

# Review of factors influencing rental values in general economics essay



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The purpose of this paper is to explain the determinants of rental values of a commercial property market in Nigeria, highlighting the display of rental volatility and why it is so. The paper begins with a general review of the real estate market and in a later section focuses on Nigeria. The paper also explains why the amplitude of volatility varies by property sector. The paper discusses how these relevant factors affect property investment decisions across the different sectors in Nigeria. In this study residential sector is chosen as it is a growing sector of commercial real estate market in Nigeria.

In Africa, one of the most populous country is Nigeria, and rank eight in the world. With reference to (2009 estimate by the United Nations Department of Economic and Social Affairs -Population Division) Nigeria housing challenge are enormous and need adequate attention. Majority of the populace lives in rented houses and from the statistic available it shows that 89% are in this situation. In Nigeria, Lagos State in particular has a population of 15 million and 70% of residents are tenants and housing demand is estimated to be approximately 2. 25 million. Demand for residential houses is on the increase and supply is on the low. Some of the existing accommodations are provided by private developers, and rent could be as high as 55 - 75%of intending tenant monthly incomes.

To achieve the above aims and objectives, literature review is undertaken, from sources such as Articles, Textbooks, Lecture notes, online information and journals. Analysis of relevant sources is in detailed. Also graphs, charts and some statistics are used. Relevant and appropriate references provided.

Briefly state the outcome of the study

Briefly state the suggestions/recommendations you want to make based on the study results to make the chosen market more efficient

### **A review of factors influencing rental values in general**

There are many factors influencing rental values in most markets. These include Interest rate, Inflation, Affordability, Infrastructures, Government Tax, supply and demand.

Generally, properties that are rentable are considered commercial property, and these are Offices, Retail and Industrial properties not excluding residential properties that also generate a huge income for Landlords and investors in Nigeria.

With reference: macroeconomics lecture note (2012) " Housing is essential as people need the necessity of shelter and somewhere to live with amenities. However, in the developed world most households consume more than basic needs and indeed the scale of consumption means that housing for many can be described as a luxury good. In most countries owning your home is an investment. So housing can be consumption as well as investment. Some households will rent from a public (social) landlord but these numbers are falling around the world.

In Germany the proportion of owner occupation is only 43% but in much of the rest of the European Union it is over half and in the UK it is around 69%. The countries with the highest percentages of owner occupation in Europe are Greece (76%), Spain (78%) and Ireland (79%).

Outside Western Europe, owner occupation in the major developed countries accounts for at least 60% of the housing stock. This is true also for many developing countries.”

In Hong Kong property and asset price are a major concern of Hong Kong residents and also of Hong Kong government. Since 2008 when the global financial crisis a number of economies have introduced expansionary fiscal measures and eased their monetary policies, resulting in a surge in global liquidity (The 2010-11 Budget).

The influence of the European sovereign debt crisis in 2012, brought a moderate fall in Hong Kong residential prices. However, the Financial Secretary still reminded Hong Kong citizens, “ Despite the recent stabilization of the property market, the low-interest environment persists, and the developed countries may again resort to quantitative easing policies to boost their sluggish economies. I shall, therefore, continue the strategy that has proven to be effective in facilitating the healthy and stable development of the property market.” (The 2012-13 Budget)

Leung, Chow and Han (2008) explored the short-term and long-term determinants of property prices in Hong Kong. Their studies showed that per-capita GDP, real interest rate, the amount of land supply as well as a residential investment deflator are long-term determinants of Hong Kong property prices.

The United State of America with particular attention to New York City, residents have spent millions to build themselves “ decent” places to

live/work. Well this was successful. Also urban areas such as Washington, DC  
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and NYC are seeing a huge growth in upper middle and above populations. This in turn fuels demand for all sorts of goods and services including rents.

A residential property is a durable asset. Just like all kinds of investment, investors of housing have to consider both the benefit of such investment as well as the opportunity cost of doing so. Keeping that in mind rental property is supposed to be a profit making enterprise. For much of past decade as easy credit allowed many to purchase homes rents decreased or were stagnant. Now that's all over and obtaining a mortgage has become difficult to impossible for many, demand for what rental housing there is is going up. Remember as well for many markets because demand for private homes including co-ops and condos was so great (fuelled by the mortgage boom) building of rental housing lagged. So now in many areas there just isn't enough rental housing to suit demand.

