THE OPTIMAL CONVERSION BETWEEN JEONSEI TO MONTHLY-RENT WITH BORROWING CONSTRAINTS

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ABSTRACT

In the Korean housing market, it is a puzzle that jeonsei has been a dominant type of rent even though the conversion rate for jeonsei to monthly rent is much higher than the rate of savings account. In this study, we investigate the optimization problem of a lessor under a borrowing constraint who has an option to convert from jeonsei to monthly-rent and provide a semi-closed-form solution to the problem, showing that when the lessor is lack of liquidity, jeonsei contracts may channels fund from a lessee to a lessor as in private lending, that is, the borrowing constraint is one of the key solution to the fairly large market share of jeonsei contract with the high conversion rates for jeonsei to monthly rent. Furthermore, we showed that the lessor wishes to convert from jeonsei to monthly-rent later as the borrowing limit tightens, the jeonsei deposit amount increases, the rent rate decreases, the income rate increases, and the investment market becomes more profitable.