

# Property Valuation in Ghana: Constraints and Contradictions

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**Key words:** Property values, valuation methods, constraints, contradictions

## SUMMARY

Property valuation is carried out in Ghana for various purposes such as for insurance, payment of compensation for state acquired lands, taxation, rent/lease, sale and mortgages among others. It has been recognized over the years that property valuations in Ghana for the various purposes is fraught with a lot of constraining factors, conditions and contradictions which often distort estimated values. Although in all these the methods of valuation are accordingly applied, it has been found that the open market value on which property value is assessed is affected by some constraints from the characteristics of the landed property and the property market. These constraints are lack of adequate data, dearth of knowledge of the property market, and a property market which is not well developed and mostly informal. It also includes high inflation and interest rates which also affect values, and difficulty in determining the interest/right in the property being valued due to conditions of land tenure. In the light of this, the paper discusses these constraining factors, conditions and contradictions which play an important role in the use of the open market value in valuation for the various purposes and how it affects property values in Ghana. The study reveals that due to these constraints and contradictions in property valuations, values are distorted and not a true reflection of what persists on the open (property) market. This also has some effect on policy decisions, investments, development of a viable property market and sustainable economic development.

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## 1. INTRODUCTION

Property valuation may be described as the carefully considered estimate of the worth of landed property based on experience and judgment by identifying and assessing characteristics of a given property. A valuer is called upon to give his or her opinion on the value of many differing types of interest in many different types of property for many different kinds of purposes. Each appraisal of the value for the various purposes therefore requires the consideration of different factors to form a basis for the valuation. The key to the accuracy of opinion is the knowledge of the factors that affect or contribute to the determination of the property value. This is based on what prices have been obtained recently for similar properties with which comparison can be made. The evidence on which such an informed opinion is based is very important in arriving at an appropriate property value. Although, the methods of valuation differ significantly, underlying each of them is the need to make comparisons since this is the essential ingredient in arriving at a market view (Britton *et al.*, 1980).

Property valuation is carried out in Ghana for various purposes such as for insurance, payment of compensation for state acquired lands, taxation, rent/lease, sale and mortgages among others. In all this though different methods are applied, the open market value important for arriving at an appropriate value on which to base decisions is influenced by a lot of other factors and conditions. These factors influence the valuations in addition to its purpose, use, location, physical state, tenure and time. The open market value has been defined as ‘the estimated amount for which a property should exchange on the date of valuation between a willing buyer and a willing seller in an arm’s-length transaction after proper marketing wherein the parties had each acted knowledgeably, prudently and without compulsion’ (RICS, 2003). The estimated amount in the definition is further explained to be a price expressed in terms of money (normally in the local currency) payable for the property in an arm’s- length market transaction. This estimate specifically excludes an estimated price inflated or deflated by special terms or circumstances such as a typical financing, sale and leaseback arrangement, special considerations or concessions granted by anyone associated with the sale, or any element of special value.

Some of the constraints on the use of the open market value to be discussed are however a more complex form of the above factors normally considered in valuations. It has been recognized over the years that these factors significantly affect the methods of valuations applied for the various purposes. Property valuations are therefore usually distorted and not a true reflection of what would be an open market value. These constraints include high inflation and interest rates, difficulty in determining interest in the property being valued due to the land tenure systems, social behaviors, dearth of knowledge of the property market, an informal property market and lack of adequate data. Until now real estate appraisers have

assessed real estate based on their intuition or experiences due to these constraints. The basis of valuation that is widely adopted is the open market value basis using the comparative method.

Now that the concern with securitization of real estate is brought to attention, the technique of appraising it more quantitatively and accurately is required (Tanaka *et al*, 2001). In view of this, though valuations cannot dictate the market; it's up to the players; sellers and buyers a properly organized valuation system is needed for a well developed property market. In addition, an adequate and reliable information on values is important for trading in properties and to provide support for capital investments.

