedgemarkets.com/article/rejection-rate-housing-loan-applications-drops-below-average-says-bank-negara>> accessed on 09 October 2018.

<sup>22</sup> Starproperty.my, ‘Different financing alternatives for your housing loan’, available at <<http://www.thesundaily.my/news/2013056>> accessed on 24 Feb. 2018.

interest on the loan. Although this would ease their initial financial burden, in reality it is only from the sixth year onwards that they will be repaying the principal sum with interest. The banks collect on their interest income upfront and in the case of a long term 35 -40 year loan the borrower would have paid almost double or more than the cost of the house.<sup>23</sup> So the only advantage is that, those who meet the less onerous eligibility criteria stand to receive 100% financing.

EPF also permits withdrawal from Account 2 for PR1MA home instalment up to retirement or end of tenure.<sup>24</sup> However these come with certain restrictions. All other permitted withdrawals under Account 2 example for medical and educational purposes, withdrawal at age 50 and for Hajj purposes will no be suspended until the PR1MA loan is fully settled. With an age cap at 60 years the scheme ostensibly targets the young. These new entrants to the employment market and those in the lower income group would not have accumulated much by way of EPF savings putting them at real risk should they withdraw their modest EPF savings. So contributors will have to weigh the implications carefully before availing themselves of the EPF withdrawal facility.

### ***EPF withdrawal criteria***

The facility for withdrawal of savings from Account 2 to either reduce or redeem housing loan balance is only available for financial institutions approved by the EPF. Further, the contributory should be below the age of 55 years at time of application and must have a minimum of RM500 in Account 2.<sup>25</sup> A degree of flexibility is given in that it is also available for a joint purchase with immediate family members. Further it does not discriminate between Malaysian or non-Malaysian contributories.<sup>26</sup>

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<sup>23</sup> Everst Home Mortgage, 'The Pros and Cons of Mortgage, available at <Amortization' <http://www.everesthomemortgage.com/mortgage-amortization/>> accessed on 24 Feb. 2018.

<sup>24</sup> *Ibid.*

<sup>25</sup> EPF Reduce/ Redeem Housing Loan Balance, available at <[http://www.kwsp.gov.my/portal/documents/10180/153718/REDUCEREDEEM\\_HOUSING\\_LOAN\\_BALANCE\\_WITHDRAWAL-final\\_19.6.2017\\_EN\\_21.06.2017.pdf](http://www.kwsp.gov.my/portal/documents/10180/153718/REDUCEREDEEM_HOUSING_LOAN_BALANCE_WITHDRAWAL-final_19.6.2017_EN_21.06.2017.pdf)> accessed on 24 Feb. 2018.

<sup>26</sup> *Ibid.*

## **Bank Loans**

Most commercial banks offer various home loan packages including flexible home loan permitting the borrower to pay off the loan earlier and reduce the interest payable by depositing the entire salary in the home financing account. Withdrawals from the excess payment are permitted anytime without charges.<sup>27</sup> Monthly repayments are lowered with longer tenures which invariably increase the total cost at the end of the term. Additionally, borrowers will be continuously in debt with for their entire working life with household debt only increasing with growing requirements over time eg. for educational and medical needs.

As for eligibility criteria, all financial institutions Follow BNM's guidelines namely:

- "70% loan margin on the third property onwards;
- Nett Financing i.e. after deducting free packages given by developer;
- Abolishment of Developer Interest Bearing Scheme (DIBS) i.e. no interest payable on loans while property is under construction;
- Loan approval based on net income instead of gross income;
- Loan tenure reduced to a maximum of 35 years and
- A Maximum 10-year tenure for personal financing"<sup>28</sup>

Banks will refer to BNM's Central Credit Reference Information System (CCRIS) to verify the credit worthiness and risk to the bank of the applicant. Generally, eligibility for a loan depends on a number of factors such as: the applicant's income and monthly expenditure, employment i.e. salaried or self-employed, credit reports, residence status i.e. whether a Malaysian or an expatriate, the project status i.e. whether the construction is in the bank's approved list, the cost of the property and the available financing margin. Careful credit assessment and prudent lending is necessary to mitigate loan default and or a fall in the financial value of the asset secured.<sup>29</sup>

<sup>27</sup> HSBC Bank Bhd. Malaysia, 'Property Financing', available at <<https://www.hsbc.com.my/1/2/personal-banking/home-loans/buying-your-first-home>> accessed on 24 Feb. 2018.

