



Housing Policies in the UK, Switzerland and the US: Lessons Learned

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Outline



- Focus on three developed countries in Western world – **UK, Switzerland and US** – and explore each country's key housing policies and their merits and demerits
- Explore...
 1. **Current status of housing market** – main challenges and risks
 2. **Main housing policies** in UK, CH, and US – How do they work? & main objectives?
 3. **Merits and demerits** of key policies
 4. What are the **lessons learned**?

United Kingdom

(builds mainly on Hilber 2015 & Hilber and Vermeulen, *EJ*, forth.)



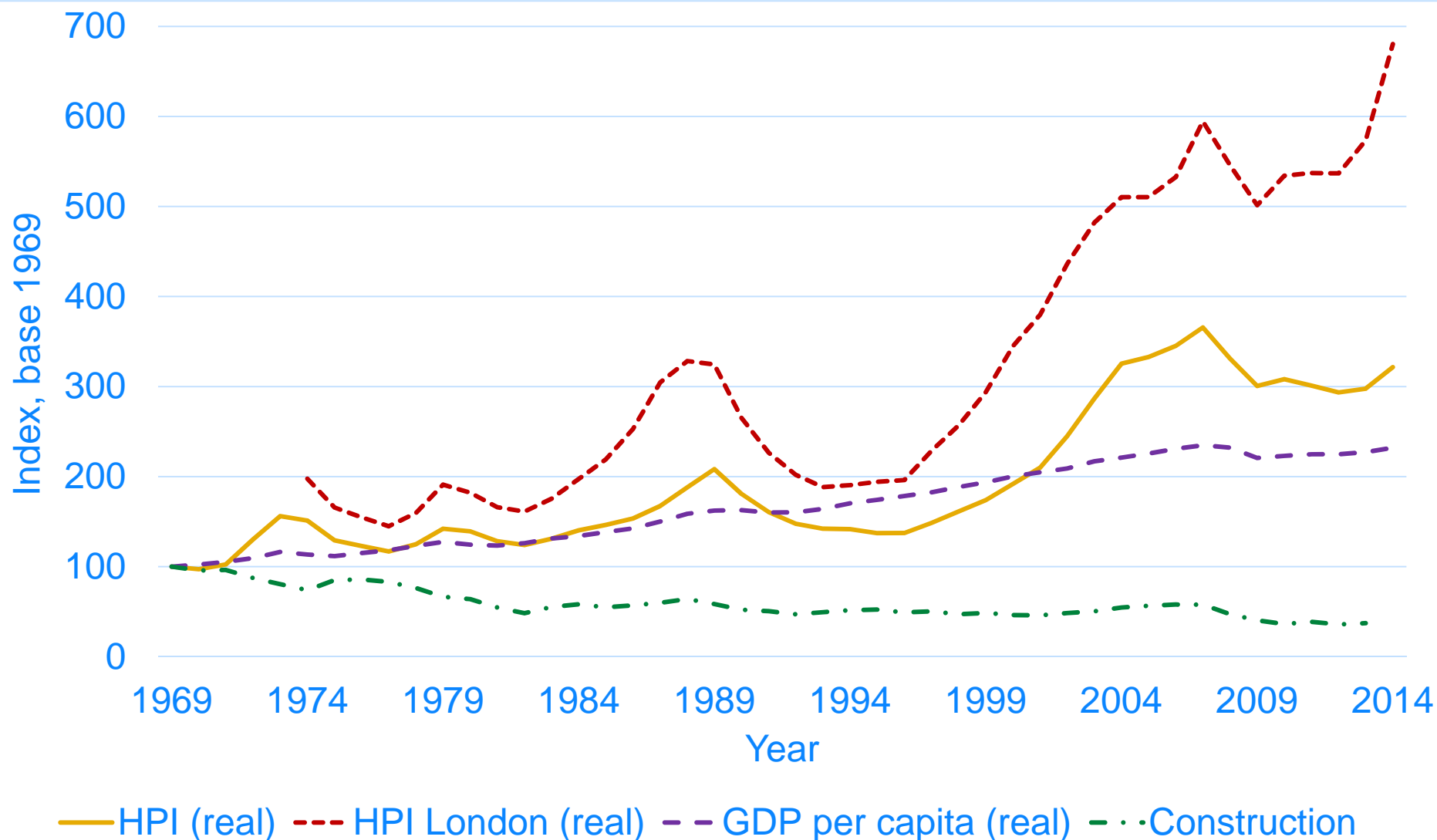
Current status of British housing market(s)

- **UK faces extreme housing affordability crisis**
 - ▶ House price per square meter 2nd highest in world (topped only by Monaco)
 - ▶ New built homes 38% and 40% smaller than in similarly densely populated NL and GER
 - ▶ Price to income multiple at record high
 - 5.0 UK & 8.5 London
 - ▶ Homeownership rate in decline since 2002
 - 69.3% (2002) to 63.5% (2013)

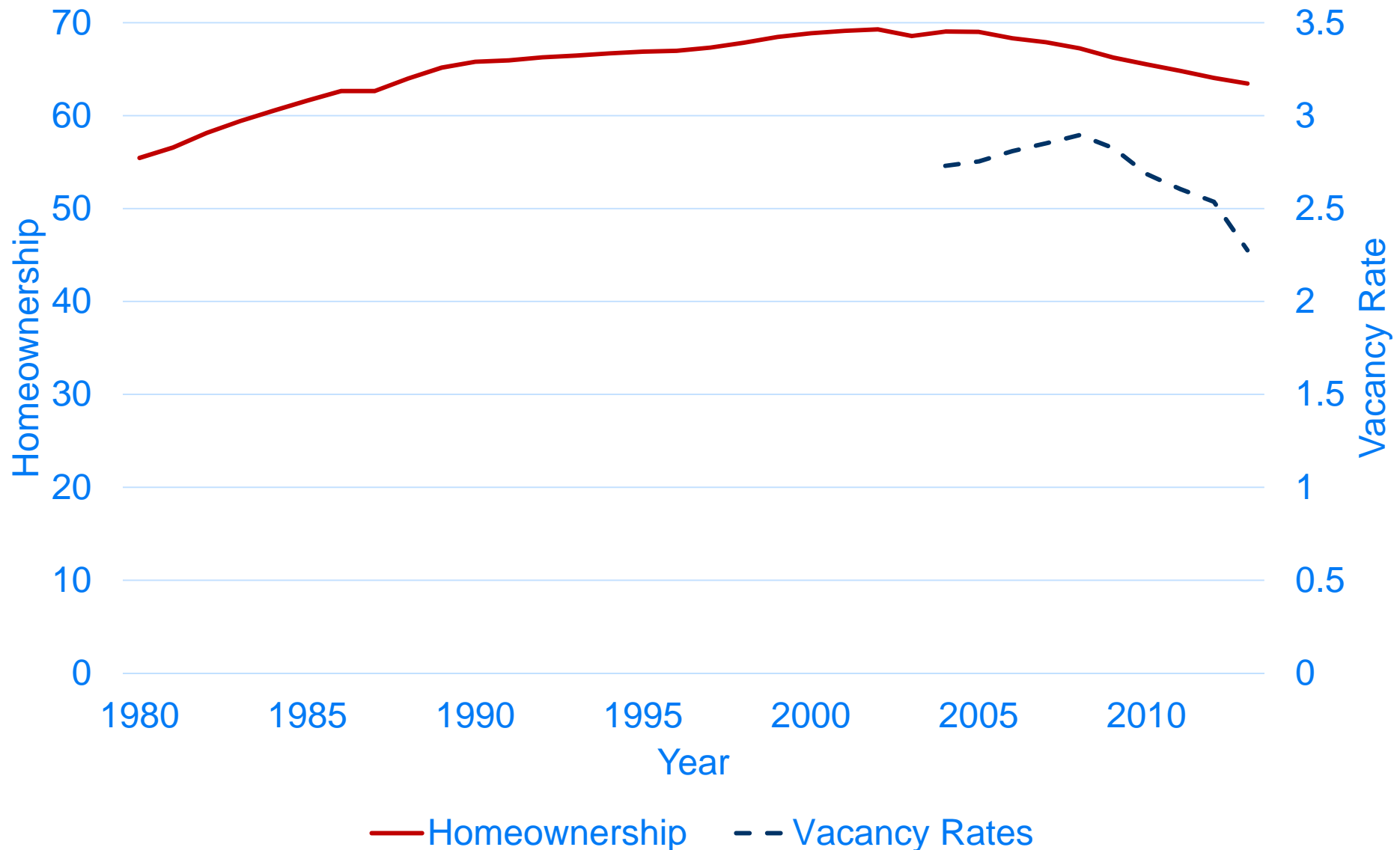
Current status of British housing market(s)

