THE ROLE OF RENTAL HOUSING IN DEVELOPING COUNTRIES: A NEED FOR BALANCE

by

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The views presented herein are those of the author(s), and they should not be interpreted as reflecting those of the World Bank.
Available statistics indicate that between one-third and two-thirds of the housing in cities of the developing world is occupied under some form of rental tenure, and there is no reason to expect these numbers to diminish. In contrast to widely-held bias against rental housing and the evils of "landlordism," data from a variety of cities suggests that occupants of rental housing are often as well served as homeowners, in terms of access to space and infrastructure, and that renters are expressing preferences among competing opportunities for use of scarce capital as well as among alternative living arrangements.

Data also indicate that -- in the absence of government policies, such as rent control, to discourage rental supplies -- an active rental subsector may be particularly effective in delivery of improved living conditions to the lower income segments of the urban population and may increase total rates of private sector capital formation and investment in housing. Benefits of improved affordability and cost recovery may be achieved for the housing sector as a whole.

Rental housing thus merits balanced attention in national housing policy and project design. Rentals are not a substitute for owner-occupied housing but rather serve a different market, a market often neglected because of the bias against rentals. Continued attention is needed to assure that policies and practices of the participants in Bank-sponsored urban development do not discriminate against rental housing.
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This paper was prepared as background for a broader review being undertaken in the Bank on housing policies.

Rental housing, a large and growing part of the shelter sector, has remained for many years a complex issue to deal with in the design and implementation of appropriate strategies on housing. This paper brings together recent evidence on several of the main issues that policies for the 1990's will need to address. The author also presents his conclusions and recommendations on steps that the Bank should consider taking.

Over the next twelve months, other work on rental housing questions will be in process, and there will be ample discussion within the Bank about the subject. The views expressed in this paper are intended to help facilitate that debate, not state a final position.

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David de Ferranti
EXECUTIVE SUMMARY

Large numbers of lower income people in the cities of the developing world live in rental housing, and the numbers are growing. Available statistics indicate that between one-third and two-thirds of the accommodations in typical cities are occupied under some form of rental tenure. Field observations suggest that 20-40 percent of housing in older World Bank-sponsored urban projects is now partially or totally sublet, a prevalent form of rental.

There is a widely held bias against rental housing, based in large measure on the evils attributed to "landlordism" and fostered by the generally poor economic and administrative record of public sector provision of rentals. Yet, evidence shows rental housing in many cases to be an efficient market response to conditions generally found in the developing world: burgeoning urban population, scarcity of serviced land for housing, and large numbers of households faced with competing opportunities for use of limited capital resources.

Renter households are generally younger, smaller, and have lower incomes than owner households. These characteristics are highly correlated, defying most statistical efforts to demonstrate causal relations. Nevertheless, critics of rental housing assert that such households choose to rent primarily because the option of ownership is foreclosed by lack of capital or available land. Such households are seen as likely to be exploited or at best as simply biding time until they can make the transition to ownership. Yet evidence from several cities illustrates that rental households are more likely to have access to piped water, are no more likely to live in crowded conditions, as compared to owners, and—except in cities where such policies as rent control seriously bias market conditions—are making a reasoned economic choice among alternative housing options.

Whether by necessity or choice, large numbers of households will continue to demand rental housing in the developing world's cities. The evidence suggests that greater numbers of people, particularly in lower income categories, could be helped more rapidly and more effectively through programs which take a balanced approach toward developing housing for rental as well as for ownership. Such programs could increase total housing supply at more affordable standards, increase rates of capital formation and private sector participation by mobilizing additional resources in the housing sector, and improve the likelihood of cost recovery and replicability.

Rental housing can be an attractive investment opportunity for both small and large scale investors. In the absence of a well developed system of financial intermediaries, private development of rental housing draws investment directly into the housing sector. In the context of actions taken to build housing finance institutions, lending for development of rentals increases potential to serve both savers and borrowers in a range of income
groups, increasing in turn the likelihood of institutional success. In some countries, private sector institutions appear able and ready to undertake large scale development of housing for rent and sale.

For the small scale developers of rental units, supplemental rent income can be an important aid to affordability of their property. For larger scale developers, rentals are primarily a source of return on invested capital, and will attract funds if the returns are not penalized through such mechanisms as rent controls. For lenders and tax authorities, collections may be made less political, and placed on a more businesslike footing.

In short, rental housing has a valid and productive role to play in national housing policy, a role which has significant consequence for the lower income segments of urban populations in the developing world. The Bank should exert more positive efforts to assure not only that this important sub-market is not inappropriately suppressed by national policies and local practices which discourage production of rental housing, but further, that Bank-sponsored urban housing projects offer balanced opportunities to developers of rental as well as owner-occupied housing.

The groundwork exists for increased Bank attention to rental housing: Some current project formulation review policies give at least implicit support to rentals, for example in the sizing of infrastructure. Research is being undertaken to assess in detail the impact of rent controls in selected cities. Yet few programs give explicit recognition of the role of rentals in lower income housing markets.

The observable benefits of rental housing, surveyed here, warrant more overt and comprehensive policy efforts. (Refer to Summary of Policy Recommendations.) Bank-sponsored projects (Table 1) can further demonstrate, and research can continue to assess and document these benefits, benefits potentially available to a major portion of the developing world’s urban population.
### SUMMARY OF POLICY RECOMMENDATIONS: BALANCED TREATMENT OF RENTAL HOUSING

<table>
<thead>
<tr>
<th>POLICY FOCUS</th>
<th>POLICY RECOMMENDATION</th>
</tr>
</thead>
<tbody>
<tr>
<td>Land</td>
<td>1. Continue efforts to assure that Bank-sponsored property acquisitions, land subdivisions, and ownership instruments do not discriminate against rental housing or against development of land to maximum market densities.</td>
</tr>
<tr>
<td></td>
<td>2. Continue efforts in design and development of Bank-sponsored urban projects to assure that appropriate subletting, subdivisions, and construction of auxiliary units for rent are not discouraged. Wherever possible, statements of policy permitting and encouraging such rental development should be explicitly made.</td>
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<tr>
<td></td>
<td>3. In countries where institutional and entrepreneurial resources are appropriate, maintain policies which permit release of land in blocks to developers of housing for rent or resale. In these cases, continue to focus government effort on infrastructure.</td>
</tr>
<tr>
<td>Capital and Finance</td>
<td>4. Make efforts in Bank-sponsored housing finance and savings bank schemes to assure that small scale participants can be attracted, and that lending for small scale rental properties is not discouraged.</td>
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<tr>
<td></td>
<td>5. Continue to encourage incremental development and upgrading of dwellings but avoid any discrimination against rentals. Actively encourage rentals where market conditions are appropriate.</td>
</tr>
<tr>
<td>Infrastructure and Construction</td>
<td>6. Standards of affordability should be set to reflect practices of subletting and development of auxiliary units found generally in target markets for Bank-sponsored projects. Where politically feasible, make these standards explicit.</td>
</tr>
<tr>
<td></td>
<td>7. Continue setting infrastructure standards in Bank-sponsored projects to accommodate development to maximum market densities, rather than for strict single-household affordability. The strategy should be made explicit wherever possible.</td>
</tr>
<tr>
<td>Tenure and Development and Use Rights</td>
<td>8. Place continued emphasis on extending infrastructure to serve the greatest area possible and to encourage directly subsequent development and upgrading of dwellings in newly served areas.</td>
</tr>
<tr>
<td></td>
<td>9. It should be recognized that subletting is a valuable element of project planning and will occur even if subsidies are substantially eliminated.</td>
</tr>
<tr>
<td></td>
<td>10. In those countries where current government policies and practices discriminate against rental housing, the Bank should continue to expand its efforts to have these policies changed. Short term policy studies and research to identify the degree to which these policies and practices foster inefficiencies and inequities in the housing sector may be warranted.</td>
</tr>
<tr>
<td>Policy Development and Sponsorship</td>
<td>11. The Bank should document and present the relative merits of rental housing and encourage balanced consideration of rental housing in national housing policies.</td>
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<tr>
<td></td>
<td>12. Undertake research on the following questions:</td>
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<tr>
<td></td>
<td>Demand —— o What role does rental housing play in integrating new migrants into the urban community?</td>
</tr>
<tr>
<td></td>
<td>o How do family and other social relationships influence characteristics preferred in rental units?</td>
</tr>
<tr>
<td></td>
<td>Supply —— o Do family and other social relationships unique to a particular city or country significantly influence the rate of development of auxiliary units and growth in density within projects?</td>
</tr>
<tr>
<td></td>
<td>o Does secure tenure encourage faster growth in numbers of dwellings, where subletting and construction of auxiliary space have occurred?</td>
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<tr>
<td></td>
<td>o What are the principal sources of finance for rental housing, and particularly for auxiliary space in Bank-sponsored projects?</td>
</tr>
<tr>
<td></td>
<td>o What are real rates of return on investment in rental housing, and what factors influence these rates in different market contexts?</td>
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1. THE IMPORTANCE OF RENTALS -- RECOGNITION AND BIAS