<sup>28</sup> Michael Yeoh, 'Bank Negara Malaysia's Lending Policies: How Do They Affect You?' (4 May 2017) iProperty.com, available at <<https://www.iproperty.com.my/guides/bank-negara-malaysia-s-lending-policies-how-do-they-affect-you/>> accessed on 24 Feb. 2018.

<sup>29</sup> Catherine Soke Fun Ho and Nurul Izza Yusoff (2009), "A preliminary Study of Credit Risk Management Strategies of Selected Financial Institutions in Malaysia", 28 *Jurnal Pengurusan* 45-65.

## ***Government loans***

Government servants including employees of Statutory bodies and Local Authorities are eligible for any of seven types of housing loans.<sup>30</sup> The amount of loan approved is based on the loan eligibility, house price, amount applied, outstanding bank loan and market value, whichever is the lower.<sup>31</sup> The interest on government loans has also been fixed at 4%, much lower than a bank loan and does not fluctuate making it attractive and affordable.

## ***Islamic Home Loans /Islamic Housing Finance***

### *Why Islamic Home Loans/Islamic Housing Finance*

An alternative scheme is the Islamic home financing. According to Kuwait Finance House (KFH Research 2010)<sup>32</sup> there has been increasing growth of Islamic home finance from RM6.8 billion as at end 2001 to RM23.3 as at end of November 2009. Its attractiveness lies in the interest free and flat rate loans.<sup>33</sup>

### *What are the Instruments in Islamic Housing Finance?*

The procedure involves the Bank purchasing from the applicant through a 'Property Purchase Agreement' for the amount of the approved 'loan' and selling back to the applicant through a 'Property Sale Agreement'

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<sup>30</sup> Jabatan Penilaian dan Pinjaman Harta, 'Types of Housing Loan'. Seven types of housing loan including but not limited to purchase of a completed house or residential parcel, construction of a house on land belonging to the applicant, purchase of a house or a residential parcel under construction, purchase of land for the purpose of constructing a house, redemption of an existing loan from a bank or financial institution, construction of a house on the applicant's land which has been purchased by a government housing loan and renovation of a house, available at <[https://www.jpvh.gov.my/V2/pdf/Government\\_Housing\\_Loan.pdf](https://www.jpvh.gov.my/V2/pdf/Government_Housing_Loan.pdf)> accessed on 24 Feb. 2018.

<sup>31</sup> *Ibid.*

<sup>32</sup> KFH Research (2010), "Islamic finance research", Kuwait Finance House, available at <[www.mifc.com/index.php?ch%4151&pg%4735&ac%4402&bb%4670](http://www.mifc.com/index.php?ch%4151&pg%4735&ac%4402&bb%4670)>, assessed on 24 Feb. 2018.

<sup>33</sup> Bassir, Nur Fadhli; Zakaria, Zarina; Hasan, Haslida Abu; Alfian, Ervina, (2014), "Factors Influencing the Adoption of Islamic Home Financing in Malaysia, Transformations in Business & Economics". 2014, Vol. 13 Issue 1, p155-174. 20p.

at the end of the agreed tenure at a predetermined price. These instruments are based on the concept of Islamic contracts namely, murabahah, ijara wa iqtina, bay bithaman ajil (deferred payment sale (BBA)) and musharakah mutanaqisah (diminishing musharakah (MM)). A brief descriptions of these instruments is given in Table 1 below.

**Table 1.** Instruments in Islamic Housing Finance

<b>Property own by</b>	Customer	Customer	Financier/Lessor	Both the financier and customer own the property according initial share
<b>Type of property</b>	Completed	Completed and Under construction	Completed	Completed and Under Construction
<b>Liability held by</b>	Financier	Customer	Financier/Lessor	Both the financier and customer held the liability according to share
<b>Monthly payment fixed or variable</b>	Fixed	Fixed/Stepped-up	Variable	Variable
<b>Is early sale allowed</b>	Yes, and the customer entitles to the gains from the difference between purchase and sale price	Yes, and the customer entitles to the gains from the difference between purchase and sale price	Yes and the customer entitles to the gains from the difference between the principal and sale price	Yes and the customer entitles to the gains from the difference between principal and sale price according to the portion of share owned.
<b>Is home improvement allowed</b>	Yes	Yes	Yes	Yes
<b>Is early payment allowed</b>	No	No	Yes	Yes
<b>Is securitization suitable</b>	No	No	Yes	Yes
<b>Are taxes and insurance included</b>	Not included in the purchase price	Normally insurance/takaful included in the purchase price	Typically included in the cost of lease	Typically included in the cost of lease
<b>Bank Risk (based on the length of ownership by the bank)</b>	Low risk	Low risk	High risk	High risk