- **Crisis has slowly emerged over last 40 years**
 - ▶ Real house prices grew faster in UK over last 40 years than in any other OECD country
 - London far outstripped rest of UK
 - ▶ Housing construction in steady decline since late 1960s (despite strong price growth)
 - Today 1/3 of construction of late 1960s
- **House prices also extremely volatile**
 - ▶ During last full cycle (80s/90s): UK as a whole substantially more volatile in real terms than single most volatile market in US
 - UK: +83%/-38% vs. Los Angeles: +67%/-33%

Current status of British housing market(s) in two graphs (1/2)



Current status of British housing market(s) in two graphs (2/2)

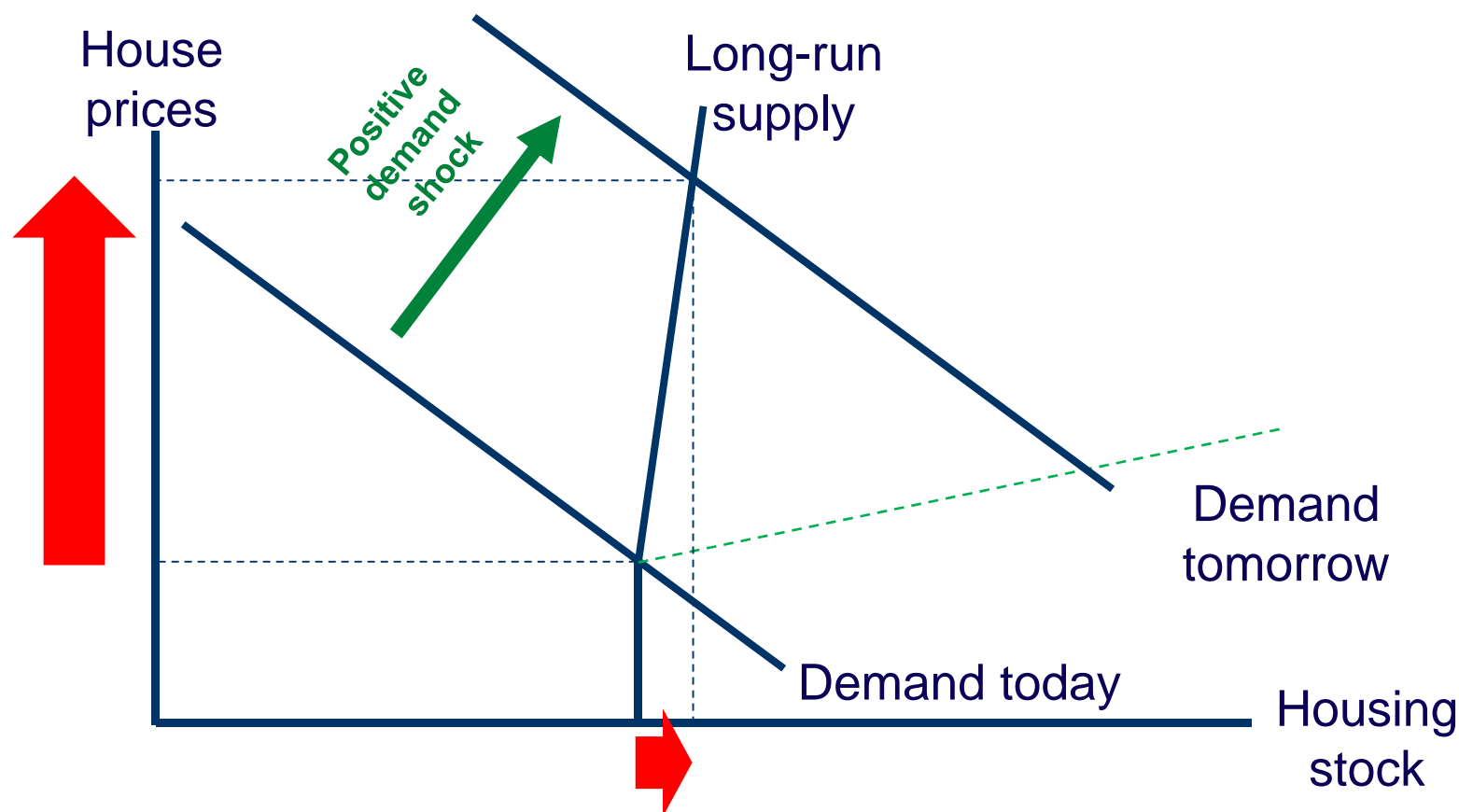


What caused the crisis?

- British planning system is **extraordinarily rigid by world standards**
 - ▶ Extreme form of urban containment through green belts (introduced in mid-1950s)
 - ▶ Strict controls on height
 - ▶ Local authorities face most of the cost of development (infrastructure, congestion) but few of the benefits (little tax revenue), so have no incentives to permit development
 - ▶ ‘Development control’: There are no zones designated for residential use – each plot of land requires separate planning application & approval
 - ▶ Each application is subject to objection by NIMBY-homeowners (or in UK better: BANANAs)

Implications for British housing market(s)

- **Housing supply** curve becomes **extremely inelastic**, particularly in London & South East



UK housing policies

- British housing policies focus on addressing housing affordability crisis & providing access to homeownership
- Three key policies:
 1. Social housing (or “council housing”)
 2. Right-to-buy
 3. Help-to-buy

UK: 1) Social Housing

- In place since 1919 to help “those in need”
 - ▶ Originally only provided by local authorities (“council housing”)
 - ▶ Later also by “housing associations” = private, non-profit org. but regulated & receive public funding
- Merits
 - ▶ Provides low cost housing for households in “priority need” (homeless other ‘vulnerable’ people according to priority criteria)
 - ▶ Does not appear to be associated with negative peer effects, adversely affecting student performance (Weinhardt, 2014)