Large numbers of low income people in the cities of the developing world live in rental housing, and evidence shows the number is growing rapidly. As available statistics make apparent, rental accommodation is the predominant form of tenure in many—perhaps most—of the cities of the developing world. Surveys show that 20-40 percent of the residents of Bank-assisted projects are renters. Evidence suggests that this situation is in fact an efficient market response to demand preferences and supply opportunities.

1.1 Motivation for Reconsidering Rental Housing

The Bank’s 1980 policy statement on "Shelter" asserted that rental facilities, and typically shared accommodation, are the principal way shelter needs are met for large numbers of people in many communities in the developing world whose incomes are among the lowest. The statement then went on to say that "in new sites and services there is increasing recognition of the need to provide rental units within the project area. "For a variety of good reasons, the degree to which this need has been met has varied substantially among projects. The Bank’s experience with rental housing in a few countries both illustrates the problems which have occurred and the opportunities which may exist within ongoing urban lending programs.

A better understanding of rental housing markets and their role within the housing sector can lead to more rational strategies for government intervention through production, regulation, or finance. The following sections will discuss the scale of urban rental housing markets in developing countries, and a number of key issues of demand and supply which influence these markets. While the term "rental housing" often brings to mind blocks of government-operated flats, the rental sub-sector is quite diverse.

Why people choose rental tenure, and the possible consequences of that choice, have a number of long-term implications for savings, capital formation, and general quality of housing in developing urban areas. In the shorter term, a strong rental subsector can simply provide better standards of housing to greater numbers of households, at affordable levels of cost. Broader attention to rentals, and the policy initiatives posed to encourage such attention, are only a start in overcoming a long-standing bias against an important element of the urban housing market.
More than two years ago, The Urban Edge featured work by Alan Gilbert who, in spite of the widely published statistics showing the clear dominance of rentals as the more likely form of tenure, is one of the few researchers to deal specifically with conditions of rental housing in the cities of the developing world. Attention to rental housing in the U.S. and Europe has focused on failed public programs, and has frequently been pervaded by an air of crises (GAO, 1979; and Downs, 1979; for example). The Bank's research on its own activities has touched upon the biases against rental housing and the possible benefits of removing these biases, but little definitive action has yet been taken (Keare & Parris, 1982; and Malpezzi and Mayo, 1985; for example).

Experience with Bank-sponsored urban projects has yielded a rule-of-thumb that households in the lowest twenty percent of the income distribution generally cannot be reached with sites and services housing. These households are often major consumers of rental housing and, as statistics from a number of cities illustrate, gain access, through rentals, to improved conditions in typical urban projects.

1.2 Bias Against Rental Housing

However, in many countries rental housing is viewed as undesirable, particularly when undertaken by a profit-motivated private sector. Heavy emphasis is placed on home-ownership, often in the absence of any sound understanding of the factors underlying demand for or supply of rental versus owner-occupied housing. For example, the World Bank's 1985 report on Economic Development and Urbanization Policy for Kenya notes that only now, after more than a decade of experience with Bank-sponsored urban development, is the dominance of rental housing officially acknowledged.

This bias against rental housing is widely held, based on powerful rhetoric and failed examples of public supply. Transient populations or those trapped in Turner's "slums of despair" are widely viewed as the principal tenants of private sector rental supplies, tolerating poor conditions and exploitation by landlords because they have no choice. "Landlordism" is an evil to be rooted out of the housing supply system.

Apart from rhetoric about "landlordism," several problems are frequently attributed to rental housing:

- Areas with high proportions of rental housing are believed to be poorly serviced and poorly maintained, in terms both of individual dwellings and the neighborhood as a whole;
- Areas with high proportions of renters are believed to have weak social structures, and less cohesion and stability;
- Renters are thought to be particularly vulnerable to economic losses within a system characterized by rapid escalation of land prices and general crowding accompanying urban growth.
The generally abysmal performance of public sector rental housing in both industrialized and developing countries has further diminished the already low esteem in which rental housing is often held. National and local policies have introduced a real economic bias against rental housing through such means as tax advantages for owners and imposition of rent controls.

1.3 A Complex Problem

Objective study of the role of rental housing is complicated by the extreme difficulty of separating the roles of supply and demand in any statistics on the housing market. The decision of a household to rent or to purchase a dwelling is tied closely to location, availability of and preference for units of particular size and quality, available financial options, and the household’s alternative uses for limited capital.

While the problem is complex, evidence suggests that in many cities people do make a meaningful choice between renting and ownership, and differences in welfare often associated with tenure status may be better explained by other factors than tenure status itself. Indeed, even in the United States, where the goal of home-ownership is a basic part of the culture, there has been serious questioning of the social benefits attributed to high rates of ownership (Struyk, 1977), and a concern that the pendulum of housing policy has swung too far in the direction of discouraging production of rental properties (GAO, 1979).

1.4 Structure of This Paper

This paper describes the several reasons why rental housing deserves greater attention as a productive and desirable element of a balanced housing policy and should be given more overt attention and a better defined role in urban projects sponsored by the World Bank:

- There is a clear demand for rental housing;
- Contrary to widely held biases, rental housing appears in a number of cases examined here to bring better quality of housing to its occupants, and sooner, when compared to owner-occupied dwellings, and is not selected simply because these occupants have no choice;
- The limited resources of the Bank and its clients can achieve greater leverage in increasing total housing supplies if rental development is given even treatment in housing policy and project development.

Chapter 2 considers the overall scale of the market for rental housing observed in cities at various stages of development. Chapters 3 and 4 then describe the factors which affect demand for and supply of rental housing. A basic policy issue is addressed in Chapter 5: Are there real advantages to supporting homeownership? The answer to this question suggests there are opportunities to be captured through a more balanced approach to rental housing. Chapter 6 discusses these opportunities. Chapter 7 concludes this presentation with recommendations for how more balance may be encouraged in Bank-sponsored urban development programs and projects.
A part of the debate over the value of rental housing may be one of definition. The term "rental housing" represents a diverse assortment of housing types and tenure arrangements, often made difficult to distinguish by the unique social and economic characteristics of a particular country. Without trying to be too exacting, four principal categories of rentals seem adequate for this discussion:

i. **Investor-owned commercial rental housing.** Full dwellings are developed, singly or in groups, and owned by a landlord who typically does not live in the dwelling. Landlords may be private businesses or public agencies operating in a commercial capacity. Medium to large blocks of flats are a frequent form for this category of rentals, although a single dwelling unit rented in its entirety to a single tenant would qualify as well.

ii. **Owner-occupied commercial rentals.** Full dwellings are developed and managed in small groups, typically of two to four units, by an owner who occupies one of the units. Duplex apartments and subdivided older houses are frequent examples of this category.

iii. **Auxiliary units.** Dwellings are developed as additions or partitions of units initially intended to be single, and are managed by the owner-occupant of the original unit. The added units may be complete with all services, or may share access to common water and sewer, but at a level no worse than the owner's.

iv. **Shared accommodation.** Portions of a dwelling are leased to tenants, who must share both space and services with other tenants. The owner may be resident, sacrificing a degree of privacy in access to services and common areas, or may move out entirely.