Source: HANAFL, HANIRA, BINTI (2012) *Critical Perspectives on Musharakah Mutanaqisah Home Financing in Malaysia: Exploring Legal, Regulative and Financial Challenges*, Durham theses, Durham University. Available at Durham E-Theses Online:

The controversial issues of profit and interest raised in *Arab-Malaysian Finance Bhd v Taman Ihsan Jaya Sdn Bhd & Ors; Koperasi Seri Kota Bukit Cheraka Bhd* (Third Party),<sup>34</sup> was overcome with the Musharakah Mutanaqisah (MM) house financing concept where the customer and Islamic banking institution jointly acquire and own the property. In practice, it has been argued that MM concept is superior to the BBA as MM is seen to better promote the welfare of the people because the outstanding balance of financing at any point in time will not exceed the original price of the asset.<sup>35</sup>

<sup>34</sup> [2009] 1 CLJ 419.

<sup>35</sup> *Supra* n 29.

## **LEGAL AND FINANCIAL IMPLICATIONS OF DEVELOPERS AS FINANCIERS**

The scheme to permit developers to become licensed money lenders under the Money Lenders Act 1951 and the Pawnbrokers Act 1972 raises numerous concerns. First, no criteria have been given for the scheme.<sup>36</sup> Secondly, will developers who themselves need project financing be able to offer loans to homebuyers with or without security? If it is without security, what will be the collateral for the developer? It is to be noted that developers will also have their own conditions and undertake a risk assessment of the potential borrower. What would be the probability of a developer granting finance to those who have been rejected by banks? The scheme places the developer in a position of conflict of interest vis-à-vis the homebuyer. Moreover, will the homebuyer who does not qualify for a bank loan be able to afford the exorbitant interest rates of between 12% - 18%? How long will a borrower be able to sustain such high repayment? How will developers deal with loan defaulters and how long could they endure non-performing loans? Ultimately it looks like a recipe for insolvency and prove to be counter-productive.<sup>37</sup>

In practice, developers who have responded to the scheme have done so under a separate subsidiary financing company.<sup>38</sup> Even then it could only work with the 'build and sell' projects, not the usual 'sell and build' concept. According to Land & General Bhd (L&G), the scheme is too costly for most developers to implement besides not being experienced in the moneylending business.

### **ALTERNATIVES**

#### ***My Deposit scheme.***

First House Deposit Financial Scheme (MyDeposit) was introduced by the Ministry on 6<sup>th</sup> April 2016 to assist the middle income group (M40)

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<sup>36</sup> Diane Foo Eu Lynn, 'Government to Review Proposal to Give Lending Licence to Developers', available at <<https://www.propertyguru.com.my/property-news/2016/9/135838/government-to-review-proposal-to-give-lending-licence-to-developers>> accessed on 24 Feb. 2018.

<sup>35</sup> *Ibid.*

<sup>38</sup> Pressreader, 'The Domino Effect', available at <<https://www.pressreader.com/malaysia/the-star-malaysiastarbiz/20160910/281479275865962>> accessed on 24 Feb. 2018.



to own their first house. a budget of RM200 million has been allocated for this purpose. The scheme offers a one-time only gift from the government to the successful applicant of 10% of the purchase price of the property or RM30,000 whichever is the lower. To qualify the applicant must be:<sup>39</sup>

- “1. Malaysian
2. Aged 21 and above;
3. The applicant is first time house buyer within one household family;
4. Able to secure financing for the property from financial institutions;
5. Gross monthly household income lies between RM3,000 and RM15,000
6. The property must be priced below RM500,000.
7. Successful applicant will receive an approval letter from KPKT with a condition that the Sale And Purchase Agreement should be executed within 30 days.
8. Property purchased under MyDeposit cannot be sold for 10 years, from the date of the Sale & Purchase Agreement.
9. the deposit will be paid directly to the developer’s account or in the case of a sub-sale property, to the account of the lawyer”.