This paper in the light of this focuses on an examination of the factors and conditions which are a constraint on the use of the open market value method of property valuation in Ghana for the various purposes. It will discuss these factors and conditions and examine how they affect property valuation and lead to contradictions in property appraisals. The paper will also briefly look at the effects of these constraints and contradictions on property values on capital investment, policy decisions and economic development.

## **2. GENERAL PERSPECTIVE ON PROPERTY VALUATION**

The pricing of real estate has been studied extensively since the early 1980s using a variety of methods (Din *et al*, 2001). The purpose of valuation is however, to determine 'value', a term generally prefaced by some description such as market value or benefit value. The determination of a property value depends on a number of physical and economic characteristics which must be taken into consideration very carefully in a property valuation procedure. Some of these characteristics are intrinsic to the property; others are external or environmental factors. These factors can be determined in an objective way but there is always a certain degree of subjectivity that is difficult to measure in valuation process (Yomralioglu, 1993a).

There are also many property market characteristics that make valuation a difficult and often subjective task that is dependent on a high degree of experience and local knowledge, example are the heterogeneity of each interest, economic influences at national, regional and local scales and social factors. This is the state of the environment for property valuations in Ghana. These market characteristics which play a major role in property valuation cannot be altered and indeed make valuation a challenging profession. However, it would be seem prudent to minimize valuation complexity by improving data accessibility and dissemination (Wyatt, 1995).

Valuations are often based on the open market value and this requires adequate records of transactions (Wyatt, 1997) but appraisers are often unable to gather adequate information on comparable properties due to commercial secrecy, a lack of data, real estate tax system and adhoc information dissemination. Besides, a property can have an emotional or cultural value, just as a work of art has, for example, because the landscape embodies defining cultural values or because of the association of a location with a particular event or person. This can

lead to an individual being more than willing to purchase a particular property and fetch a price that is greatly in excess of their value in production. The price determination for a property is therefore influenced by all these factors and property valuation is the process of identifying and quantifying these 'value factors'. The result should be an informed opinion of value based on the assessment of those factors considered relevant to the value of the subject property.

Real estate/property is one of the central commodities in any economy and as such is subject to far more influences on its value. The combination of the importance of it to an economy and the complexity of its relation with the economy as a whole has led to the need for an equally complex and sophisticated set of tools for assessing its value (Dent, 2000). Real estate can be evaluated under four main headings namely use, location, structural quality and legal ownership and these can be broken down further into smaller components. Use for example can be broken into various categories such as agricultural, industrial, offices, residential, retail, leisure and warehouse. Each of these categories comes with its own determining factors which all contribute to the value of a property. The market value of any real property for example depends in part on its location. The identification and accurate description of the property units and their relation to neighboring properties is essential as much as the environment within which it is located. Also important is a clear definition of what is being valued which relates to the ownership rights subsisting on the property. In most valuations carried out in Ghana, this is an important factor because of the communal land tenure system and the family/social relationships which results in a complexity of ownership rights.

Real property may be viewed from different perspectives. For an ordinary person, it is a place of habitation, for the investor, a capitalization of assets, for the economist, an economic commodity necessary for production, and a lawyer, a set of real property rights. Others may see it as part of nationhood and cultural heritage (ECE, 2004). In Ghana, it should be recognized that other factors outside those above mentioned also play an important role and because they are not easily quantified are a constraint on property valuation.

According to Dale (2000), valuation is one of the essential pillars of a property market. It is therefore necessary for the full exploitation of capital generation through investments in land resources for economic development. He also states that for the element of valuation to contribute effectively to a functional land/property market it must be clear and well understood, based on market prices, accepted and used as a basis for calculation of asset values, provide a clear mechanism for offering real property for sale, support and make available mortgage advice and provide quality data. Therefore the need for a well structured property valuation system to stimulate capital investment for economic growth cannot be over emphasized.