Within these categories there can be substantial variety in the way the transactions between landlord and tenant are structured. In Korea, for example, government survey data distinguishes four categories of tenure which in many countries would be termed simply "renter occupied" (Follain, et al., 1982). The terms of rental differed substantially, depending primarily on how much has to be paid in advance of occupancy. In some cases, the amount required may exceed the renter household's annual income and is held by the landlord until the tenant leaves. The amount of rent is then the return foregone by the tenant and received by the landlord (not necessarily the same amount). Property owners in Seoul can finance the construction of new rental units by collecting this payment from the prospective tenant, in advance of construction.

Commercial rental units (categories i and ii) are more likely to be developed and operated by the formal sector of the economy. Auxiliary units and shared accommodations are generally supplied through the informal sector. Rentals typically grow in Bank-sponsored sites-and-services projects when auxiliary units are developed and when portions of houses are sublet. Few studies have been made to identify in even general terms the degree to which such rental development has occurred.
<table>
<thead>
<tr>
<th>Country City</th>
<th>Year</th>
<th>GDP per capita (in 2010 $)</th>
<th>Average Household Size</th>
<th>Demand/Supply</th>
<th>Vacancy Rate</th>
<th>Average Persons/Room</th>
<th>Average No. Rooms</th>
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<td>3681</td>
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</tr>
<tr>
<td>Panama</td>
<td>1980</td>
<td>400</td>
<td>3.0</td>
<td>3.0</td>
<td>3.0</td>
<td>3.0</td>
<td>3.0</td>
<td>3.0</td>
</tr>
<tr>
<td>Peru</td>
<td>1980</td>
<td>300</td>
<td>3.0</td>
<td>3.0</td>
<td>3.0</td>
<td>3.0</td>
<td>3.0</td>
<td>3.0</td>
</tr>
</tbody>
</table>

**Notes:**
1. All data from U.N. statistics, unless otherwise noted. 2. Data not available. 3. Urban population growth only. 4. Residuals are due to housing provided through work, contract, or informal arrangement. 5. National total, unless otherwise noted. 6. Includes non-residential construction. 7. Kitchens are not counted as rooms. 8. Excludes formal housing estates. 9. Data for 1980. 10. Renters include those who receive free housing under work contracts. 11. For buildings rather than households.
Table 2. Tenure of Households in National Housing Stock of Selected Industrialized Countries

<table>
<thead>
<tr>
<th>Country</th>
<th>Census Year</th>
<th>Tenure (percent)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td>Owners</td>
</tr>
<tr>
<td>Australia</td>
<td>1971</td>
<td>67</td>
</tr>
<tr>
<td>Austria</td>
<td>1972</td>
<td>49</td>
</tr>
<tr>
<td>Belgium</td>
<td>1970</td>
<td>54</td>
</tr>
<tr>
<td>Finland</td>
<td>1970</td>
<td>59</td>
</tr>
<tr>
<td>Germany</td>
<td>1972</td>
<td>34</td>
</tr>
<tr>
<td>(Federal Republic)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Greece</td>
<td>1971</td>
<td>71</td>
</tr>
<tr>
<td>Japan</td>
<td>1973</td>
<td>59</td>
</tr>
<tr>
<td>New Zealand</td>
<td>1976</td>
<td>70</td>
</tr>
<tr>
<td>Norway</td>
<td>1970</td>
<td>53</td>
</tr>
<tr>
<td>Spain</td>
<td>1970</td>
<td>57</td>
</tr>
<tr>
<td>Switzerland</td>
<td>1970</td>
<td>29</td>
</tr>
<tr>
<td>United Kingdom</td>
<td>1971</td>
<td>43</td>
</tr>
<tr>
<td>United States</td>
<td>1977</td>
<td>65</td>
</tr>
</tbody>
</table>

Source: United Nations and national data, as reported in Howenstine (1983).
In most cases, shared accommodation represents use of a building in a way differing from that for which it was designed. A prevalence of shared accommodation may be a sign of a mismatch between the characteristics of the housing stock and housing demand, a mismatch which can come about when rapid urban growth or political change have brought new groups of housing consumers into the market. However, in some cities (for example, in West Africa), where shared accommodation may be a substantial part of the rental subsector, structures are constructed specifically for shared accommodation, with communal cooking and toilet facilities. Such shared accommodations assume many of the characteristics of large scale commercial rental housing (category i).

The size of the market for rental housing varies substantially among countries, and among cities within the same country. Nevertheless, trends in the share of urban housing provided by rentals can be observed, although consistent and reliable statistics are difficult to assemble. The data presented in Table 1 is indicative of the range of variation and the general size of the market in cities where the World Bank is most likely to be active. In most instances, between one-quarter and two-thirds of the urban housing is rented. (Rural housing is often largely owner-occupied.) These estimates may be conservative, because of the typically large informal component of rental housing in less developed countries.

Rental housing's large market share is not strictly related to level of development. Table 2 illustrates that rental housing has perhaps a more significant share of the market in more industrialized countries. While these aggregate national statistics (rather than urban data only) may tend to reduce rentals' share, the data may be generally comparable to Table 1 because of the high urbanization rates in most of these countries.

Of almost 70 countries reported in United Nations statistics published since 1970, only four instances can be found where the percentage of rental households comprises less than 15 percent of the urban housing market (Niue Island, 1966; American Samoa, 1968; Nepal, 1961; and Guatemala, 1964). In general then, rentals may account for one-third to two-thirds of urban housing markets. Figure 1 illustrates graphically the apparently steady pattern of demand for rentals over a range of development levels.

Figure 2 illustrates that the rapid growth of urban population appears to have substantial impact on the demand for rentals. Where subdivision of larger houses and subletting are not restricted by law, the rental sub-sector—and informal rentals in particular—can avoid the time-consuming process of land redistribution and site preparation, to respond most quickly to increased housing demand associated with high urban population growth, and in particular, high in-migration.
Figure 1.
Relationship of Rental Tenure and per Capita Income, Selected Developing Countries (data from Table 1)
Figure 2.
Relationship of Rental Tenure and Urban Population Growth Rates, Selected Developing Countries (data from Table 1)
The stereotype of rentals as a temporary solution for new urban migrants on their way to home ownership would suggest that the overall demand for rental housing would decline following reductions in urban in-migration. More stable population might reduce the need for housing market flexibility which a greater proportion of rentals implies. Hence, whatever the current position of rental housing in a less developed country, one might anticipate a long term decline in its importance. However, the emphasis in this hypothesis is decidedly on "long term," and the absolute demand for rentals is unlikely to fall even if rentals' share declines. Indeed, government policies discriminating against supply of rental housing have brought broad declines in production in a wide range of more industrialized countries, leaving demand apparently unmet and causing alarm among policy analysts (Howenstine, 1981, 1983).

Other factors may give rise to a higher share for rentals in urban housing markets: Alternative investment opportunities for limited capital will influence tenure preferences. Households with a shortage of capital may prefer to invest in opportunities other than housing, particularly those which can produce cash income. In El Salvador, for example, rental units with direct street access were observed to command a premium rent, because the occupant could establish a small business. In general, renters show a lower propensity to consume housing than do owners (Keare and Parris, 1982; Malpezzi and Mayo, 1985). Cultural preferences may lead households to choose to rent, even when actual shortage of capital is not a constraint. In the major cities of West Africa, for example, many people retain strong ties to their villages and towns of origin, own property there, and have apparently little desire to own in the city of their current employment. (Traditional tribal systems of land tenure may accentuate the effect). In some countries--the U. S. for example--older people may prefer to maintain their capital in a more liquid form than housing.

