





FACTORS AFFECTING HOUSING PRICES IN MALAYSIA: A LITERATURE REVIEW



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ABSTRACT

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Housing prices or the value of houses in Malaysia have fluctuated significantly in the last decade. This sort of indecisions creates an obvious effect on the people who wish to invest or buy housing in Malaysia. Many researchers had argued in the past that housing prices are closely related to the affordability of buyers to own a house, therefore the government plays a vital role in ensuring the housing prices of Malaysia are at par with the income levels. As such, the current study aims to discuss on several factors which affect housing prices in Malaysia. The study had identified several factors, namely foreign direct investment (FDI), gross domestic product (GDP), interest rate, unemployment and inflation for purposes of discussion. Hence, it is important to understand the factors affecting the housing prices in Malaysia for government and policy makers to make decisions. This study is made to provide answers for factors affecting Malaysia's house prices.

Contribution/ Originality: The study documents a research that has been conducted on factors affecting housing prices in Malaysia. This study would benefit governments, policymakers and consumers in the sense that they would be able to monitor these changes and make beneficial decisions on based on these factors.

1. INTRODUCTION AND RESEARCH OBJECTIVES

Housing prices have been one of the main topics discussed in the recent years. Overall various scholars and academics have come to conclude the various factors affecting house prices. For example, Gholipour *et al.* (2019) stated that the impact of foreign investment on housing price do not considerably make it more expensive to purchase homes. Besides that, Choy *et al.* (2013) indicated that foreign direct investment (FDI) inflows promote economic growth through spill over effects and more employment opportunities while the estimated coefficient for FDI inflows is positive and significant yet its impact on real estate prices is only modest. Moreover, Gholipour *et al.* (2014) found that foreign investments in the real estate sector do not cause higher property prices. Based on the various factors contributed by the scholars mentioned above, the variation of the findings is mainly due on how to measure housing prices, which had been produced through different results.

Since the 2011 to 2013 housing bubble faced by Malaysia, the housing affordability in the country has become an issue for its people. This has caused the housing index to skyrocket to a staggering 12 point in the year 2012,

and further up to 13 points in the year 2013 before finally starting its slow yet steady descend. The issue faced has caused housing to become so unaffordable for its people, that even 3 years after the Malaysian housing bubble, the housing prices were still deemed unaffordable. The obvious problem faced by the buyers during this time was that the household income did not grow at the same pace as rate of which housing prices grew. In other words, the individual wages were so low, that no one could afford buying property, meanwhile the prices of these properties kept on increasing. However, even though the housing prices are decreasing now, the fact remains that property developers are still facing a growing problem known as an overhang. This happens when properties are vacant and have been vacant for a long period of time and are not being sold. Therefore, it is important to understand the factors that affect housing prices in Malaysia and how the identification of these factors will benefit the government, buyers, sellers, and the financial institutions involved.

As such, this conceptual paper seeks to make further discussion on factors which influences housing prices in Malaysia. Section 2.0 describes the methodology used to conduct the study. Further, Sections 3.0 to 5.0 presents detailed and rich descriptions of themes that emerged from data exploration regarding the factors being investigated. Finally, Section 6.0 summarises the current study.

2. METHODOLOGY

The current study mainly refers to previous literature to discuss on factors affecting housing prices in Malaysia. The study had identified several factors, namely foreign direct investment (FDI), gross domestic product (GDP), interest rate, unemployment and inflation for purposes of discussion.

3. FACTORS AFFECTING HOUSING PRICES

Current insights in Malaysia demonstrate that enough houses are being built in pace with the current growing population. According to the National Property Information Centre the number of unsold residential properties has been rising since 2011 and peaked sharply in 2017. Housing prices have been one of the main topics discussed in the recent years. However, there are various factors affecting house prices in Malaysia.