### **3. CONSTRAINING FACTORS AND CONDITIONS ON PROPERTY VALUATION IN GHANA**

The underlying factors that are constraints on the determination of property values in Ghana are now examined.

#### **3.1 Lack of Adequate Data**

One main factor which is a constraint in the use of the open market value is the lack of data. This constraint is a problem which cuts across the use of all the methods. The structural mechanism for collating property data in the country is weak and does not provide adequate information on which a valuer can rely to make an informed opinion about property values. This makes it difficult to make critical analysis and achieve a sound base for valuations using the open market values. Apart from a few well established property firms and organizations who keep some form of data, it is difficult to find formally organized data for property valuation. Even then, data in these private sources are not formally kept and it is not easy to gain access to them due to commercial secrecy and the desire to protect clients in an emerging stable political and macroeconomic environment.

Besides this, the effect of social elements which form an important component of the value arrived at cannot be quantified but depends on the discretion of the valuer. This makes such data less reliable and subjective. Many valuations carried out therefore do not portray the true open market value of the property. The Land Valuation Board is the government institution mandated to collate research, manage and record all data on properties. From observations, the department has not been able to efficiently carry out this function. In any valuation and in the use of the methods of valuation, data is very important because although the methods differ significantly, underlying each of them is the need to make comparisons since this is the essential ingredient in arriving at a market view and without data, this comparison will not be possible. The lack of credible property data for valuation is therefore a constraint on the use of the open market value in property valuation.

#### **3.2 Lack of a Developed Property Market**

In Ghana, the property market in which the transfer of ownership rights concerning properties takes place is not well developed. Though there is free trading of properties, many are done informally and knowledge about the property market is limited and fragmented. There is no clear legal basis and policies on trading in properties. Buyers and sellers therefore act in their own way. Due to this, there is also no proper regulation of property values which are often subject to the whims of the people involved in the transactions and each property is to a large extent traded on its own merit under its particular circumstances. This especially holds true in the urban areas where most property owners aided or unaided by valuation professionals sell and determine their own terms and conditions without recourse to any established formal guideline on property values or valuation principles.

### **3.3 Influx of Unqualified Estate and Land Agents**

In recent times, the influx of untrained estate/land agents in the trading of properties has led to another constraining condition on property values. Though these agents are not qualified and do not understand the factors that are necessary to be considered to determine property values, to a large extent they are currently responsible for the marketing (buying and selling) of properties in Ghana. Their activities are having a negative effect on property valuation because they do not seek professional advice on the property's value but determine it themselves. In addition, due to the dearth of knowledge of the property market and lack of adequate data, they do not assess the property values based on any sound economic analysis. They also charge fees (commission) for their services based on the income to be derived or expended on the property and some inflate such values in order to increase their earnings regardless of the effect this might have on the general level of property values. The value of a lot of properties are therefore informally assessed and are not subject to any formal valuation principles. However, value from such transactions are used for comparison in valuations to determine the open market value of properties.

### **3.4 Variances in Demand**

Another factor which is a constraint in the valuation of properties is the current changes in the character and variation of demand for properties especially residential properties. Increasingly, citizens residing and employed outside the country because of the higher purchasing power of their foreign resources under the conviction of the estate/land agents part with large sums of money to purchase properties especially in the urban areas. Often the value of property is arbitrarily decided between the parties and the money paid for the property is not subject to any valuation method or principle. This has currently developed to such an extent that many properties both residential and commercial in priced areas now command values in foreign currencies (specifically dollars which are exchanged at rates high above the local currency). This leads to arbitrarily high capital and rental values for residential properties especially in the urban areas when such values are used as comparisons and basis of analysis in subsequent valuations.

