

The Problems With Rent Control Research Being Relied on by Advocates, Including Oregon House Speaker Tina Kotek

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In the debate about rent control, many opponents reference the problems associated with World War II era hard caps on rents. Advocates for rent stabilization counter this argument by saying it's an outdated way of thinking – newer rent stabilization policies have not had the negative effects of a hard cap. This gives rise to the natural follow-up question: has sufficient research been done on newer second generation rent stabilization policies to determine what the effects have been on metro areas employing them?

Throughout the 1990s and early 2000s as researchers set out to study this topic, they found mixed results. Some of these studies, particularly early on, argued that if implemented carefully and in the right set of circumstances, rent stabilization policies could avoid the negative ramifications of first generation “hard” rent control, and may have some mitigating effects on rent increases. The potential for positive effects was predicated on three incredibly significant factors:

1. Rent stabilization must directly address the underlying problems causing high rents.
2. The market conditions are such that conversion of rental units to owner-occupied units does not exacerbate the housing shortage in a way that disadvantages low income renters.
3. The program put in place at a local level is well thought out, and follows the recommendations of the research studies that have now been conducted on rent stabilization.

Because we cannot know what individual cities like Portland will implement, this paper focuses on conditions #1 and #2 above. In many of the studies I refer to here, the authors note that if bad policies are implemented they will do more harm than good in both the short and long term. It is also important to note that Richard Arnott, a researcher whose initial work in 1995 suggested that rent stabilization could be successful and who is often cited by rent stabilization advocates, later took a dimmer view of such policies. Just two years later, in 1997, he argued that enacting temporary second generation rent controls may improve efficiency, but will not improve quality or affordability, writing:

“Thus, according to this modern view of the housing market, it should be possible to design a second-generation rent control programme that improves efficiency. This argument for rent control is very different from the conventional one put forward by non-economist advocates of rent control, which centers on notions of “equity” and “affordable housing” and fails to acknowledge that setting rent below the market level discourages maintenance and new construction. The new, economically respectable argument in favour of rent control is also more tentative. All it claims is that there is some set of rent control programmes which would improve

efficiency. It emphatically does not assert that second-generation rent control programmes are in general desirable.”¹

In other words, even if the State of Oregon or individual cities come up with an optimal set of temporary rent controls, it is unlikely that such policies will address the core issue of affordability currently affecting renters across the state.

1. Does Rent Stabilization Directly Address the Underlying Problem Causing High Rents?

In Richard Arnott’s research for the *Journal of Economic Perspectives*, he states, “It is a general rule that the best policy to deal with a distortion is that policy which addresses the distortion most directly. Rent control is then desirable when the distortion is the unavailability of insurance against a sharp, unanticipated rise in rent.” He footnotes this assertion with the example of rent control enacted in response to Alaska’s oil boom. A comparable recent example could be the natural gas boom in North Dakota, where the cost of living suddenly ballooned due to the discovery and exploitation of natural resources.

In Portland, as in much of Oregon, the extent of the housing crisis may have come as a shock to many, but it was neither sharp nor unanticipated. According to Census data, permitting for apartments in Portland was incredibly low from 1991-1993, 1999-2002, and especially in 2009-2011. Furthermore, the recovery in building permit rates that occurred between 2003 and 2007 did not meet the high permitting rates seen in other peak years. In 2005-2006 approximately 2,500 apartment units became condos, representing a 1% loss in apartment stock.² Meanwhile, population growth in the Portland Metro Area (PMA) was 26.5% between 1990 and 2000, 15.5% between 2000 and 2010, and 6.83% between 2010 and 2015. While building permits are currently at record highs, comparing permit rates and population growth indicates that while the population was booming over a 25-year period, apartment construction was clearly and demonstrably not keeping up with demand. In-migration to Portland is not a sudden or even recent phenomenon, and it is not currently occurring at an unprecedented rate. In fact, this crisis could have been predicted during the late 1990s, almost 20 years ago.

It is important to ask why Portland’s shortfall of new housing supply has continued during periods of continuous population growth. Part of the answer can be found by looking at a zoning map of central Portland. Most of the inner city of Portland is zoned for single family residential use, even in and around so-called transit corridors. Many neighborhood groups have successfully lobbied the city to keep their neighborhoods looking the same, at the expense of adding sufficient levels of additional housing. Recently, *DenverUrbanism* published an article by a local city planner who explains that urban stability requires allowing neighborhoods the flexibility to change and grow.³ In capitulating to NIMBY-oriented neighborhood groups, the city of Portland has effectively destabilized the city by hampering its ability to

¹ Arnott, Richard. “Rent Control” *Boston College Working Papers in Economics*, 1997. Page 11.

<https://dlib.bc.edu/islandora/object/bc-ir:102975/datastream/PDF/view>

²<https://static1.squarespace.com/static/52b886f5e4b00d4e733f7a27/t/52cc3d3be4b0422ecd648dc5/1389116731838/Winter+2007+Newsletter.pdf>

³ <http://www.moderncities.com/article/2017-jan-a-changing-neighborhood-is-not-an-unstable-one>

respond adaptively to population increases. This can also be said of cities like Bend, which has not expanded its urban growth boundary since 1981, thereby artificially limiting the housing supply.