UK: 1) Social Housing—*Cont.*

■ Demerits

- ▶ Associated with poor housing conditions & corruption
 - By 1970s council estates became “grim havens of decay and lawlessness” and there was a “powerful smell of corruption...as the cosy relationship of local politicians and their friends in building and architecture was laid bare” (Wheeler, 2015)
- ▶ Inefficiencies and welfare losses associated with undersupply and misallocation (due to long waiting lines)
- ▶ The ‘clever’, ‘patient’, and ‘persistent’ are successful rather than those ‘most in need’
- ▶ Taxes necessary to fund rental subsidies are associated with deadweight loss

UK: 2) Right-to-Buy

- **Introduced in 1980 by Margaret Thatcher**
 - ▶ Policy allowed “council estate” tenants to purchase their homes at significantly subsidized price
 - ▶ Explains rise in homeownership during 1980s/90s
 - ▶ *Now:* Conservatives promised to extend policy to housing association tenants in next parliament
- **Merit**
 - ▶ Rise in homeownership attainment (desirable to the extent that social benefits > social costs) – *literature is ambiguous*

UK: 2) Right-to-Buy—*Cont.*

■ Demerits

- ▶ Best social housing stock moved from socially rented to privately owned ⇨ potentially fosters “ghettos”
- ▶ Taxes necessary to fund subsidies are associated with deadweight losses
 - If government does not reimburse housing associations, then this will endanger their ability to finance construction of new homes
- ▶ Does not help solve housing affordability crisis
 - Aggregate demand and aggregate supply are unchanged
 - Fosters NIMBY-homeowner influence

UK: 3) Help-to-Buy

- **Introduced in 2013 by Coalition Government**
 - ▶ Policy aimed to stimulate housing demand
 - ▶ Policy consists of four instruments: equity loans, mortgage guarantees, shared ownership, and a 'new buy' scheme that permits LTV of up to 95%
- **Merit**
 - ▶ **Probably none** because demand increase in UK does not lead to more construction & price increase offsets incentives to own

UK: 3) Help-to-Buy—*Cont.*

■ Demerits

- ▶ Likely helped foster price boom: House prices in London up by 26% in year following announcement of policy
 - Does not help solve housing affordability crisis
 - Housing *less* affordable for young would-be-buyers
- ▶ Taxes necessary to fund subsidies are associated with deadweight losses
- ▶ Generates systemic risk in that government assumes most of the risks + remaining risks assumed by marginal homebuyers
- ▶ Scheme is difficult to withdraw since possible price drop unpopular



Switzerland

(builds mainly on Werczberger 1997 & Hilber and Schoeni, work in progress)