3.1. Foreign Direct Investment (FDI)

FDI is where foreigners invest in estates and property in a country. In Malaysia Liberalisation policy is implemented which causes house prices in Kuala Lumpur and Penang (highly dynamic states) to increase in the long run. In a way the effects are not visible towards expensive house pricing that much but more to the less pricey properties as supply is less elastic. FDI also drives up prices by more in local authorities with larger house price earnings elasticity which is ones with less elastic housing supply. Along that, FDI reduces home ownership rates suggesting that residents may be priced out of the market in areas where foreign investors are more active and must rent rather than own homes.

3.2. Gross Domestic Product (GDP)

Gross domestic product plays a role in the factors that affects house prices and it is known that if house prices rise, then the wealth effect is likely to cause an increase in consumer spending which leads to higher aggregate demand and is likely to cause and increase in Real GDP and a higher rate of economic growth. This theory is aligned with the study of [Kok et al. \(2018\)](#) who argued that the effect of real GDP on house prices and transaction volumes persist comparably longer and stronger. While, the study of [Ong \(2013\)](#) showed that GDP is significantly and positively correlated with housing price in Malaysia. However, [Pillaiyan \(2015\)](#) justified that there is a real danger that the house prices are in a bubble as GDP was not identified as a driver of long-term house prices. Furthermore, [Gholipour \(2013\)](#) indicated that foreign real estate investment (FREI) is a significant determinant of house price appreciations. However, FREI only plays minor role in house price appreciations in the countries under

study. Next, [Gholipour et al. \(2014\)](#) explained how property prices are mostly affected by economic activities such as GDP and inflation in the short run.

GDP on the other hand, does not have a direct effect on house prices. However, if a collapse in the housing market were to ever occur, it will spread through the economy and causes the GDP to fall. In Malaysia, property is a main need for many Malaysians. Yet, not many of them could afford it. If one day, the government decides to increase the household credit, it is going to dry demands for housing, which will lead to residential investment contraction.

3.3. Interest Rates

Interest rates are controlled and monitored by the Central Bank of Malaysia known as Bank Negara Malaysia (BNM). Monetary policy will control the liquidity in economic growth through interest rates where BNM will either increase or decrease it to ensure economic stability. If the interest rates increase, the cost of mortgage will hike up causing people to rent and not buy property at the time being. When prices are high homeowners will sell their houses, which causes the number of sellers to increase yet the amount of buyer's decline and leads to the fall of house price. As interest rates are at its peak people will be more careful in their spending and the majority will start saving up which causes people not buying property because of the state of the economy and their income.

Interest rates play a big role in housing price determinant. However, based on the study of [Ong \(2013\)](#) finding shows that there is no significant relationship between the interest rate and the housing price. This study argued that if everyone is seeking the same thing, buyers or speculators will not care about the interest rate charged by financial banks, as the demand and supply are unbalanced. The same findings were found from the study of [Gholipour \(2013\)](#) where there is no significant impact of interest rates on house prices. [Choy et al. \(2013\)](#) also agrees that variable is estimated to be statistically insignificant and bears unexpected sign which indicates that real interest rates do not contribute to effects of housing prices in specific areas. According to [Mallick and Mahalik \(2015\)](#) housing prices has mixed response as the real interest rate increases. In addition, [Gholipour et al. \(2019\)](#) found that foreign investment, availability of finance services, economic activities, interest rate and costs of constructions are the main determinants of house prices. [Wang et al. \(2018\)](#) had also suggested that households are more likely to purchase properties when interest rates are low, resulting in increases in house prices in such circumstances.

Further, [White \(2015\)](#) had studied on an adopted model which had explicitly considered the role of mortgage market in impacting house prices. This relationship is in addition to the role of interest rates which were used to capture a channel of liquidity in earlier researches. [Mohan et al. \(2019\)](#) mentioned that a profound dynamic change would indicate that housing prices are influenced by mortgage interest rates or are sensitive to the mortgage market. [Gholipour et al. \(2014\)](#) had also indicated that important variables such as interest rates can influence property prices. As seen from this review, there were many scholars that expressed their opinions based on interest rates following their results found and some scholars have evidence of bias because data research made was only through one perspective and not the big picture.

