

Lecture 17– Housing policy

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1 Housing supply subsidies.

1. Demand subsidies

- (a) housing benefit (£10 billion in 1997/1998).
- (b) income support for mortgage interest payments for low income home-owners (£900 million in 1997/1998).
- (c) discounts to help tenants purchase social housing (£900 million in 1997/1998).

2. How large are housing supply subsidies in the UK?

- (a) Net central and local government support for housing costs other than spending on housing benefit was about £8 billion in 1997/1998.
- (b) This includes spending in several categories.
 - i. capital allocations to local authorities (£754 million in 1997/1998) for the renovation of housing stock, grants to Registered Social Landlords (RSL's) to build social housing, cash incentives to help social housing tenants purchase housing, grants to renovate private homes, and grants to carry out adaptations for disabled people.
 - ii. expenditure on housing from regeneration programmes (£1.3 billion in 1997/1998).
 - iii. funding for RSL's through the Housing Corporation to support development of social housing (£673 million in 1997/1998).

- iv. renewal fund (£100 million in 1997/1998) to improve poorer quality council housing estates.
 - v. subsidy for local authority Housing Revenue Accounts (£640 million in 1997/1998).
 - vi. other spending by local authorities on housing (£1.1 billion in 1997/1998).
- 3. Overall, a large amount is spent on supply subsidies and is spend in a variety of ways.
- 4. Much evidence and theory suggests that housing supply subsidies are inefficient.
- 5. Same result can be obtained by demand subsidies which give consumers more choice of housing. Public supply usually is less flexible than private supply. If consumers' live in public housing and want to move to a different location or to a larger home, this can be very difficult. Publicly provided housing tends to limit the options available to public housing consumers.
- 6. Evidence in US suggests that government provision of housing is more subject to inefficiency/corruption than privately provided housing.
 - (a) Why? Poor incentives to people who run housing to make efficient decisions.
 - (b) Extreme example. In the late 1990's the Chicago public housing authority was taken over by the US federal government because the local authority had been siphoning money meant for public housing in Chicago into building condominiums in Florida. Large numbers of public housing units in the city were uninhabitable and had been uninhabitable for decades.
 - (c) Another example It is usually cheaper to provide low income housing through buying and refurbishing old housing than through construction yet most publicly provided housing in the past has been through new construction. Incentives to housing authorities are not usually based on meeting demand of customers at minimum cost.

7. Counter arguments in favour of public provision of housing.
 - (a) Possible economies of scale from public provision. This might be the case for instance if the public sector can force through changes in planning laws on a large scale or force many property owners to sell their land to create a large project.
 - (b) High income people may want the government to provide low income housing in locations that are far from their own residences.
 - (c) Market failures in private rental markets
 - i. Fraud: Low income households may be victims of fraud perpetrated by private landlords.
 - ii. Imperfect contract enforcement: low income moves in, landlord promises low rent. Household moves in, landlord raises rent. Household pays or else faces eviction or high moving costs.
 - iii. Imperfect insurance market for risk of volatile housing rents. Housing prices and rents are volatile. Purchasing insurance against such volatility is difficult because insurance markets for such risk are under-developed. Government provided housing can in part correct this market failure by offering insurance against rent volatility.
 - iv. Asymmetric information in housing markets: It might be easier to ensure the quality of the low income housing supply through government provision than through private provision. On the other hand, government provision of housing is no guarantee of housing quality.
8. Public supply through subsidisation of private production of low income housing.
 - (a) New construction is costly and is usually not the most efficient method to provide low income housing.
 - (b) Problems of flexibility are reduced.
 - (c) Problems of corruption/inefficiency are often reduced.
 - (d) Less efficient at transferring wealth to low income than direct cash payments or housing demand subsidies.

- (e) Need an argument as to why private providers are underproviding housing.

2 Rent regulation or rent control

1. Many cities have rent control. These policies limit how much rents can increase over time.
2. In the UK, tenants who let their flat before 1989, pay mostly regulated rents. Rent increases are limited to inflation or to being tied to improvements in the quality of the property.
3. In San Francisco for example, rent increases are limited to the rate of inflation unless major repairs are made or the tenant moves out.
4. Draw picture of effects
 - (a) Reduces the supply of housing
 - (b) Creates excess demand for housing. This must be rationed somehow.
 - (c) Deadweight loss
5. Other impacts
 - (a) People don't want to move. Many rent control laws only apply to existing tenants.
 - (b) People get around rent control by selling rights. To the extent they do, rent control, is a pure transfer from landlord to existing tenants
 - i. If market rent increases, landlord pays tenant to leave
 - ii. In 1999, Kelly, who had lived in the same flat in Manhattan for 7 years, was paid \$12,000 by her landlord to move out of her flat who promptly raised the rent
 - iii. John, a landlord in SF, only rented to tenants who appeared likely to remain for a short tenure.
 - (c) Limits ability of market to adjust to changing market conditions

- (d) Tax on renting a property discourages long term development of rental housing
- 6. Cash transfers and housing vouchers are both preferable methods of subsidizing housing demand.

3 Quality or quantity controls

- 1. Concern about housing for poor being of too low quality or too small
 - (a) NYC no splitting up of flats
 - (b) Result restrict supply at low end of market, live in illegal housing
 - (c) Correct solution again is cash transfer to poor or demand subsidy

4 Other housing regulations

- 1. Building code and other regulations of rental market
 - (a) Minimum quality, safety, size, sanitation standards
 - (b) Concern about fire hazard
 - i. Fire is externality
 - ii. N houses in a community
 - iii. Ideal: minimise costs of fire and fire protection

$$C = \min_{\{e\}} \left\{ e + \left(\sum_{i=1}^N F_i \right) * P(e) \right\}$$

- A. e = investment in fire protection
- B. F_i = loss to person i
- C. $P(e)$ = probability of fire. $\frac{dP}{de} < 0$, $\frac{d^2P}{de^2} > 0$
- D. Social optimum first order condition

$$1 + \left(\sum_{i=1}^N F_i \right) \frac{dP}{de} = 0$$

$$\text{iv. Private decision } \min_{\{e_i\}} \left\{ e_i + F_i * P \left(e_i + \sum_{j \neq i} e_j \right) \right\}$$

$$1 + F_i \frac{dP}{de} = 0$$

v. Draw picture: Subsidize fire protection or tax failure to do so

vi. Problems:

A. Might be hard to measure $P(e)$, F_i , or e

B. F_i might change when e changes: moral hazard

C. Use known technology with known effects on P to combat A.)

(c) Concern about housing for poor being of too low quality or too small. Concern that purchaser or renter cannot see many aspects of quality, costly to inspect.

i. Performance standards vs material/technology standards similar to fire problem.