A first point can then be made, that rental housing plays a substantial role in the urban housing market of developing (and developed) countries. Biases against rental housing must have substantial social and economic impact. Examining the sources of demand for rental housing shows where some of these impacts fall.
Who are the occupants of rental housing, particularly in a developing country, and what factors influence their consumption of housing? There are several views: One view posits a basic sociological and demographic difference between the households who rent and those who choose to own their dwellings. Ingram (1984), for example, reports typical findings, that renter households in Bogota and Cali, Columbia, have younger heads, smaller families, and lower incomes than owners. Howenstine (1981), comparing rental markets in industrialized countries, writes of the special groups which prefer rentals--households of the elderly, the more highly mobile, the younger and more newly independent. The implication of this view is that there will be a base level of demand for rental housing in any city or country, related to the population of these special groups.

An alternate view is that constrained supply limits homeownership, consigning those who cannot own to rental status. Rentals then represent a residual of unsatisfied demand for ownership, a residual which increases as market conditions make ownership more difficult. For example, Gilbert (1983) suggests that ability to gain access to land is one of the principal influences on the size of the rental market. Where land prices rise at rates outpacing the market's ability to respond with smaller plots and less desirable locations--in such cities as Mexico City and Bogota--there are increases in numbers of renters.

A third view sees renting as a transitional stage in the life cycle of a household--people rent only until they reach a stage of life when they will choose to own. John Turner's influential descriptions of the slum-dweller espoused this view, which suggests that there may at any given time be a real demand for rentals, but that this demand will be maintained only to the extent that new renter households enter the market at a rate equal to that at which households "mature" to ownership. This third position is similar to the second in that those households trapped in the "culture of poverty" will be unable to make the transition, and will always be renters.

In much of the discussion of rental housing there is the expressed or implied proposition that everyone would choose to own a home, if only the supply situation would permit it. Extended to a normative position—that everyone should own his own home—this view has been an ideological basis for housing policy in the U. S. for at least four decades. People in other countries seem not to hold the dream so strongly (Boersch-Supan, 1985).

Whatever the actual causes of demand for rental housing, conditions associated with high demand for rentals are likely for the foreseeable future to remain typical of most developing countries' cities. High rates of birth and family formation, combined with high rates of urban in-migration, assure a continuing presence of the types of households likely to be the prime rental market.

Beyond this basic source of demand, other common features of the occupants of rental housing can be observed in data from a number of countries. These features characterize the demand for rental housing, in terms of numbers of dwellings and of such characteristics as sizes of dwellings preferred.
3.1 Household Incomes

Household incomes of renters are found generally to be low, as compared to homeowners (Estudio, 1978; Cronin and Rasmussen, 1980; Ingram, 1984; Mayo, et al., 1983). The pattern is reflected in a variety of statistics. Figure 3, based on household surveys in five cities, shows typical results. In Seoul, Bogota, Cali, and Manila, the percentage of households owning their dwelling increases generally with household income. Only in Cairo, where rent control makes it advantageous (at all income levels) to remain in desirable rented units, is the pattern different.

But whether low income is a cause of the rental choice or is simply associated with other characteristics of the renter household is unclear. Lower age of the household head and smaller family sizes, also found to typify rental households, are closely correlated with income. Together, these statistics represent a pattern that younger--perhaps "newer" is a better term--households are a principal source of demand for rental housing. To conclude simply that renters are necessarily the poorer households is in many cases not well justified (Gilbert, 1983).

3.2 Dwelling and Household Size

Renters seem generally to demand less space than owners. For example, in Cairo the mean number of rooms per owner-occupied dwelling was 3.64, compared to 3.22 for renters (Mayo, et al., 1982). In many cities in Nigeria, the percentage of rooms occupied by owners is typically higher than the percentage of owner-occupied dwellings (Table 3), implying that owner-occupied dwellings must have larger numbers of rooms. Moreover, the individual renter household’s demand for housing increases somewhat more slowly with growth in income than does the comparable owner household’s (de Leeuw and Ekanem, 1973; Follain, et al., 1982; Mayo and Gross, 1985).

These relationships may be due to the large initial cost of becoming an owner in most countries, or may simply reflect the owners’ view of housing as an investment as well as a consumption good. However, the relationship may also be due to correlations of income with household sizes and the need for space. Figure 4 illustrates the generally strong relationship between household size and the fraction of households owning. (As in Figure 3, Cairo’s rent control produces unusual results). The relationship is demonstrated across cities and countries as well. (See Figure 5.) The steeper slopes of the plots in Figure 4, compared to Figure 3, illustrate the stronger effect that household size may have on likelihood of ownership.

3.3 Desires for Tenure Security

Security of tenure, widely cited as a major advantage of homeownership, is valued highly by renters as well. For example, studies in the Philippines (Friedman, et al., 1985) found that renters were apparently willing to pay a premium rent for a unit in legal, non-squatter areas, 11-18 percent above rents for otherwise similar units in squatter areas.
Figure 3.
Likelihood of Homeownership versus Household Income, by Deciles, for Selected Developing Country Cities (data from surveys, various years)
Table 3: Conditions of Tenure in Selected Higerian Cities

<table>
<thead>
<tr>
<th>Location</th>
<th>Percentage of Dwellings</th>
<th>Average Monthly Rent</th>
<th>Percentage of Rooms</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Owner-Occupied</td>
<td>per 10 sq. m</td>
<td>by Rent Status</td>
</tr>
<tr>
<td></td>
<td>(N. 1973/74)</td>
<td></td>
<td>Normal Free</td>
</tr>
<tr>
<td>State</td>
<td>City</td>
<td>Rooms</td>
<td>Nominal  Own. Oct.</td>
</tr>
<tr>
<td>SOUTHWEST</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Lagos</td>
<td>Lagos Metro</td>
<td>4.8</td>
<td>7.12</td>
</tr>
<tr>
<td>Oyo</td>
<td>Ibadan</td>
<td>23.4</td>
<td>5.2</td>
</tr>
<tr>
<td></td>
<td>Ile</td>
<td>30.3</td>
<td>0.8</td>
</tr>
<tr>
<td>Ondo</td>
<td>Akure</td>
<td>30.5</td>
<td>2.6</td>
</tr>
<tr>
<td></td>
<td>Ilale</td>
<td>40.2</td>
<td>0.8</td>
</tr>
<tr>
<td>Ogun</td>
<td>Abeokuta</td>
<td>31.0</td>
<td>2.6</td>
</tr>
<tr>
<td>Bendel</td>
<td>Benin City</td>
<td>20.7</td>
<td>4.5</td>
</tr>
<tr>
<td></td>
<td>Sapele</td>
<td>9.9</td>
<td>2.6</td>
</tr>
<tr>
<td></td>
<td>Wuse</td>
<td>8.4</td>
<td>5.2</td>
</tr>
<tr>
<td>SOUTHEAST</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Rivers</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Port Harcourt</td>
<td>1.3</td>
<td>1.9</td>
</tr>
<tr>
<td></td>
<td>Nensere</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Imo</td>
<td>Aba</td>
<td>11.1</td>
<td>3.5</td>
</tr>
<tr>
<td></td>
<td>Usuakwa</td>
<td>79.2</td>
<td>0.3</td>
</tr>
<tr>
<td>Anambra</td>
<td>Etaga</td>
<td>6.6</td>
<td>4.2</td>
</tr>
<tr>
<td></td>
<td>Onitsha</td>
<td>15.6</td>
<td>4.3</td>
</tr>
<tr>
<td></td>
<td>Afikpo</td>
<td>92.1</td>
<td>0.9</td>
</tr>
<tr>
<td>Cross River</td>
<td>Calabar</td>
<td>21.7</td>
<td>2.7</td>
</tr>
<tr>
<td></td>
<td>Edom-Ekpe</td>
<td>38.1</td>
<td>2.1</td>
</tr>
<tr>
<td></td>
<td>Ugep</td>
<td>82.3</td>
<td>1.5</td>
</tr>
<tr>
<td>Benue</td>
<td>Makuwari</td>
<td>25.3</td>
<td>2.8</td>
</tr>
<tr>
<td></td>
<td>Igara</td>
<td>27.2</td>
<td>1.6</td>
</tr>
<tr>
<td>NORTH</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kwara</td>
<td>Bornu</td>
<td>41.7</td>
<td>4.7</td>
</tr>
<tr>
<td></td>
<td>Ojala</td>
<td>50.3</td>
<td>1.8</td>
</tr>
<tr>
<td></td>
<td>Ilehoja</td>
<td>20.6</td>
<td>3.12</td>
</tr>
<tr>
<td>Niger</td>
<td>Minna</td>
<td>26.5</td>
<td>2.15</td>
</tr>
<tr>
<td></td>
<td>Bida</td>
<td>68.0</td>
<td>2.6</td>
</tr>
<tr>
<td>Sokoto</td>
<td>Sokoto</td>
<td>74.0</td>
<td>3.01</td>
</tr>
<tr>
<td></td>
<td>Gusau</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Kaduna</td>
<td>Kaduna</td>
<td>10.5</td>
<td>5.27</td>
</tr>
<tr>
<td></td>
<td>Zaria</td>
<td>64.4</td>
<td>3.55</td>
</tr>
<tr>
<td>Kano</td>
<td>Kano</td>
<td>44.3</td>
<td>3.66</td>
</tr>
<tr>
<td>Bauchi</td>
<td>Gumel</td>
<td></td>
<td></td>
</tr>
<tr>
<td></td>
<td>Bauchi</td>
<td>17.3</td>
<td>3.98</td>
</tr>
<tr>
<td></td>
<td>Akwara</td>
<td>81.3</td>
<td>1.72</td>
</tr>
<tr>
<td>Plateau</td>
<td>Jos</td>
<td>17.3</td>
<td>3.96</td>
</tr>
<tr>
<td></td>
<td>Lafia</td>
<td>81.2</td>
<td>0.54</td>
</tr>
<tr>
<td>Borno</td>
<td>Maiduguri</td>
<td>37.6</td>
<td>10.5</td>
</tr>
<tr>
<td></td>
<td>Nguru</td>
<td>76.3</td>
<td>7.6</td>
</tr>
<tr>
<td>Gongola</td>
<td>Mubi</td>
<td>63.4</td>
<td>4.9</td>
</tr>
</tbody>
</table>