### **3.5 High Inflation and Interest Rates**

In addition to the above are the high inflation rates which lead to unstable prices of products and buildings on the property market. This has created the tendency for property owners and the land/estate agents to quote high property values above what prevails on the open market without any economic analysis. This phenomenon results in an unstable property valuation environment making it difficult to determine with certainty the interest rate to adopt in valuations especially for investment purposes. Interest rates sometimes adopted in valuations are therefore not the result of a sound economic analysis but are reached arbitrarily. High inflation also causes an unstable cost of building materials and makes it difficult to analyse and use the cost method of valuations with any degree of certainty. Even when inflation and interest rates decline, it does not lead to a significant reduction on the cost of building material and property values on the property market because demand is high.

### **3.6 Social Factors**

Furthermore, another factor that plays a role is the social influences on property valuations. Social relations and influences such as prestige and fraternity have an impact on people's actions though it cannot be quantified in real monetary terms. This must however be taken into account in determining property values because they play an important role in the negotiations of such transactions in Ghana. The relationship between the parties in many cases greatly affects negotiation of the price/value of properties. Relationships can come in the form of family, school/class fraternity, colleague, friends, or tribal sentiments. The value of properties purchased under such circumstance is therefore not a true reflection of what persist on the open market, as the definition of open market value ignores a bid by a purchaser with special interest. This is because such 'value factors' are difficult to quantify and though they may be considered irrelevant to the value of the subject property, under these circumstances they have a great influence on it.

In addition, most people see the acquisition of properties especially for residential purposes as more of a prestige than an investment. The desire to acquire property is therefore not driven by investment but social recognition and a personal sense of satisfaction. This has resulted in the current situation whereby individuals once they become rich spend huge sums of money to build or acquire mansions in good locations of high value in the urban and rural areas which are either left empty or not used frequently. Furthermore, few people manage and protect their acquired properties as an investment capital though property values are always appreciating due to inflation, high demand and the shortfall in the supply of all types of properties.

### **3.7 Land Tenure Issues**

Land tenure under the communal landownership system is often difficult to determine and current conflicts of land ownership has led to unclear titles to land. Besides, though individual property rights are created now in communal lands due to the cumbersome process of land title registration, most ownership rights are not registered and do not have any legal recognition or backing. Even when such title to land is registered, it is not easy to be certain of its legality because of the uncertainties in the legal institution of land title registration. Most properties valued as a result of this do not have clear title. This becomes particularly difficult when valuation must be carried out for mortgages or compensation for land expropriated where the valuation for such purpose must be based on clear legal titles.

### **3.8 Other Factors**

Other factors which are a constraint on the use of the methods of valuation are inadequate knowledge of planning regulations and laws. This leads to a minimal recognition of planning laws on the value of properties though it should form an important aspect of it. In addition, a lack of an addressing system for properties in Ghana makes it difficult to properly identify and reference properties for valuation purpose when comparisons of similar properties are needed.

In the use of the comparative method of valuation, although the location of any property is unique it is often difficult to find similar properties in the neighborhood of the subject property to use for comparisons. It is therefore always necessary to compare properties from similar neighborhoods. In Ghana however, this is difficult to achieve because there are many variations in neighborhoods and many buildings are unique because they are constructed according to the taste and requirements of the owner and not according to a statutory building plan.

#### **4. CONTRADICTIONS**

Many of the contradictions that arise in property valuations in Ghana are the result of the above discussed factors. These contradictions are due to unrealistic property values due to the procedure by which property is assessed and valued informally by property owners and estate/land agents. Others are uncertain land tenure system, the frequent lack of legal title to land, and the character and influences of demand and supply on properties. This means some of the factors important to property valuations are not easy to quantify and this leads to a lot of subjectivity in valuations. This is further compounded by the lack of formal property data which can be relied on for comparison. This also results in a lot of complexities in property valuations, makes it difficult to develop a formal functioning property market and affect investments decisions necessary for fully harnessing capital resources for economic development.