The scheme is good as it does not differentiate between public and private sector employees and safeguards against abuse of the scheme.

### ***Perumahan Penjawat Awam 1Malaysia (PPA1M)***

Under the 2018 Budget the PPA1M will be constructing more affordable housing priced between RM90,000 and RM300,000.<sup>40</sup> The scheme is open to all Malaysian citizens employed in the public sector, including those who are retired or serving on a contractual basis. However, the successful applicant will be prohibited from selling or otherwise transferring ownership except to the immediate family, for a period of 10 years.<sup>41</sup>

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<sup>39</sup>Malaysia Housing Loan, available at <MyDeposit <https://malaysiahousingloan.net/mydeposit-first-home-deposit-funding-scheme/>> accessed on 24 Feb. 2018.

<sup>40</sup>The Malaymail online, ‘Affordable housing among focus of BN government, says Najib, available at <<http://www.themalaymailonline.com/malaysia/article/affordable-housing-among-focus-of-bn-government-says-najib#8LvXoYoYH5ttEeXM.99>> accessed on 26 Feb. 2018.

<sup>41</sup> PPA1M ‘Conditions for application’, available at <<https://www.ppa1m.gov.my/application/condition>> accessed on 26 Feb. 2018.

The Public Sector Housing Financing Board (LPPSA) has recently been empowered to exercise more flexibility where loans are being provided for houses under the 1Malaysia Civil Servants Housing Project. They can now apply for housing loans beyond their 60% salary limit as part of the government's effort to encourage home ownership among its employees.<sup>42</sup> Whilst this may ease the access to financing, it calls into question the subsistence capability of the borrower whose card debts and other short term borrowings may increase, raising the household debt.<sup>43</sup>

LPPSA has also introduced additional measures to facilitate homeownership for public servants from 1 January 2018 being:<sup>44</sup>

1. "Allow financing by LPPSA to construct property on waqf land;
2. Include legal fee-related to sale and purchase agreement as part of financing by LPPSA;
3. Allow LPPSA joint-loan for husband and wife or children with a condition that all applicants must be public servants; and
4. Allow joint-home financing between husband and wife or children, with a condition at least one of the applicants is a public servant. The non-public servant needs to secure loans from financial institutions or agencies that provide financing facilities which agrees to be the second mortgage holder".

Whilst these initiatives are laudable, it does not detract from the fact that homebuyers still need to look for additional sources to cover their differential financing which only goes to increase the individual's indebtedness. Moreover, the scheme only benefits public sector employees.

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<sup>42</sup> The Malaysian Reserve, 'Govt. removes 60% salary limit for civil servants housing loans' (16 Nov. 2017), available at <<https://themalaysianreserve.com/2017/11/16/govt-removes-60-salary-limit-civil-servants-housing-loans/>> accessed on 26 Feb. 2018.

<sup>43</sup> Lim Le Sze, 'Debunking the Myth: Property Measures Have Led to Higher Loan Rejection Rates' BNM Quarterly Bulletin, 1<sup>st</sup>. Quarter, 33, available at <[https://www.bnm.gov.my/files/publication/qb/2017/Q1/p5\\_ba1.pdf](https://www.bnm.gov.my/files/publication/qb/2017/Q1/p5_ba1.pdf)> accessed 26 Feb. 2018.

<sup>44</sup> Malaysia Housing Loan, 'Malaysia Budget 2018, Housing Sector', available at <<http://malaysiahousingloan.com/malaysia-budget-housing-sector/>> accessed on 26 Feb. 2018.

### ***The Smart Sewa Programme***

PR1MA has introduced a Rent-to-Own (RTO) scheme for city dwellers. Rental accommodation for between 2 - 3 years at fixed monthly rental is offered whereby part of their rental will channelled as savings to finance their future home purchase. It is directed at low income earners but the homes are not for sale. The scheme has been introduced in Selangor and Johor.

