

What is Rent-to-Own (RTO) and How Does It Work?

By Ku Nur Ilyani Binti Ku Abd Aziz | 6 April 2020



The rent-to-own (RTO) scheme is a new concept in Malaysia that was introduced a couple of years ago to make owning property more affordable for more Malaysians. This scheme is relatively little known in Malaysia but has been around overseas for decades.

A rent-to-own agreement allows the buyer the option to buy the rental property at a future date. In the meantime, the buyer is also a renter for the property and makes regular payments to the seller. It does not require the hefty down payment associated with buying a house outright.

Concisely, those looking to buy a property enter into a lease which is a contract between the developer and the potential buyer that requires a certain length of time which the buyer will first rent the home. At the end of this contract, you can exercise the option to purchase the property.

The scheme works through a lease agreement that gives you the option to end with a sale or, to put it more simply, you can try before you buy!

Are Rent-to-Own Schemes The Answer To Easier Home Ownership?

The major reason why RTO schemes were made available is due to the down payment issue. It intends to fill the gap of the down payment and all other related fees to own a house. If you are looking for an option that provides you with a property that you can call your own but without having to save tens of thousands of ringgit to secure a property, then RTO could be the way. Economist Lee Heng Guie, Executive Director at Socio-Economic Research Centre (SERC) said renting a house may be a wise move for young working adults or young families as it allows more flexibility, less financial commitment and less investment than buying a property.

Besides, the RTO scheme also fills the gap that involves the aspect of "trust". As we know, the potential buyer will only get loan approval from the bank if the bank is confident about the borrowing repayment. Therefore, potential buyers must prove they have sound credit ratings. With the RTO option, tenants have the opportunity to show the bank that they can pay their rental (mortgage) on a continuous basis without lapsing. This helps build their credit trustworthiness with the bank. If the buyer is able to pay rent without fail for two to five years for example, it is quite safe for the bank to assume that the buyer can continue to pay for the home they buy after the monthly rental becomes a monthly mortgage.

The next gap is the "better buy now" mentality. There is some merit to this way of thinking because the cost of constructing a home increases with time. Thus, buyers who take the RTO route today would secure the property price at today's price instead of trying to save faster than the rate that the property price increases.

Who Can Adopt The Rent-To-Own Scheme?

Just about anyone who meets the criteria, can use Malaysia's various rent-to-own schemes if they are unable (or unwilling) to shell out a hefty down payment for buying a property.

The scheme is often found to be most suitable for young families and working professionals who do not have the earning power yet to qualify for housing loans.

Depending on which scheme you use, (Maybank's HouzKEY and PR1MA are two of the most popular) there are a few stipulations which interested candidates must meet. These can include being a Malaysian citizen, having the right number of guarantors from your family (i.e., someone who agrees to pay your rent for you if you are somehow unable to do so), and having a combined household income above a certain amount (usually around RM5,000 and above).



What Are The Advantages And Disadvantages Of Rent-To-Own Schemes?

Pros:

1. More affordable housing

The reason RTO schemes exist is to help lower-income families get into the property market, even if they do not have the down payment to purchase a house, or if they do not qualify for housing loans from banks.

2. You get to 'try it out' before you commit

Able to stay in the property before deciding on property purchase decision. This gives buyers the chance to check out the neighbourhood, expose any potential issues with the property, and see whether it is a property that suits their needs (in the long-term).

3. Smart buyers can lock in a good price

RTO schemes allow buyers to lock in the purchase price of a property based on the current value. This means, when they decide to make the purchase, the sale price does not change, even if the property's market value is higher over the years.

Cons:

1. You still do not actually 'own' the property during the lease

During rent-to-own, the buyers are not the owner of the property until a sale has taken place, which means if their lease term is 10 years, for example, they cannot renovate or make any changes without the owner's approval.

2. Missed payments are dangerous

In RTO schemes, buyers are locked into long lease periods. If in default, it will cause the buyers to lose the house and suffer a lot of debt.

3. If property prices do drop, you might not benefit from this scheme

The price of the property will be locked at the current value, if property prices suddenly or unexpectedly drop, buyers will not be able to buy at the cheaper rate because they will have to buy at the price that was originally agreed to.

Summary

Industry experts and observers suggest that renting may not be a bad thing and could in fact assist some people to eventually own their own home if it is done in a systematic way, such as in the form of a RTO scheme. If more state governments or agencies play their roles and move in the same direction to promote RTO schemes, it could encourage home-ownership. On the other hand, 10% down payment to purchase a house will also be an issue for most young buyers and if there is any RTO scheme offered, it will help to lessen their burden of owning their first home.

At the end of the day, it comes down to personal preference, and what you are financially capable of. Although it is widely considered as the answer to home ownership for many Malaysians, there are a few things to consider when deciding if RTO is for you or not because these leasing agreements and transactions can be complicated, and if you are not careful, you could find yourself in some really sticky situations. Therefore, before you enter into any RTO agreement, make sure you have done your research and have spoken to real estate professionals who can help ensure you get the best value for you and your family.

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Ku Nur Ilyani Binti Ku Abd Aziz is a lecturer from the Department of Commerce and Accountancy at Faculty of Business and Finance, Universiti Tunku Abdul Rahman (UTAR). To contact her, email: nurilyani@utar.edu.my

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 UTAR Sungai Long Campus
Jalan Sungai Long
Bandar Sungai Long, Cheras
43000 Kajang, Selangor Darul Ehsan

 cccd@utar.edu.my

 cccd.utar.edu.my

UTAR Kampar Campus
Heritage Hall, First Floor
Jalan Universiti, Bandar Barat
31900 Kampar, Perak Darul Ridzuan