This premium was generally lower than that found for ownership. The higher premium for owners may be related to the commitment of capital required of the purchaser of a house. Improved security of tenure for the owner represents a reduced risk of loss of investment.

Formal leases are not necessary to increase renters' sense of secure tenure. A good quality roof and construction of a second floor increased perceived safety from eviction--i.e., security of tenure--of renters in that building. Thus, benefits of increased security of tenure for the building owner, encouraging improvement of the property, may be passed on to tenants and may elicit higher rents.

3.4 Renters As Mobile Households

The relatively high transaction costs--psychological as well as economic--associated with becoming a homeowner are generally presumed to encourage households which wish to maintain their mobility to rent accommodation rather than to own. The age of the head of household, a proxy perhaps for wealth and mobility, is a significant determinant of the likelihood of ownership. While the direction of the causal relationship may be argued (Boehm, 1981), the relationship that owners are generally less likely to move than are renters is clear.

Figure 6 illustrates the relationship observed. Households that have remained in the same dwelling for longer periods are more likely to be owners. The relationship appears to be true even in Cairo, here rent control has made it effectively costly for a tenant of long standing to move to other accommodations.

The increase in likelihood of ownership across income deciles is less substantial than across length of residence. (Compare Figures 3 and 6). Like household size, household mobility may be more significant than income as an indicator of the demand for rental housing.

3.5 Tenure Choice in the Housing Market

The factors discussed the preceding sections establish a basic level of demand for rental housing. However, studies of tenure choice developing countries, demand for rentals may be significantly greater than these basic levels.

One of the more popular approaches to analysis of the tenure decision involves surveying recent movers. A presumption is made that the household had to move to buy, although location and tenure decisions are not necessarily tied together (Ihlanfeldt, 1980).
Figure 4.
Likelihood of Homeownership versus Household Size, by Deciles, for Selected Developing Country Cities (data from surveys, various years)
Figure 5.
Relationship of Rental Tenure and Average Household Size, Urban Sector of Selected Developing Countries (data from Table 1)

Estimated Average Household Size

Nigeria (Lagos)
Nigeria (Kano)
Zimbabwe
Guatemala
Philippines

World Bank—30865:5
Figure 6.
Likelihood of Homeownership versus Household's Length of Time in Residence, by Deciles, for Selected Developing Country Cities (data from surveys, various years)
In fact, tenure and locational decisions can seldom be truly separated. On the one hand, external discrimination and internal household preferences may make certain locations much more desirable than others, even though opportunities for rental or ownership may be restricted in those areas. On the other hand, once the decision on tenure is made, household income and housing prices will combine to determine which areas are effectively available for consideration (Cronin and Rasmussen, 1980). Inefficient land markets and urban expansion, combined with poor transport infrastructure, place a premium on locations which would be particularly desirable for the occupants of rental housing and increase effective prices for rentors.

A recently published study compares tenure choice in the U.S. and Germany and concludes that the tax advantages and basic ideological bias toward homeownership are principal factors underlying the high rates of ownership and the prevalence of single-family detached housing in the U.S. (Boersch-Supan, 1985). (It is interesting also that relatively recent tax incentives for homeownership in the U.K. led a vice-president of the investment banking firm of Salomon Brothers Inc., quoted in The Wall Street Journal, to term that country "on a per capita basis, the fastest-growing homeownership country in the world.")

Boersch-Supan found that households in the U.S. are much less likely than Germans to be influenced by relative prices to shift from ownership to rental. While Germans may state a preference for ownership, they find large rental units attractive as well. Yet in both countries, tenure type is the primary dimension for characterising housing choice -- choices of structure types and sizes follow after the tenure decision, again supporting the notion that there will be a minimum underlying demand for rentals in most countries and that suppression of rentals (for example through rent control policies) will have significant costs.
4. THE LANDLORDS: CHARACTERISTICS OF SUPPLY

In most developing countries -- and increasingly in more developed countries as well -- there is a substantial diversity of arrangements under which those who effectively own housing resources become landlords and rent accommodation to others. Because this diversity is often poorly described, statistics on rental supply conditions must be examined with care. The case of Korea, where government survey data distinguishes four categories of rental tenure, has been mentioned: Terms of rental differ substantially, depending primarily on how much has to be paid in advance of occupancy. Advance payments received by potential landlords in Seoul are a significant source of financing for the construction of new rental units.

In the broadest terms, as suggested in the description of four principal types of rental housing units, production of urban rental housing in developing countries is typically two-tiered: At the upper level, formal sector construction produces modern blocks of flats; attached duplex, row or terraced units; and single family units. This upper tier builds generally for civil servants or middle and upper management of private companies.

At the lower level, informal production proceeds largely by infill and subdivision. In much of east and west Africa, for example, separate structures may be built on the same property, effectively subdividing the plot and filling open land. In North Africa and the Middle East, a second or third storey may be added to an existing building. In Latin America, a wing may be added on. These informal types of rental housing have various names -- auxiliary or accessory units, "mother-in-law" or "granny" flats, shared accommodation, and sublet dwellings.

Leasing of one or two rooms within a single-family dwelling (i.e., shared accommodation) represents the lowest of the lower tier of production. In some areas, such as West Africa, the scale of shared accommodation may become substantial, and large blocks of single-roomed units are built. Households occupy one or two rooms in the building, and have access to whatever cooking and toilet facilities are available. This style of rentals may be the only shelter accessible to the poorest households.