### **INITIATIVES FROM DEVELOPERS**

Developers who adopt the 'build and sell' concept are offering limited leasing or 'Rent to-Own (RTO) schemes to help the homebuyer tide over the financing. Among these are UEM Sunrise Bhd., Mah Sing Group Bhd., TAHPS Group Bhd's "Stay and Own" scheme, Selangor Dredging Bhd (SDB) "Reside and Purchase" (RAP) programme and Khoo Soon Lee Realty Sdn Bhd's "Rent Now Buy Later" programme. It offers both conventional and Islamic RTO options. Typically, under the RTO scheme, buyers sign a tenancy agreement for between 2 -3 years and a Sale and Purchase Agreement with the developer and enter into occupation. They will have to pay at least a 5% down payment. Part of the rental will go towards financing their purchase price. Rentals could range from RM3,000 to RM10,000 per month.<sup>45</sup> Sunway Bhd. also offers leasing options for a limited period at higher interest rates than banks. The financing plan offers 88% guaranteed loan upon property completion, a deferred payment scheme, and a voluntary exit plan.<sup>46</sup> Innovative as the schemes are they come with their own challenges. Though it assists medium and high -end buyers who do not qualify for a 100% loan to cover the differential sum, the monthly rental could be prohibitive. Further this only applies to completed projects under the 'build and sell' concept. Consequently, only developers with a strong financial base could afford to offer such a scheme.

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<sup>45</sup> Lum Ka Kay, 'Property Developers open to Rent- to-Own, (17 Nov. 2017) The Edge market, available at <<http://www.theedgemarkets.com/article/property-developers-open-renttoown>> accessed on 26 Feb. 2018.

<sup>46</sup> iMoney.My Learning Centre, 'Property Developers To Offer Home Financing (9 Sept. 2016)', available at <<https://www.imoney.my/articles/property-developers-to-offer-home-financing>> accessed on 24 Feb. 2014.

Another innovative scheme is MayBank Group's 'HouzKey' in collaboration with five developers. This is an alternative method of home financing by way of leasing, based on the Islamic concept of Ijarah (lease) that provides customers with the option to purchase the property at a predetermined price at the end of the lease.<sup>47</sup>

## CONCLUSION

Housing and Local Government Minister Zuraida Kamaruddin announced in July 2018 the formulation of a new housing loan package targeting the first-time home buyers that will be finalised by BNM soon. Discussion was underway between the central bank, the commercial banks, the EPF and the Finance Ministry for this purpose.<sup>48</sup> Towards this end, the ministry was studying various initiatives that could be taken to address the issue of 'affordable housing' in Malaysia. Among the proposed initiatives is the formation of a National Affordable Housing Council (NAHC) that will centralise and synchronise all public affordable housing schemes to enable the ministry to provide guidelines on pricing, design and distribution of housing schemes. Meanwhile the Ministry was also looking at Singapore's Housing Development Board (HDB) scheme and the Industrialised Building Scheme (IBS) to lower the cost of construction.<sup>49</sup>

Stress occurs when elements that pushing beyond capacity to deal with and affect to the mental health. In current scenario, if the housing affordability stress continues to exist, it will bring a negative effect and influence on household wellbeing. It is because household wellbeing could be determined by the level of housing affordability stress for each family. The heart of the problem of home financing is the

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<sup>47</sup> Lum Ka Kay, 'Malaysia's first-of-its-kind rent-to-own scheme'(24Nov. 2014) The Edge market, available at <<https://www.edgeprop.my/content/1240171/malaysia%E2%80%99s-first-its-kind-rent-own-scheme>> accessed on 26 Feb. 2018.

<sup>48</sup> Bernama, 'Cabinet paper to coordinate all entities under KPKT' (4 June 2018), available at <<https://www.malaymail.com/s/1638346/cabinet-paper-to-coordinate-all-entities-under-kpkt>> accessed on 15 August 2018.

<sup>49</sup> Coach Rashid, 'How far has the new government caught up on its manifesto?'Berita Hartanah (25 Aug. 2018), available at <<https://coachhartanah.com/how-far-has-the-new-government-caught-up-on-its-manifesto/>> accessed on 3 Sept. 2018.

disparity between income and affordable housing. The pricing of houses is in turn affected by various factors such as cost of labour and materials, taxes, general economic conditions and the value of the currency. There is no easy single solution. The scheme for turning developers into financiers is fraught with high risk and attendant issues for both parties. The Government initiative to provide more affordable housing is a step in the right direction. However, offering longer term loans is not an ideal solution as it only increases the household debt. A more viable option would be to offer a limited period of leasing where you rent and pay your way towards property ownership. It is suggested that the government policy should be considered in order to understand the factors that influence stress for household to own a house.

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