One contradiction is the high values of property based on foreign currencies which have very high exchange rates to the local currency. An example is when residential properties are selling for between \$150,000 and \$500,000 in some suburbs of Accra and the exchange rate is \$1: GHC 9000. The creation of what is termed a “dollar market” where values are determined in this currency in a local property market is inappropriate because it leads to unrealistic and high property values. This has also resulted in a dual market which though unrelated are an influence on each other. Similarly, business requiring rental accommodation in prime areas also sometimes have to pay the rent in foreign currency rather than the local currency increasing their capital cost.

In addition, planning laws and regulations are often disregarded in property valuation though it also plays an important role. Furthermore, neighborhoods that are classified as first class and therefore commands high property values often do not have some basic urban facilities like developed roads and the necessary modern housing facilities according to international standards to merit it. This defeats the rationale behind the classification of properties for valuations and does not take into consideration the significant role of the neighborhood and location of the property to the valuation.

Furthermore, the lack of a sound basis for the choice of a capitalization rate for valuation defeats the investment purpose of the property valuation and does not portray the true reflection of yields from capital investment in properties.

Also the necessary ingredients for a solid basis for property rights and title to land on which to base property valuations are missing.

In all, it can be said some of what can be called the main elements of valuation such as planning regulations, legal interest, environment/location, defined property rights and data on similar properties for comparison do not receive enough important consideration in property valuation.

## **5. EFFECT ON INVESTMENTS AND CAPITAL GENERATION**

The effect of the constraints on property valuation are that the general legal controls to ensure transactional quality and general honesty which should be an important element in property valuation are not available. The principles to carry out property valuation are lost in the informality and under all the constraining factors and its effect on property valuation and the setup of a functional property market is hindering efficient capital mobilization for economic development.

These factors and conditions make property valuation more subjective than objective in Ghana and open market values obtained are not able to provide a sound basis for economic analysis but leads to an over-estimated capital investment sector. This also makes investments unattractive to investors both local and foreign due to the fact that a high percentage of the investment goes into the capital asset acquisition of land/buildings at a high value.

The current government through its policies and drive for local and direct foreign investment has created a 'golden age of business' to promote growth and investment in the private sector. This is however not yielding the required results as the current situation discourages inflow of capital from foreign sources. According to an FT's (Financial Times of London) exposé, the 'Golden Age of Business, ' proclaimed by President Kufuor (the current president of Ghana) upon assumption of office has 'failed to materialize as rapidly as many had hoped.' The reasons cited as accounting for the small foreign investment, in spite of our efforts, include 'high business costs and problems such as land tenure.' In addition, an uncertain and informal property market and values limits the creation of mortgage facilities to support property development and economic growth.

## **6. CONCLUSION**

As stated earlier, these conditions and factors which play a major role in property valuation cannot be altered and indeed make valuation a challenging profession. The price determination for an open market property value is therefore influenced by these factors. Property valuation is therefore not the result of an informed opinion of value based on the assessment of those factors considered relevant to the value of the subject property. However the combination of the importance and complexity of its relation with the economy as a whole requires the need for an equally complex and sophisticated set of tools for assessing property value.

It would therefore be prudent to minimize valuation complexity by improving data quality and accessibility and create a sound property data system to provide uniformity and clarity in the open market value for the property market. Some efforts are being made by the Ghana Institution of Surveyors to standardize and improve on the data quality through the establishment of data bank. This effort needs to be encouraged for a good interpretation and analysis of market data to draw meaningful valuation conclusions.

There is also the need to formalize the functions of the land/estate agents and provide them capacity building to play an effective role. Again, the Ghana Institution of Surveyors is making some efforts to bring this into effect. It will however need the appropriate support from the policy makers to bring this into being. Furthermore, a sound land registration system on which to base property rights and a structuring and formalizing of property valuation is important for reliable property values.

According to Wallace (1999) in a land administration system, ascribing values is an essential mechanism for making rational decisions about liabilities, risks and state intervention in land uses. In this view, there is the need to properly address the issue of property valuations in order to be able to harness capital resources for economic growth and development.

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## **BIOGRAPHICAL NOTES**

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