3.4. Unemployment

Unemployment works both ways either demand side or supply side. Demand side serves as financial constraint and reduces the number of buyers as unemployment prevents a household from entering the housing market. Supply side as unemployment rate increase it lowers the expectations of job security and makes homeowners less willing to change houses since there would be a possibility of not being able to buy new ones as there are higher chances of being unemployed in the next period ([Goleman et al., 2019](#)). On the other hand, smaller cities of lesser population would experience big changes in prices compared to larger cities when facing similar changes in unemployment rates. The government on the other hand should increase the amount of affordable housing so that

people that used to be unemployed are employed again it wouldn't be too much of a burden to purchase an expensive property; this also helps to increase the purchase of property in Malaysia.

Unemployment rate in Malaysia had averaged at 3.28 percent from 1998 until 2019, reaching an all-time high of 4.50 percent in March of 1999 and a record low of 2.70 percent in August of 2012. Based on [Mohan *et al.* \(2019\)](#) it was revealed that a positive shock to unemployment rate tends to immediately lower housing prices. In other words, a growth in unemployment level may discourage individuals to purchase houses. Besides that, [Wang *et al.* \(2018\)](#) had estimated that unemployment rate shows insignificant impact on house prices. A lower unemployment rate may alleviate affordability constraints because of the increased purchasing power associated with higher incomes. Further, [Ciarlone \(2015\)](#) estimated that unemployment is also significant and have the expected negative sign towards house prices.

3.5. Inflation

Another factor affecting house prices is inflation. According to [Gholipour *et al.* \(2014\)](#) inflation increases construction costs of new houses. Higher construction costs will result in higher prices of new houses. A such, results of this study had shown that there is a 1 per cent increase in inflation would increase property prices by 0.027 per cent. Besides that, [Pillaiyan \(2015\)](#) concluded that Malaysian house prices (MHPI) were found to have a strong long-term relationship with inflation. [White \(2015\)](#) agreed that house prices will increase with the rate of real house price, with inflation exceeding a negative value from real wage inflation. [Ong \(2013\)](#) on the other hand, found that inflation does not affect housing prices and only three macroeconomic variables of GDP, population and RPGT were found to be positively and significantly correlated with housing prices.

Lastly, inflation is defined as a general and ongoing rise in the level of prices in an entire economy. According to [Tsatsaronis and Zhu \(2004\)](#) most things in the economy will increase in price during inflation. However, housing is viewed from two separate perspectives when it comes to inflation. Generally, housing is viewed as a good asset when it comes to inflation as housing prices tend to rise in tandem with inflation. However, from the other end of the spectrum we see the rise in housing in a negative effect on the younger generation as with inflation; the housing in Malaysia is not a reality they can afford.

4. CONCLUDING REMARKS

The current study has discussed on factors affecting housing prices in Malaysia. Findings from this study is hoped to be significant to governments, financial institutes and consumers. This research would benefit the government and policymakers in the sense that they are able to control these factors that affect the changes in housing prices in Malaysia. Governments can use this research to monitor and maintain certain variables that affect changes in housing prices in Malaysia. Moreover, this research would also benefit the financial institutes which monitor and invest largely in housing in Malaysia. Through this research financial institutes can see certain variables that significantly affect housing prices in Malaysia and monitor those variables and use them as a method to invest in housing in Malaysia and control the amount of risk faced by the financial institute. This research would also be very beneficial to financial institutes as they provide funds to consumers when purchasing real estate.

Therefore, it is very important for financial institutes to constantly monitor factors that affect housing market as it could affect their profitability. Lastly, consumers and corporate companies can benefit from these researches as well. Consumers and corporate companies can understand these variables, and this could provide them information on when to and when not to invest in housing in Malaysia follow the trends of these variables. Hence, we can conclude that these factors are highly beneficial to Governments, Financial Institutes and Consumers and Corporate Companies.

Moving forward, the researchers intend to test these factors using secondary data found in journals, books, newspapers, and other online resources. From investigations done via the use of secondary data, this research will

aid in the understanding of the factors that affect housing prices in Malaysia and in what way the identification of these factors will profit the government, buyers, sellers, and the financial institutions concerned.

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