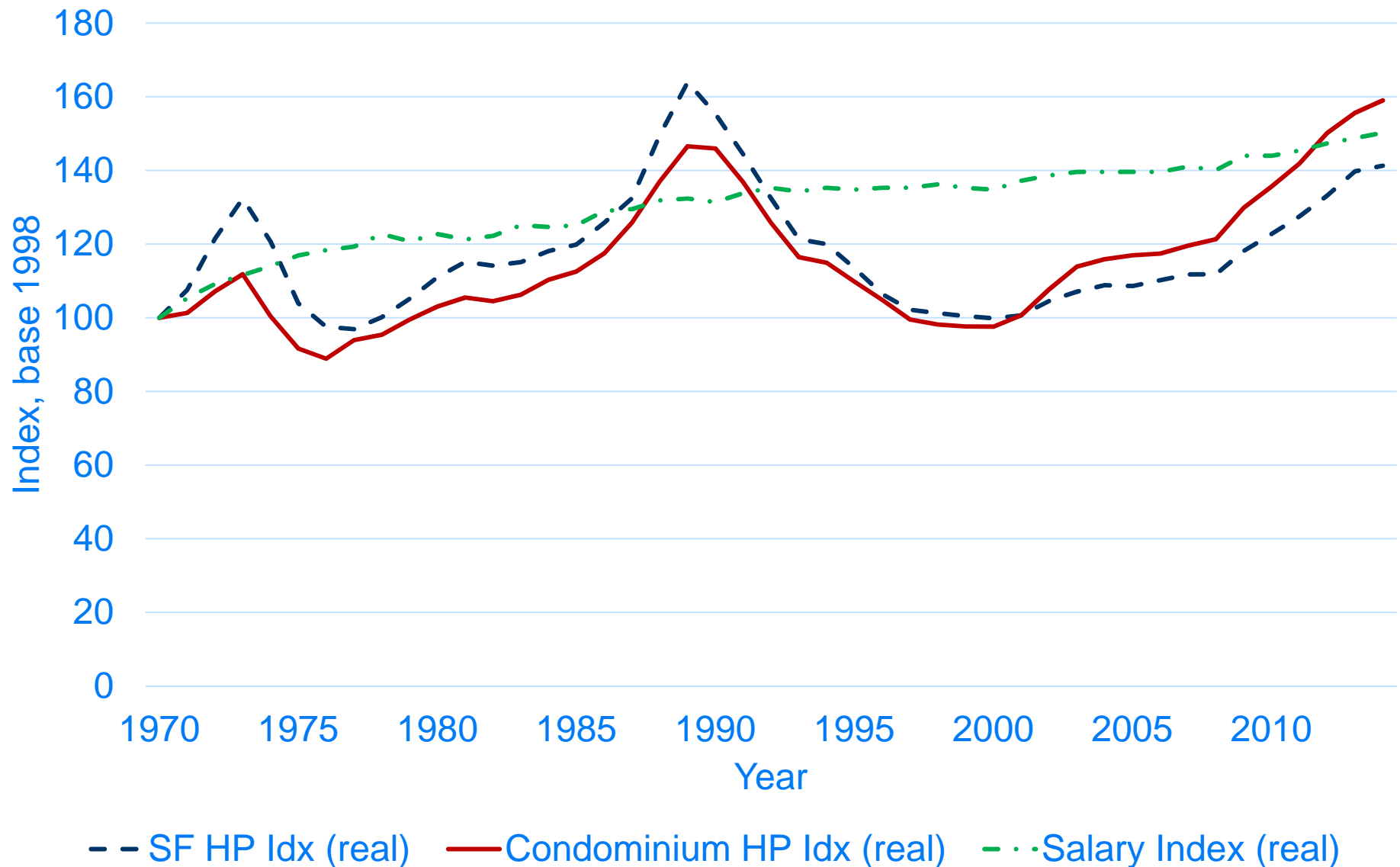


Current status of Swiss housing market

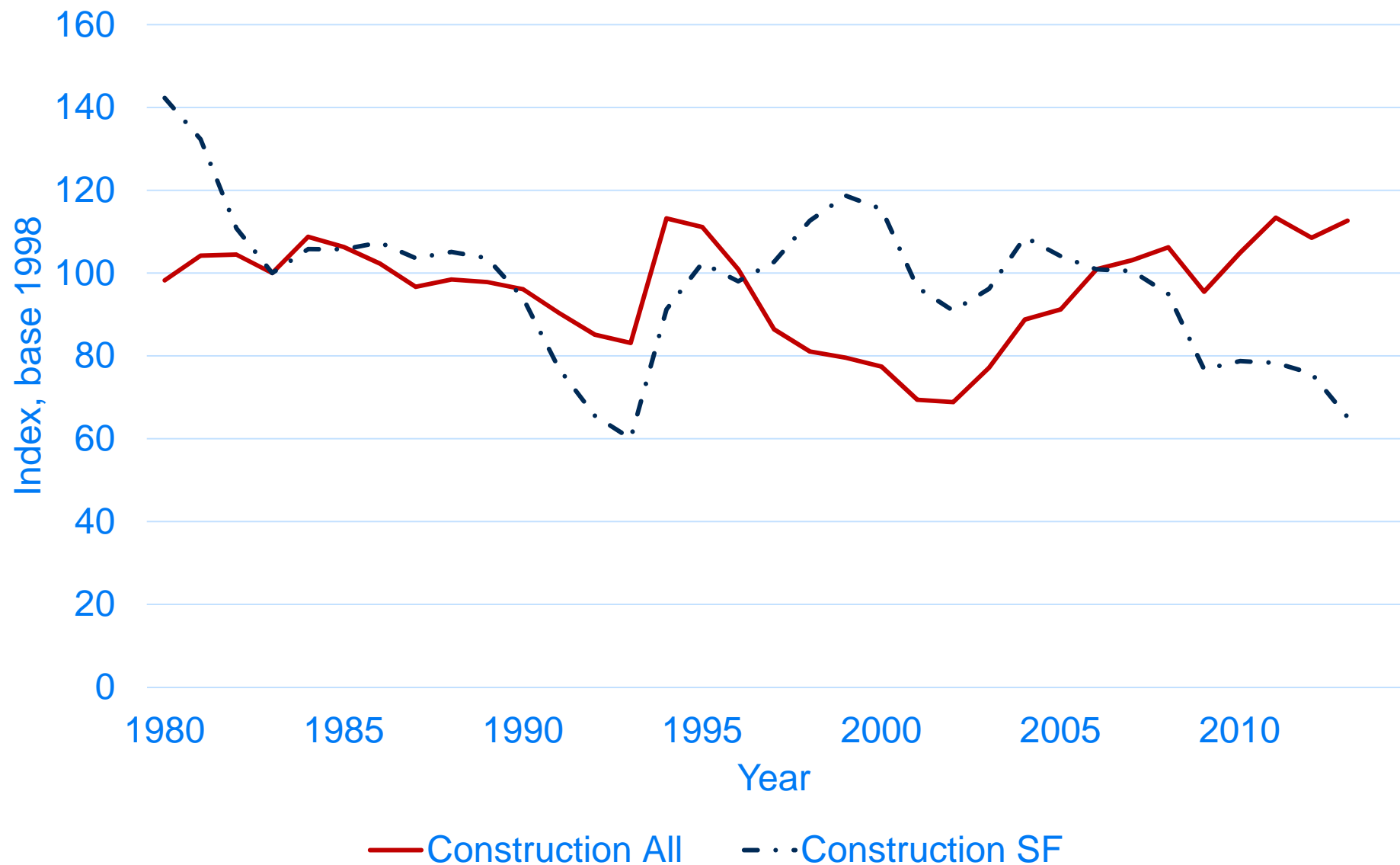
- Switzerland is a **country of renters** (37.5% owned in 2013)
 - ▶ But homeownership rate on the rise with 2.9% increase since 2000
- Property market is characterized by **moderate price and construction boom** since around turn of millennium
 - ▶ Driven mainly by condominium-boom in booming cities & tourist areas
 - ▶ CH has 1/8 of pop. of UK but 1/3 of its construction (2013)
 - ▶ CH: real SF HP increase since 1974: 17%
 - ▶ UK / London: real HP increase since 1974: 113% / 244%

⇒ Sustained construction boom created **sprawl problem**

Current status of Swiss housing market (1)



Current status of Swiss housing market (2)



What caused sprawl problem?

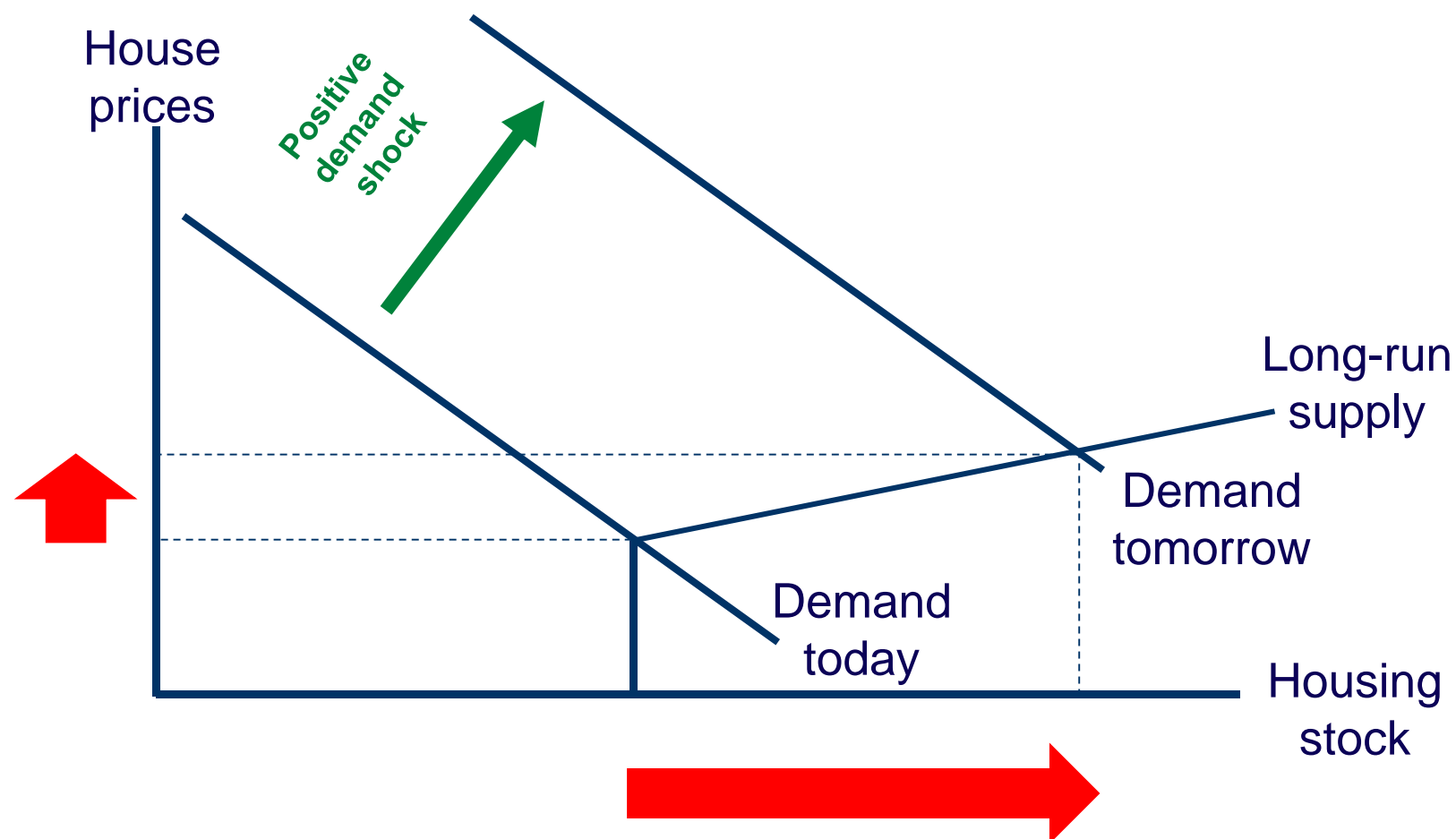
On supply side:

- Local public services in Switzerland financed via local income taxes
 - ▶ Strong incentives for local municipalities to attract new (wealthy) tax payers
 - ▶ **Strong incentives** to permit development

On demand side:

- Strong immigration & robust economy throughout great recession
- Extremely low interest rates (fixed rate mortgages around 1%)

Implications for Swiss housing market(s)



Swiss housing policies

- Swiss housing policies focus on stabilizing rents & combat sprawl
- Two key policies:
 1. Rent control
 2. Restrictions on construction of 'second homes' ("Second home initiative")

CH: 1) Rent Control

- Introduced first during World War I
 - ▶ Abolished and reintroduced several times since then, 'permanent' since 1972
- Today's form of rent control fairly flexible:
 - ▶ Landlords can increase rents but must justify
 - ▶ Rent levels linked to two economic indicators *average mortgage interest rate* and *CPI*
 - ▶ Only other justification for rent increase: major renovation
 - ▶ Also renters are protected against 'abusive evictions'

CH: 1) Rent Control—*Cont.*

- Merits

- ▶ Real rents are increasing fairly moderately & steadily (by less than 33% since 1983)

- Demerits

- ▶ Welfare losses associated with undersupply and misallocation (Glaeser & Luttmer, 2003)
 - Extremely low vacancy rates in CH
- ▶ Private landlords have strong incentives to select 'good tenants' making it more difficult for disadvantaged to rent
- ▶ Rent control *may* reduce HH mobility (Ault *et al.*, 1994)
- ▶ Lowers housing quality (Gyourko and Linneman, 1990)
 - Not observed in CH since law ensures minimum quality standards + renovation provides justification for increasing rents

CH: 2) Restricting construction of 2nd homes

- 'Second home initiative' was approved by Swiss population in March 2012 with 50.6% of votes and just over half of cantons (13.5 out of 26)
- Idea: Municipalities with second home share > 20% of all houses are banned from building any new second homes
- Merit
 - ▶ Reduces sprawl in most touristic areas of country with 2nd home share >20% (to extent no loopholes are found in law)

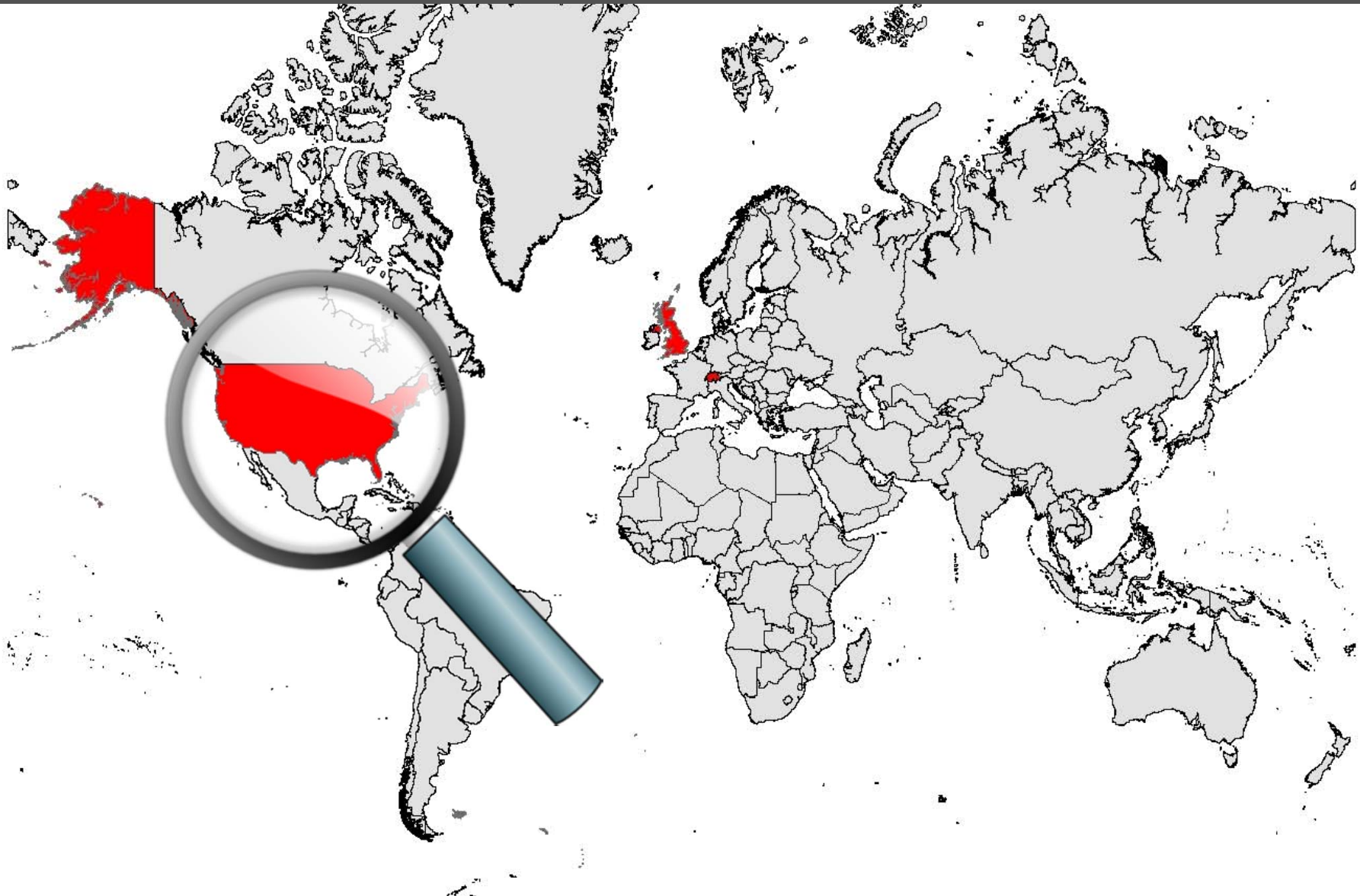
CH: 2) Restricting construction of 2nd homes—*Cont.*

■ Demerits

- ▶ Loopholes: Sell existing house as 2nd home and build new first home; build hotels and rent out; merge neighboring municipalities to lower share below 20% etc.
- ▶ Demand will shift from most touristic areas to municipalities just below 20% ⇒ sprawl will just shift geographically
- ▶ There may be big price and rent increases for first homes in municipalities ‘just below 20%’