The situation found in El Salvador typifies the supply of informal rental housing in many developing countries (Estudio..., 1978): Mesones were small apartments, centrally located near jobs in the old downtown area. These were the units which -- when they gave the occupant direct access to the street and thus opportunities to operate a small shop or other business from the home -- commanded premium rents. In less central locations, old large homes (casas viejos) were subdivided into larger apartments which might eventually be purchased by the resident. Finally, on the fringes of the urban area, illegal subdivisions (colonias ilegales) grew, with large enough lots to permit development of auxiliary units. In the central mesones, lack of capital was the most frequently cited impediment to small businesses, and those people with capital apparently preferred not to invest it in housing. In the colonias ilegales, auxiliary units generated the supplemental income essential to affording payments on loans which enabled land purchase.
Figure 7.
Relationship of Rental Tenure and Average Housing Output, Urban Sector of Selected Developing Countries (data from Table 1)
The Bank-sponsored urban project which was placed in this area found that participant households in the lowest income decile were devoting up to 40 percent of their incomes to housing, while those in higher income groups allocated less than 20 percent. The investment motives were seen in the high proportion of houses or parts of houses that were rented. To be able to construct auxiliary units for rental, participant's resources were drawn from throughout the extended family structure and funneled into this investment opportunity (Keare and Parris, 1982).

4.1 How Access to Land Can Motivate Rental Supply

Although there are arguments to the contrary (Mohan and Villamizar, 1982), lack of access to land is widely believed to be a major restriction on production of all types of housing. Constraints to land access spring from a variety of sources, including lack of infrastructure, sprawling growth which separates living space from employment opportunity, government regulation, and tightly controlled historical patterns of ownership. Where land is most restricted, there is likely to be a strong incentive on the part of small scale land owners to develop auxiliary units.

If land is restricted, then auxiliary rental units may become a substantial part of the housing supply. One might expect there to be a correlation between higher levels of housing production and higher levels of rental tenure. Figure 7 illustrates relationship, although very weakly.

The incentives to develop rental housing can be depressed by such policies as rent control. For example, the Bank-sponsored urban program in Burundi emerged during a period of unprecedented domestic inflation and stagnant urban housing development. Kwijabe, the site of initial development of serviced plots and upgrading, was the first new development in Bujumbura in the two decades since the end of colonial control. The 1981 lifting of rent controls on private units in Bujumbura was followed by a boom in new construction of units for higher income households. Development of auxiliary units, termed an "annex" in Burundi, was implicitly accepted as a way to improve affordability in the project, and indeed, 80 percent of the first units completed, by June 1983, apparently went to the target population of households below the 55th percentile poverty threshold.

4.2 Rent Control's Effect

Conventional wisdom, supported by numerous studies, is that supply of rental housing is over the long term suppressed by imposition of rent controls. Less generally accepted is the observation that a consequence of suppressed supply is effectively increased prices for rental housing — observed perhaps as declining quality of accomodation or increases in expenditures on travel or other costs related to staying longer in a particular residence than would be the case without the incentive of controlled rent. The net effect of rent control may then be exactly the opposite of what was intended when controls were put in place. (See Thibodeau, 1981, for example.)

Effects generally depend on the specific form of rent control imposed. For example, the supply of rental housing may be not so much suppressed, as driven "underground." Small scale landlords continue to develop units and use such mechanisms as "key money" to collect market rents. In Cairo, for
example, key money payments may be six to seven times the annual legal rent for a controlled dwelling (Malpezzi, 1986).

The experience in a Bank-sponsored project in Mauritius may illustrate a similar effect. Here, individual real estate entrepreneurs can develop more units but are restricted in the prices they can charge. Nevertheless, Bank staff have observed that small scale rental development is widespread. Demand for loans to low income households, under the Bank's initial urban project (now in supervision), has been substantially higher than expected, an indication perhaps of the value or equity built up by lower income households "locked" into their current accommodation by the advantages of long tenure under rent control. This accumulated economic advantage, which may be difficult to overcome when such factors as increasing household size would otherwise encourage a move, is a motivation for owners and renters to invest in physical improvements.

A study of the impact of rent control in New York City, however, found a clear decline in supply (Moorhouse 1983):

- There was an unambiguous decline in the quality of housing available under rent control, including an increase in crowding;
- Reduced tenant turnover and vacancy rates occurred, and were linked with higher search costs and higher relative prices for better quality;
- Landlords were able to trim maintenance and operating costs as a strategy for maintaining their return on invested capital;

In spite of the evidence that housing supply -- and consumers as well -- are hurt by imposition and maintenance of rent controls, control persists in many markets. Of course, as opponents of rent control point out, the motivations for adopting rent controls may have less to do with the welfare of renters than with political expediency (Kochanowski, 1980; Drier, 1979).

In Mauritius, for example, the Bank has been working to encourage a review and reconsideration of the rental situation and of the controlling Landlord and Tenant Act. However, the government has apparently had little motivation to move rapidly on this reconsideration, not a surprising situation given that a majority of the urban population are housed in rent-controlled dwellings.

4.3 The Effects of Depreciation and Maintenance

While there are arguments to the contrary, particularly with respect to groups in higher income levels, the weight of evidence seems to support a conclusion that buildings which incorporate owner-occupied dwellings are better maintained than those which do not. One major reason for this situation is that the owner-occupant typically values the time spent on maintenance activities at below-market rates (O'Hare, 1981; Galster, 1983). Besides the welfare benefits for owner-occupants themselves, this observation implies that renters in units auxiliary to owner-occupied dwellings may

These benefits may include lower relative housing price as well as better
quality. Because of the relatively high proportion of fixed costs in ownership, current revenue (rents charged) and turnover are the two principal variables influencing return on investments in rental housing. The small scale landlord, in contrast to the large scale operator, is generally found to be a turnover minimizer rather than a revenue maximizer (Downs, 1979). This would suggest that producers/managers of informal units would be more likely to maintain constant rents, even with otherwise general inflation.

The likelihood that major maintenance activities, including complete structural rehabilitation, will be undertaken (by both absentee landlords and owner-occupants) are significantly influenced by neighborhood characteristics, which seem to affect psychological and economic willingness to upgrade. Better neighborhood characteristics may suggest less risk in the maintenance/upgrade investment. The complexity of factors influencing the rate of economic depreciation (see Malpezzi, et al., in press) makes it difficult to forecast in general whether maintenance expenditures are warranted by economic factors.

In any case, the landlord’s or owner-occupant’s stated willingness to upgrade is not directly related to income, and thus appears to be a more important factor than economic resources in predicting where major maintenance will occur (Mayer, 1981; Strassmann, 1984). Strassmann found that this willingness was strongly influenced by installation of infrastructure: The rate of improvement in his study areas doubled when access to infrastructure services was provided. This observation has important policy implications for Bank-sponsored projects.
Figure 8.
Relationship of Availability of Piped Water and Rental Tenure, Urban Sector of Selected Developing Countries (data from Table 1)
5. DOES SUPPORTING OWNERSHIP YIELD REAL ADVANTAGES

Two major points can be drawn from the preceding discussion: First, there is likely to be a definite and substantial demand for rental housing in those countries in which the Bank is active. Second, in the absence of policies discriminating against the supply of rental housing, much of this demand is met through existing private sector supply mechanisms, particularly small scale developers of auxiliary units and other forms of informal rentals.

In most areas of economic activity, it probably would be considered obvious that suppressing supply in a major segment of a market in which there is substantial demand will lead to inefficiencies and foregone economic and social benefits. But because rental housing is viewed negatively by policymakers it is a special case; ridding the sector of the evils epitomized by "landlordism" is felt to be worth the costs. The evidence suggests these evils generally are not real. To the contrary, renters -- particularly in lower income groups -- may realize a variety of benefits relative to homeowners.

Ozanne and Struyk (1976) are perhaps most direct in their assessment of the issue. Their research on U.S. data led them to conclude the following:

If one controls . . . for differences in the characteristics of occupants and neighborhood condition, the advantages of owner-occupancy (in dwelling condition) largely vanish. This suggests only small differences in the 'efficiency' of owner-occupants as producers . . . . The superior level of housing services associated with owner occupancy results to an important degree from the larger units and better neighborhoods they inhabit . . . . Owner occupants are demanding more housing and related services than comparable renters, and they maintain this housing at rates at least equivalent to landlords in similar circumstances (p. 55).

The small scale landlord, in particular, is sensitive to his inability, perceived or actual, to have substantial influence on rent level, and so maximizes his return by assuring a steady rent owner-occupied rental housing, would presumably increase individual security of tenure as well as overall neighborhood stability, calling into question one of the primary advantages attributed to ownership as compared to rental (Sweeney, 1974, for example).