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What factors affect the rental market, where does the market stand today and is this good news or bad news for the rental property owners. Some of the major factors are looked at in the discussion below as evidenced obtained from analyst (Right Rent 2012).

### **1. 2. 1 Affordance**

The biggest is whether the individual can afford to buy a property. Today a lot of younger people cannot afford to get onto the property ladder, thus in turn this will mean a greater number of people are renting property and a greater number of new build or first time buyer houses or flats are getting bought by property developers. With the current market first time buyers

are finding it harder and harder to afford to get onto the property ladder, more people are renting property for longer and property prices continue to rise, all be it slower than has been seen over the last few years.

### **1. 2. 2 Interest Rates**

Another factor that can contribute to the number of people within the rental market is interest rates. How does this influence the rental market? Higher or lower interest rates have a huge impact on the rental market. Lets take a scenario where interest rates rise significantly, this leads to a big change in the market, firstly, the impact on landlords is high, mortgage values on property will rise (unless on a fixed rate) rental values will increase and depending how high the interest rate hike is can have a huge impact on the market. It can lead to an increase in the number of people who are renting property, landlords selling property due to the increase in the mortgage payments or an increase in rental prices.

### **1. 2. 3 Supply and Demand**

In any industry supply and demand is a key factor to how the market performs, too much of one and not enough of the other leads to problems. Within the rental market too many houses available for rent and not enough demand will lead to a decrease in rental prices for property, adversely demand for rental property is high, lots of people looking to rent property and not enough rental property on the market will usually result in an upturn for rental values for property.

## **1. 2. 4 How does the Market Stand Today**

The present market situation today is interesting, over the last 5-10 years property prices have risen dramatically in the UK, the rise has slowed but continues. This has left a number of first time buyers in the position of not being able to afford to get onto the property ladder for a number of different reasons. Some of these are the increase in personal debt, be that student loans, credit cards or personal loans. The massive hike in property value way above the rate of employment pay increases has left the majority of people who are not on the property ladder in the position of being unable to afford firstly the minimum 5% deposit and secondly the monthly mortgage repayments. The dangers open to people here are over stretching themselves with mortgages more than 5 times their current income or 100% mortgages, even a small jump in interest rates will affect these people. Supply of rental property to demand is currently good, there are tenants to fill property, as usual the better property on the market will get filled and some areas are in higher demand than others.

### **Figure 1: Annual percentage change in real rent**

### **Figure 2: RRPI UK – Average Rental Prices for the Whole of the UK**

[http://www.rentright.co.uk/public/charts/ChartPic\\_000084.png?204ce2a6-c638-4db3-b2e8-5a6b3da35053](http://www.rentright.co.uk/public/charts/ChartPic_000084.png?204ce2a6-c638-4db3-b2e8-5a6b3da35053)

Source: Rent Right (2012), 'Factors influencing rental values' <http://www.rentright.co.uk/rrpi.aspx>, last accessed on 18 October 2012.

### **1. 3 A review of Nigeria residential property market**

This section must discuss the same/similar factors pertaining to the study area stated in the introduction

1. 3. 1 Demand

1. 3. 2 Supply

Political issues

Corruption

Speculation

### **1. 4 Effect of volatility in rental value on investment decision**

**Negative effects – capital flight – e. g. people going to Dubai to invest**

**Instability and over charging of tenants**

**Positive effects**

### **1. 5 Summary and conclusion**

**Here you must summarise the key points identified and explain how the market could be made more efficient in the study area/market you have chosen**

This in mind is good news for the rental market today there are a huge number of people who are staying in rented accommodation for years more than before due to the viscous cycle of buying a property. If the landlords can keep their property and resist the temptation of selling for the quick cash in on the increase values of their property, there is no downturn in



property prices, then they can expect tenants to stay in property longer than ever before and more and more people will be renting property for longer than ever. The big question is will times change and if so when.

Rent right Property Rental Portal will be providing statistical analysis of rental prices and any increase and decreases in rental values using the RRPI (Residential Rental Price Index) this will give an oversight if there are any significant changes in the market.