United States

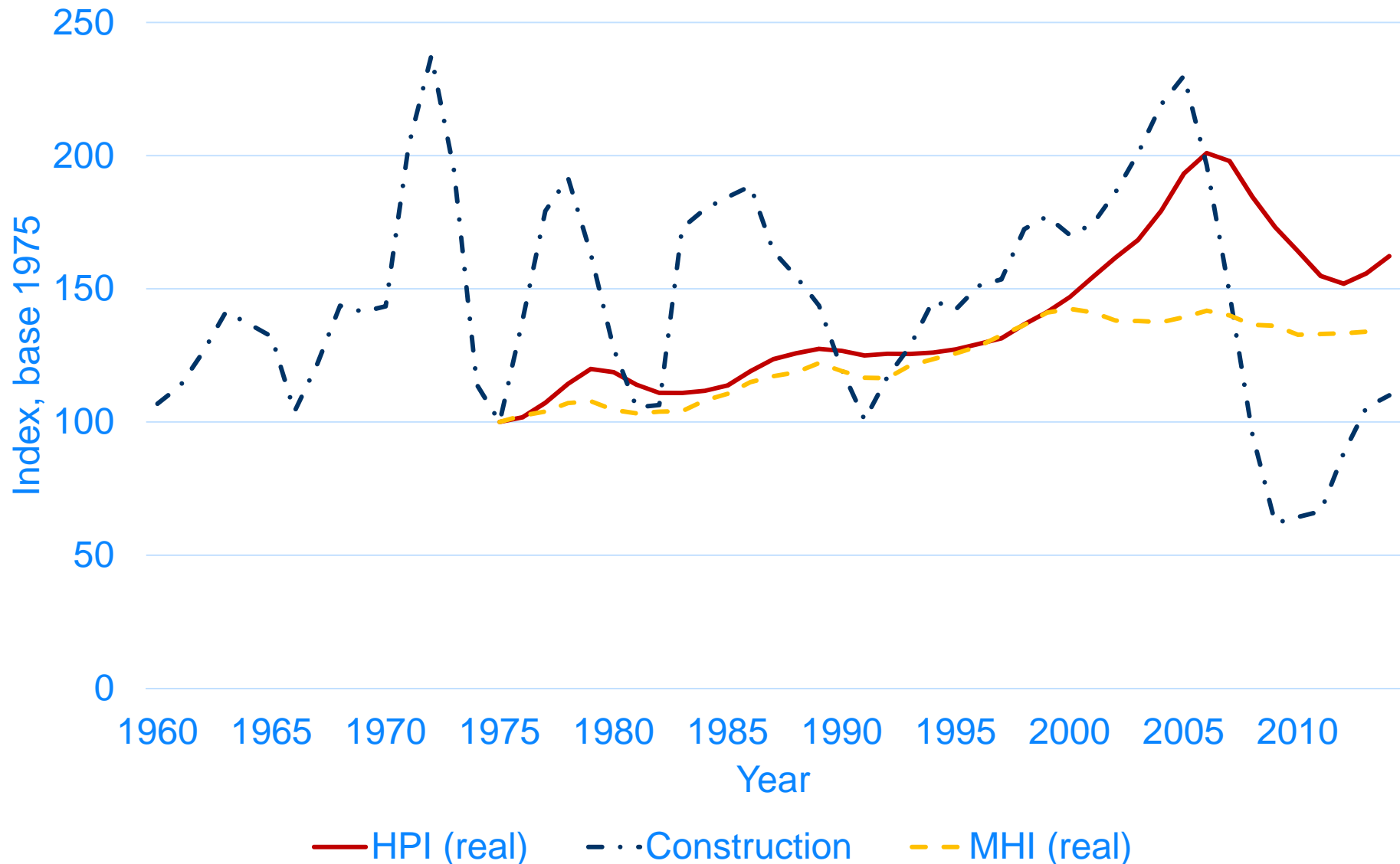
(builds on Olsen and Zabel, 2015 & Hilber and Turner, *REStat*, 2014)



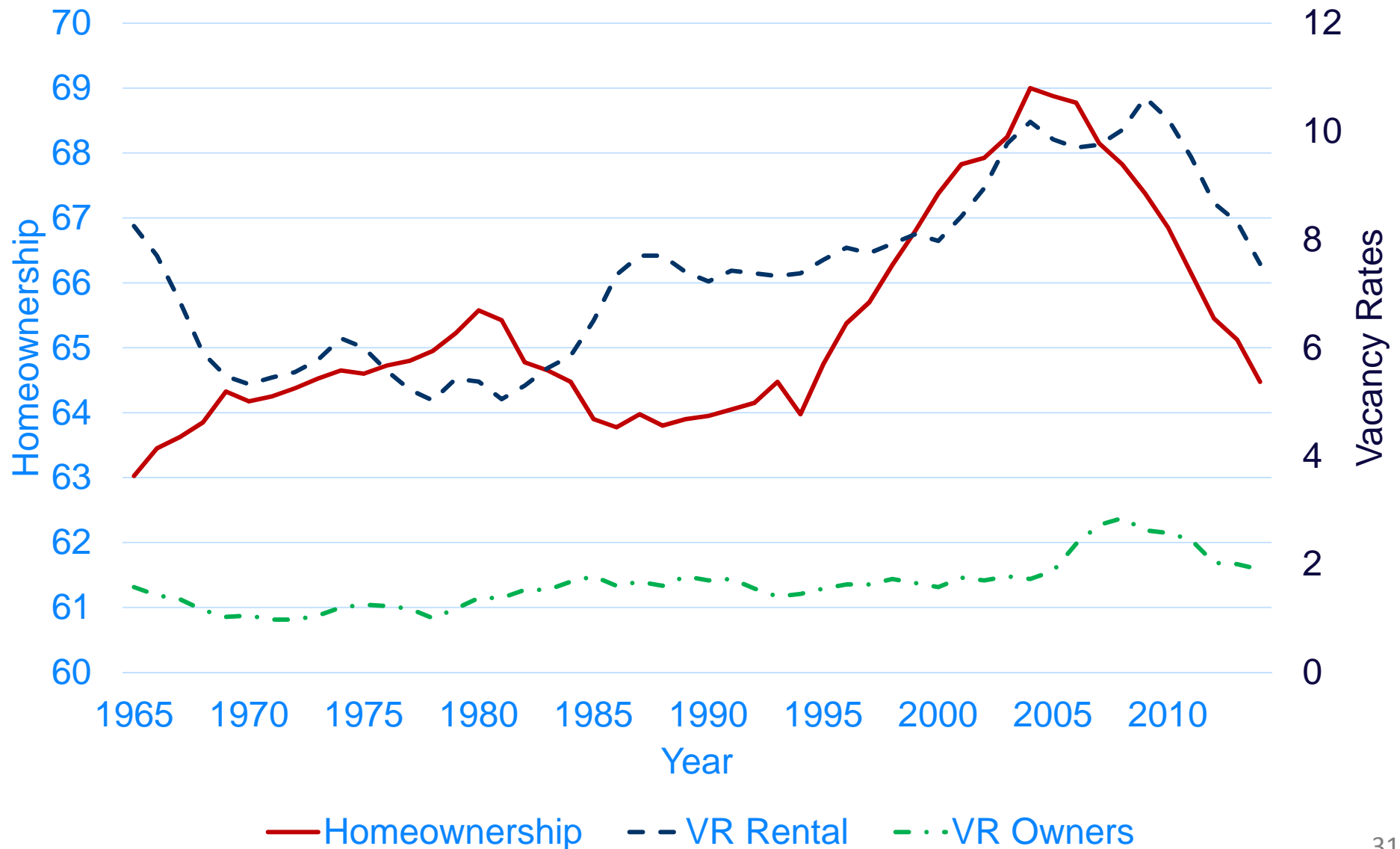
Current status of US housing market

- US is a **country of homeowners** (64.5% owned in 2014)
 - ▶ But homeownership rate in decline since 2004 (69.0%)
- Property market(s) in US **hit very badly by Great Recession** and only just recovering
 - ▶ House prices decreased b/w 2006 & 2012, in real terms, by 24.4%
 - ▶ Construction decreased b/w 2004 & 2009 by 71.7%
 - ▶ Very severe **foreclosure crisis** (in part because mortgages typically non-recourse)