Also contrary to frequently held biases, Figure 8 illustrates that in many areas there is a positive correlation between a large rental market and market nad acces piped water. This relationship, not surprising if rentals are the market's response to constrained access to land, is observed.
Figure 9.
Relative likelihood of access to piped water for renters as compared to owners for selected cities.

Notes: Income groups represent increasing household incomes in equal percentage groups. Likelihood ratio is ratio of percentage of renters with piped water to percentage of owners with piped water.
Figure 10.
Relative likelihood of access to piped water for renters as compared to owners for selected cities.

Notes: Tenure groups represent increasing length of tenure, in equal percentage groups. Likelihood ratio is ratio of percentage of renters to percentage of owners, in group with access to piped water.
regardless of income levels and length of tenure, although lower income households may actually do better than those of higher income. (See Figures 9 and 10.) It would appear that satisfying the demand for rental housing can deliver access to piped water to more households, and sooner.

Figure 11 illustrates the lack of apparent correlation between average conditions of crowding land tenure in a number of cities, in spite of the previously discussed correlations among household sizes, incomes, and tenure. In terms of this measure too, renters simply are no worse off than owners.

This observation has further significance. Since renters demand less space than owner-occupants, supply responds by producing smaller dwellings. Average dwelling size declines as rentals' share of the market increases. (See Figure 12.) Densities are observed to be higher in areas with a substantial proportion of rentals, so that a similar relationship between aggregate housing densities and rental market might be expected. The amount of land and structure required to accommodate rental households is less than that required for a similar number of owner households. Infrastructure networks will be reduced in proportion to increasing densities in areas with substantial rental housing.

Certainly, one must be wary of averages. Even in the work by Ozanne and Struyk the results were not entirely uniform. The conditions observed for very low income households -- the bottom 5-10 percent -- led to a conclusion that owner-occupancy in the U.S. did perhaps bring improvements in housing quality at given costs, and that overall supply efficiency might be improved if the lowest income households could be induced to become owners.

While others have drawn similar conclusions (Galster, 1983), such work has been performed in the U.S., where the bias toward homeownership has already been noted. It is unclear whether similar results would be found in developing countries, where the lowest twenty percent of the population, on income, is judged "unreachable" by conventional ownership programs but are often accommodated in rental housing.

In Kenya, for example, allottees in site and services areas of the Bank-sponsored Second Urban Project were explicitly allowed to rent rooms. Although affordability calculations did not reflect additional income from rents, the potential extension of project access to perhaps an additional 5-10 percent of urban families, due to the impact of this added income on affordability, was clearly presented in the appraisal report. The report observed also that development of auxiliary space was widespread in the Bank's first Kenya urban project. Appraisal of the third urban loan, the Secondary Towns Project, was less direct in its recognition of rentals, but introduced extensive servicing of land held privately by speculative developers and cooperative organizations, with no subsequent deterrents to development of rental housing.
Figure 11.
Relationship of Crowding of Dwelling and Rental Tenure, Urban Sector of Selected Developing Countries
(data from Table 1)
Figure 12.
Relationship of Rental Tenure and Average Dwelling Size,
Urban Sector of Selected Developing Countries
(data from Table 1)
6. THERE ARE OPPORTUNITIES TO BE CAPTURED

The World Bank's urban programs have focused on making home-ownership possible for a broader range of people. With exceptions -- most notably that of Kenya -- rental housing has for the most part received little explicit attention, although subletting and auxiliary space have in recent years been at least implicitly accepted in planning of most Bank-sponsored urban projects.

These programs have achieved substantial successes, and the emphasis on homeownership may well have been appropriate and necessary to the achievement of these successes. But a major share of the housing market -- rental housing -- has in many countries been neglected or actively discouraged. As the evidence presented here has shown, there are good reasons for taking a more balanced approach to the role of rental housing:

- There is a clear demand for rental housing, which can account for one-quarter to two-thirds of the market overall, and a much higher proportion of lower income households.

- Contrary to widely held biases, rental housing appears in a number of cases examined here to bring equal or better quality of housing to its occupants, and sooner, when compared to owner-occupied dwellings, and is not selected simply because renters have no choice.

- Demand for rentals is met with smaller units, denser development, and with possibly greater private sector participation (through small scale development of auxiliary space), than comparable numbers of owner-occupied dwellings. The limited resources of the Bank and its clients can achieve greater leverage in increasing total housing supplies if rental development is given even treatment in housing policy and project development.

This preliminary review of the issues shows there are opportunities to be captured through increased attention to rental housing: opportunities for mobilizing resources and increasing total housing supply; opportunities for improving efficiency of resource utilization and cost recovery.

6.1 Resource Mobilization and Housing Supply

In a free market setting, commercial rental housing can provide an attractive return to medium and large scale investors. Their investment in housing then makes it possible for small-scale entrepreneurs to obtain adequate accommodation while keeping their limited capital resources free for income- and job-producing activities. The rent premium paid in El Salvador and other countries for dwelling units with direct street access -- and subsequent opportunity to establish a business -- demonstrates the value of the situation to the tenant.

The tenant gains flexibility in managing his limited capital. The banker sees a household's liquid capital holdings in three primary categories: transaction cash used for day-to-day expenditures, precautionary cash held in reserve for emergency needs, and speculative cash available for investment. Mobilizing precautionary cash is the principal focus of traditional housing finance strategies (Chretien, 1985).
Lower income households will have very limited opportunity to distinguish between precautionary and speculative cash. Community savings and self-help schemes which exist in many countries (Kaufmann and Bamberger, 1985) allow participating households to make small contributions, compatible with income, but to draw on the larger funds accumulation if a sudden need arises. The combination savings and insurance provided may then be a mechanism for permitting the household to increase its allocations to speculative cash by reducing its need for precautionary funds.

Availability of an adequate supply of rental housing reduces the levels of "key money" and similar demands which housing expenditures make on the speculative cash reserves. In Seoul, where the developer of an auxiliary unit is frequently able to exact "key money" from his prospective tenant, in advance of construction, the renter is forced to invest in housing, at levels which may approach twice his annual household income.

The competition for capital is illustrated in Table 4, which shows statistics from Nigeria during the mid-1970's. With the formal financial sector virtually non-existent, personal effort and family loans together provided financing for over 80 percent of landlords surveyed. The same of low income businesses. In such a situation increased supply of formal sector financing would presumably serve well either the housing sector or the small scale businessmen. If one can expect that average loan size might be greater and loss associated with mortgage-secured loans might be lower for lending for rental housing development, as compared to small scale business, efficiencies of lending would be much greater if formal lending were devoted to housing. Additional informal funds might then be shifted to the business sector. On the other hand, when formal financial schemes are set up, small scale savers are more likely to be able to take advantage of schemes aimed at lending for small business or limited home improvements, because the sums involved are smaller than are required for home purchase. The ability of the financial institution to lend funds to the same population from which its depositors are drawn is a recognized element of success in mobilizing the resources of small savers (Vogel and Burkett, undated). There may then be advantages to be gained by considering programs aimed at mobilizing small-scale savers' funds for investment in small-scale rental housing. A strong rental sub-sector then can offer intermediation for both large-and small-scale capital investments.

6.2 Resource Utilization and Cost Recovery

Regardless of the sources of funds for housing, satisfying the demand for rentals can make these funds go further. The increased density associated with development of rental housing effectively reduces overall project standards, particularly with respect to increased utilization of infrastructure. However, the reduction is somewhat obscured, since the design standards are stated with respect to the planned ownership of plots and dwellings, and thus on cursory inspection may appear unchanged. The reduction may then be politically more acceptable, as the apparent general acceptance that partial sublets will occur and will be permitted in Bank-sponsored project areas demonstrates.

Subletting increases the number of households accommodated in a project area and thereby represents an increase in housing supply, achieved in the rental subsector. Perhaps more importantly, this increase is achieved at a
cost affordable to a larger fraction of the population than would otherwise be possible, as experience in El Salvador and Kenya demonstrate. Households renting these auxiliary units are offered accommodation which might otherwise be unavailable. Households choosing to own are enabled to do so by the supplemental income received from tenants. High premiums paid for ownership—perhaps expressing consumer preferences but being accompanied by limited net social benefits (Struyk, 1977 (1))—are then converted more effectively and directly from consumer savings to housing investment.

Another aspect of this conversion is a shifting of the balance of the public-private partnership toward the private sector. In the informal sector, property owners construct auxiliary rental dwelling units as well as their own dwelling, although total space constructed may increase less than the number of (presumably smaller) dwelling units. In the formal sector, private developers may be able to take responsibility for land preparation and financing of larger scale and largely rental housing developments. In both cases, for a given number of households to be served, more public sector resources can be devoted to infrastructure.

In some countries, private sector institutions appear to be able and ready to undertake large scale development of lower cost housing for rent and sale. In Kenya, for example, large blocks of land are held by private entities which could function as developers. There has apparently been some success in packaging land for private development in Tunisia, and the El Salvador experience, in which a not-for-profit cooperative was the administrative agency, may be a useful prototype for organization. The principal difference from prior projects would be an explicit recognition that a major proportion of the housing may be rented and solicitation of private sector funds to finance the construction of units for rent.

Experience in El Salvador suggests that the stream of rental income which improves affordability can improve cost recovery as well. Collections were reported to be quite good in the Bank-sponsored project. In Burundi, a "rental tax" (a property tax on the imputed value of site and structure, assuming full occupancy, and graduated to encourage structural improvements relative to expansions of area) was designed to be a major element of the cost recovery mechanisms for the project, and while no statistics are available on the rate of development of annex units in Kwijabe, steadily increasing receipts of the "rental tax" suggest that such units are doing well.
Table 4: Sources of Finance for Urban Activities in Nigeria

**SOURCES OF HOUSING FINANCE CITED BY SURVEYED LANDLORDS**

<table>
<thead>
<tr>
<th>Sources of Finance</th>
<th>Percent of Sample Citing Source of Finance</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>Gongola</td>
</tr>
<tr>
<td>Building Society Loan</td>
<td>0</td>
</tr>
<tr>
<td>Bank Loan</td>
<td>0</td>
</tr>
<tr>
<td>Loan from Employer</td>
<td>1</td>
</tr>
<tr>
<td>Family Loan</td>
<td>1</td>
</tr>
<tr>
<td>Personal Effort</td>
<td>99</td>
</tr>
</tbody>
</table>

**SOURCES OF CAPITAL FOR LOW INCOME BUSINESSES**

<table>
<thead>
<tr>
<th>Source of Capital</th>
<th>Street Traders (percentage)</th>
<th>Shop Traders (percentage)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Personal Savings</td>
<td>61.6</td>
<td>64.7</td>
</tr>
<tr>
<td>Parents</td>
<td>18.1</td>
<td>11.8</td>
</tr>
<tr>
<td>Husband</td>
<td>14.4</td>
<td>16.9</td>
</tr>
<tr>
<td>Loan from Bank</td>
<td>-</td>
<td>1.5</td>
</tr>
<tr>
<td>Other</td>
<td>2.9</td>
<td>5.0</td>
</tr>
<tr>
<td>Total</td>
<td>100.0</td>
<td>99.9</td>
</tr>
</tbody>
</table>

7. THE RECOMMENDATION: STRATEGY WITH MORE BALANCED ROLE FOR RENTAL HOUSING

The basic point to be made here is that rental housing has a valid and beneficial role to play in any urban area and particularly in many cities of the developing world. Public policies which discourage production and suppress the rental housing market are not only unjustified by a supposed oppressed status of renters but are likely to have counterproductive impact on the housing market in general. Action is warranted to encourage a more balanced approach toward urban housing, particularly in Bank-sponsored programs.

In general terms, development and maintenance of an effective housing sector requires attention to several functional components or inputs which combine to deliver housing goods and services:

- Land
- Capital and financing
- Infrastructure and construction
- Tenure and property development and use rights
- Policy development and sponsorship

A balanced treatment of rental and ownership housing will require attention to each of these components or inputs.

7.1 Land

1. As part of the Bank’s continuing programs to rationalize patterns of land tenure and management, efforts should be made to assure that Bank-sponsored property assembly, subdivisions and ownership instruments in no way discriminate against rental housing or against development of land to maximum market densities.

2. Efforts should continue in design and development of Bank-sponsored urban projects to assure that appropriate subletting, subdivisions of structures, and construction of auxiliary units for rent are not discouraged in purchase and tenure agreements. Wherever possible, statements of policy permitting and encouraging such rental development should be explicitly made.

3. Further efforts should be made, in countries where institutional and entrepreneurial resources are appropriate, to permit release of land in blocks to developers, for construction of housing for rent or resale. In these cases, government effort should continue to be focused on supply of major infrastructure, with plot development and dwelling construction left to private developers.

7.2 Capital and Financing

4. Where Bank-sponsored housing finance and savings bank schemes are developed, efforts should be made to assure that small scale participants can be attracted, and in particular that lending for development of small scale rental properties is not discouraged.
5. Continuing support should be given to programs which encourage incremental development and upgrading of dwellings, so long as there is no discrimination against subletting. Where market conditions are appropriate, rentals should be actively encouraged.

7.3 Infrastructure and Construction

6. Standards of affordability should continue to be set to reflect the practices of subletting and development of auxiliary units generally extant in target markets for Bank-sponsored projects. To the extent politically feasible, these standards should be explicitly stated in project documentation.

7. The practice of setting infrastructure standards in Bank-sponsored projects to accommodate development to maximum market densities should be continued. Efforts must be made to assure that networks are not sized to standards based on strict affordability of single-family owner-occupied households, in those projects where clear recognition of auxiliary rentals is inappropriate. The strategy should be made explicit wherever possible.

8. Continued emphasis should be placed on extending infrastructure to serve the greatest area possible, and to encourage directly the subsequent development and upgrading of dwellings in newly served areas.

7.4 Tenure and Property Development and Use Rights

9. While 100 percent subletting of dwellings in Bank-sponsored projects may be due in part to implicit price subsidies, it should be recognized that subletting is a valuable element of project planning. Administrative resources should not be diverted in attempts to control subletting.

10. In those countries where current government policies and practices—such as rent control or restrictive zoning—discriminate against rental housing, the Bank should continue to expand its efforts to have these policies changed. Short term and highly directed policy studies and research to identify the degree to which these policies and practices foster inefficiencies and inequities in the housing sector of that particular country may be warranted, to support discussions with responsible officials, on why such changes are needed.

7.5 Policy Development and Sponsorship

11. In view of its role as a research and training institution, the Bank should undertake a conscious program to document and present the relative merits of rental housing and to encourage balanced consideration of rental housing in reviews of national housing policies.

12. In particular, research on the following questions could yield valuable policy insights:
Demand
 o What role does rental housing play in integrating new immigrants into the urban community?
 o How do family and other social relationships influence characteristics preferred in selection and occupancy of rental accommodations?

Supply
 o Do family and other social relationships unique to particular city or country significantly influence the rate of development of auxiliary units and growth in density within Bank-sponsored and similarly formulated projects?
 o Does firm tenure encourage faster growth in numbers of dwellings where subletting and construction of auxiliary space have occurred?
 o What are the principal sources of finance for rental housing and particularly for development of auxiliary space in Bank-sponsored and similarly formulated projects?
 o What are the real rates of return on investment in rental housing, and what factors influence these rates in different countries and under various market conditions?

The evidence is strong that more balanced support of rental housing would be beneficial, both to Bank programs and to the lower income populations served by Bank-sponsored development activities. While there are still questions for research, observations in cities from Cairo to Seoul, from Bogota to Manila, and Bank experience from Burundi to El Salvador demonstrate not only that rentals are widespread, but that an active rental subsector can bring the benefits of improved living conditions to large numbers of households.
REFERENCES