Current status of US housing market in two graphs (1/2)



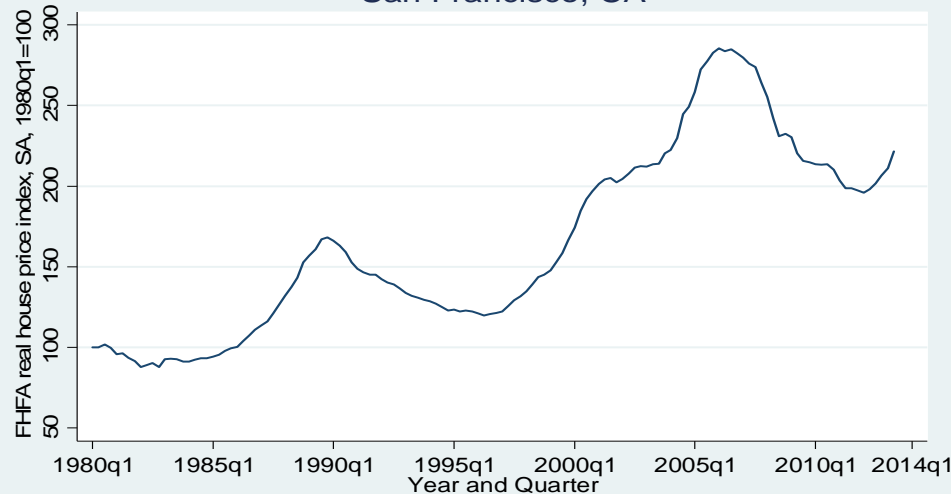
Current status of US housing market in two graphs (2/2)



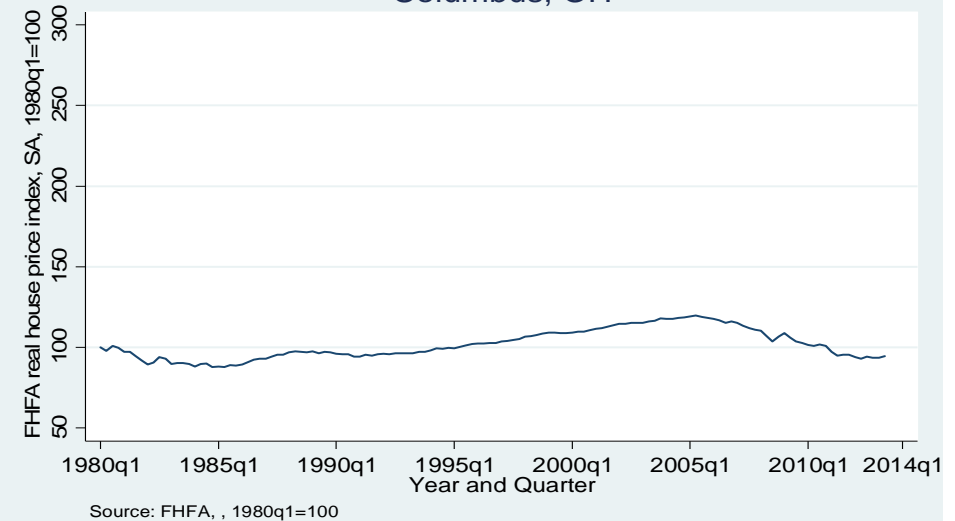
But huge variation across local markets

(Real house price growth 1980-2014)

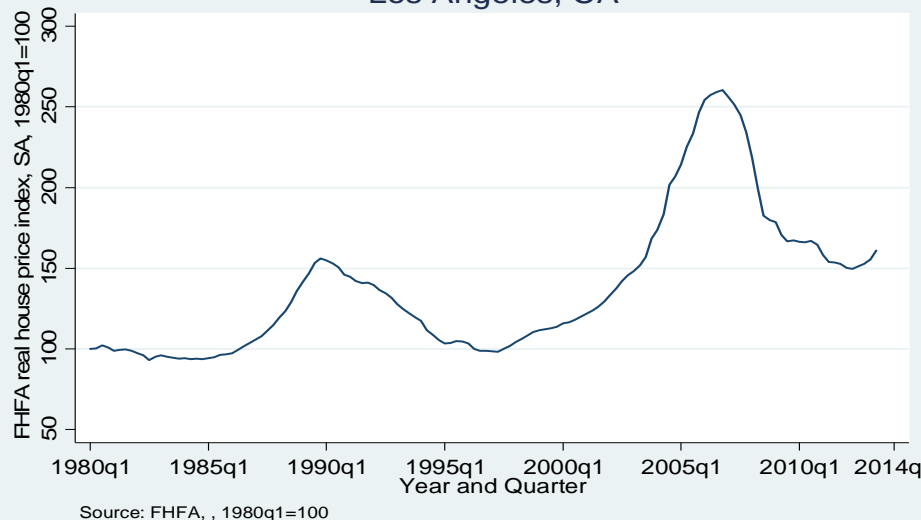
San Francisco, CA



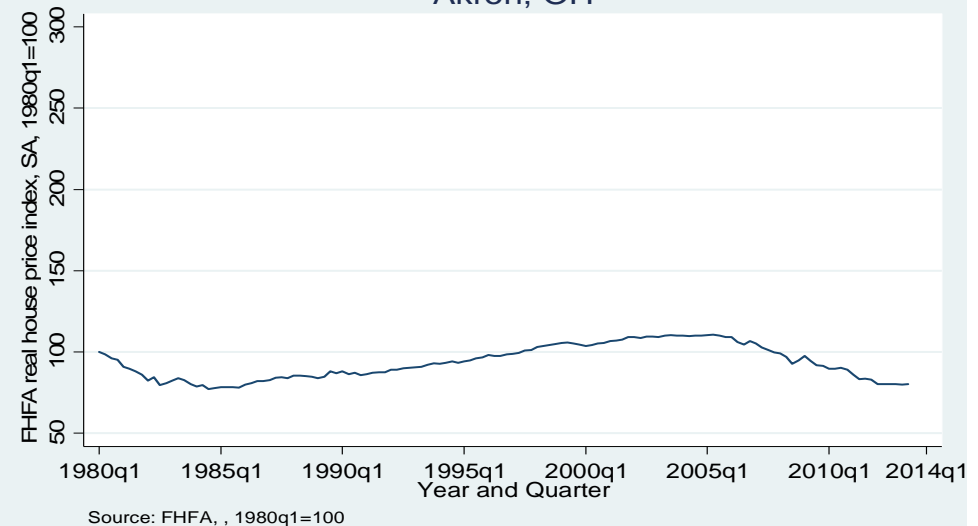
Columbus, OH



Los Angeles, CA



Akron, OH

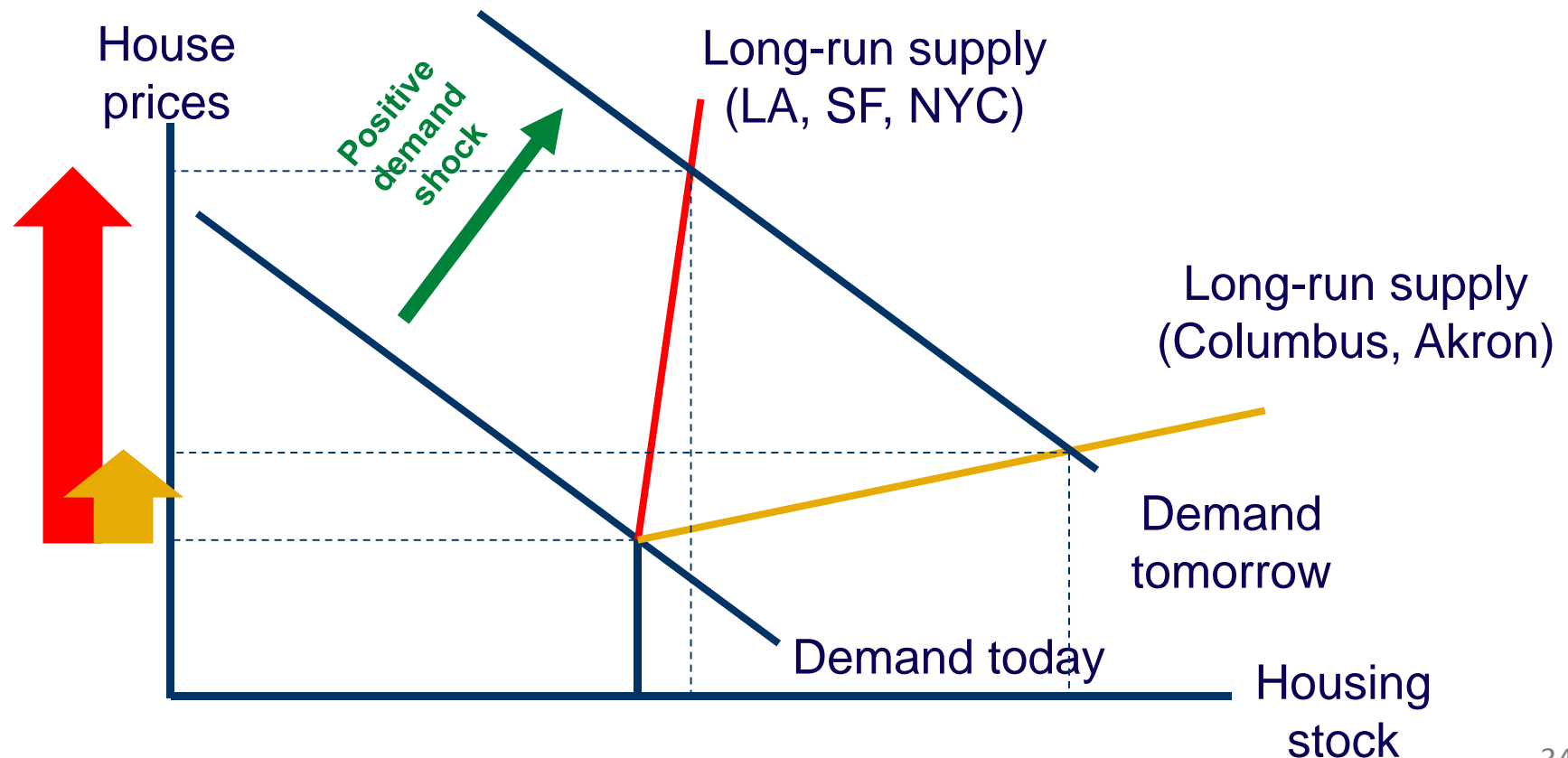


Why the huge differences across space?

- Restrictiveness of land use controls and physical supply constraints vary enormously across US
 - ▶ Some cities have very strict land use controls and tight physical constraints (SF, LA, NY) – *rather like UK*
 - ▶ Other cities have lax controls and few geographical constraints (Columbus, Akron) – *comparable to CH*
- ⇒ Some place have very inelastic supply of housing, while others have very elastic supply...

Implications for US housing markets

- **Housing supply** curve becomes **extremely inelastic**, particularly in London & South East



US housing policies

- US housing policies focus on providing access to homeownership (*+ currently: dealing with foreclosure crisis*)
- Key long-term policy: Mortgage interest deduction

US: Mortgage Interest Deduction

(based on Hilber and Turner, 2014)

- MID: Subsidy to homeowners that varies by income
 - ▶ Introduced in 1986 (Tax Reform Act)
- Aim of policy: Increase homeownership attainment
- Cost of policy: ~\$100 billion per annum in foregone tax revenue
- Merits
 - ▶ In markets with flexible land use controls (Columbus, Akron) the MID does increase homeownership attainment

US: Mortgage Interest Deduction—*Cont.*

(based on Hilber and Turner, 2014)

■ Demerits

- ▶ Only increases homeownership attainment of higher income HHs in markets with flexible land use controls
- ▶ In markets with tight land use controls (LA, SF, NYC) the MID reduces homeownership attainment
- ▶ Net effect over entire US: essentially zero
- ▶ May lead to overconsumption of housing of existing homeowners
- ▶ Enormous cost of policy in form of foregone tax revenue

Synthesis: A tale from three countries

- Main conclusion of analysis: Housing policies cannot and should not be judged in isolation from the institutional setting
- For example: Whether demand focused policies (such as Help-to-Buy or the MID) work depends crucially on nature of land use planning system
 - ▶ Demand-focused policies won't work in markets with tight planning restrictions and/or other severe supply constraints (UK, US-superstar cities)

Synthesis–*Cont.*

- Policy makers should focus more on **supply side** and, in particular, on proper functioning of **land use planning system**
- The main role of land use planning system should be to **correct market failure** (provision of public goods; internalizing externalities)
- Demand-side policies should only be implemented if supply can respond sufficiently to price signals

Q & A

Thank you!

*Presentation with references & hyperlinks
will be downloadable from:*

<http://personal.lse.ac.uk/hilber/>

Presentation is based on

Hilber, C.A.L. and O. Schöni (2015) “Housing Policies in the United Kingdom, Switzerland and the United States: Lessons Learned”, Paper prepared for ADB-ADBI Inception Workshop: Housing Policies for Emerging Asia, Tokyo, May 14-15, 2015.

Note: Data sources are provided in the paper.

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Further Readings

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Further Readings—*Cont.*

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