Another reason for the relatively slow increase in the supply of new housing in Portland is the length and complexity of the permitting process. As a researcher who keeps track of local permits, I can verify that it is not unusual for upwards of a year to pass between the submittal of building permit applications and the approval by the city. It must also be noted that prior to submitting building permits, the process of design review can take equally as long. This makes building in Portland an incredibly expensive proposition for developers before shovels even hit the ground. This also explains why many of the new developments are luxury apartment and condo buildings – achieving the highest possible rents is the only way for these projects to pencil out.

Currently, there are two more important factors that are likely to affect the supply of new units in the future. The first is inclusionary zoning, which went into effect February 1, 2017. In fact, the unintended consequences of inclusionary zoning are noted by Allan Heskin, Ned Levine, and Mark Garrett in their 2000 article, “The Effects of Vacancy Control.” In assessing whether vacancy control causes a decrease in new supply, he attributes some of the supply side issues to inclusionary policies in West Hollywood, which he says, “drive up the cost of construction and may push developers toward the higher return at the ownership end of the market” (22). The Portland Metro Area is currently facing a shortage not only of rental units, but of owner-occupied units. The increase in the median sale price of a single-family home has far outpaced the increase in median rents since 2011.⁴ With housing supply already limited by zoning and permitting policies, and a history of housing stock not keeping up with the pace of demand, the new inclusionary zoning policy is going to further exacerbate the housing shortage in Portland.

The second factor is the crisis facing the Low Income Housing Tax Credit (LIHTC) program as a result of the newly-elected President’s promise to cut corporate tax rates to 15%. This anticipated significant reduction in the federal corporate tax rate means that corporations no longer have an incentive to bid on these tax credits, and their value is rapidly dropping, leaving many planned affordable housing projects in the lurch. Already, there are 27 affordable housing projects in Portland that might not get built if alternate funding is not found.⁵ While this problem could fall under the umbrella of being unanticipated, it in and of itself is not going to cause a sharp increase in rents. It is instead the longer-term problem of the city artificially keeping supply from meeting demand over the past 25 years that is causing rents to reach the levels we are currently seeing.

2. Will the Conversion of Rental Units to Owner-Occupied Units Exacerbate the Housing Shortage in a Way That Further Disadvantages Low Income Renters?

Many advocates of rent control cite studies in which rates of homeownership increase as a result of conversion of units from rental to owner-occupied (e.g., condo conversions). Many of the studies that remark on this side effect of rent stabilization focus on time periods during which homeownership was a much more attainable goal in the United States than it is now: the 1990s and the period directly after

⁴ Between 2011 and 2016, median list price of homes in Portland have increased by 90%. Median rents have increased over that time by 30%. (Figures from <http://www.deptofnumbers.com/rent/oregon/portland/> and REIS 4Q 2016 Metro Portland report)

⁵ <http://www.portlandmercury.com/news/2017/02/01/18826467/trumped-towers>

World War II. It is important to note that the lax regulations in home lending in the 1990s contributed to the housing market collapse in 2007. Since the housing market collapse, lenders have imposed significantly stricter borrowing rules to avoid a similar situation in the future, making it significantly more difficult for borrowers with poor or limited credit histories to obtain home loans. Furthermore, metro areas in Oregon such as Portland and Bend are experiencing a serious lack of supply in the non-rental housing market that has contributed to the affordability crisis. Again, I will focus on Portland, as that is the region I am most familiar with.

Currently, Portland's housing crisis is not solely or even primarily a rental housing crisis. From 2015-2016, housing prices increased 13.8% in Portland, which represents the fastest growth rate in the nation.⁶ Every month the Oregonian features homes that have sold for significantly above asking price, and frequently the list includes houses at the lower end of the market's price range.⁷ Much of the problem can be attributed, like the increase in rents, to a supply shortage. The condo market in Portland is similarly strong, with prices increasing approximately 36% over the past three years.⁸

The studies frequently cited by the Speaker's office argue that a reduction in rental units is not a problem if more people become owners. That argument, however, only applies to a market in which there is enough housing for everyone. If rental units become owner-occupied units in a balanced market, renters are becoming owners. This is not the situation in Portland. There are not enough houses for sale OR apartments for rent in Portland. Many apartment units are likely to be converted to condos if rent control is enacted precisely because housing prices are so high in the metro area. Furthermore, it is more difficult than ever to buy a house or condo. Credit requirements for a mortgage are unattainable for most low-income families, interest rates are expected to increase three times this year, saving for a down payment is incredibly difficult as costs of living outpace wage growth, and programs to assist low-income home buyers are increasingly cash-strapped. If rental units become condos, those condos will be bought by people at the higher end of the pay scale, and there will be fewer apartments for lower-income families. This will lead to lotteries and waiting lists for apartments, and more displaced families who cannot find a place to live near job centers.

Again, this comes back to the problem of cities such as Portland dis-incentivizing development. A restrictive urban growth boundary, an overly complex permitting process that is time consuming and incredibly costly, and the recent implementation of inclusionary zoning are all contributing to supply restriction in Portland. Even if rent stabilization policies do not contribute to that problem, we are already at a point where there are not enough housing units being built to keep up with the in-migration and population growth that has occurred over the past three decades. These are not the conditions under which units being converted to condos helps lower-income renters or families.

3. Conclusions

While it is possible, as Arnott states, that second generation rent controls may in the right circumstances improve market efficiency, it is clear rent control will not improve housing affordability for Oregonians.

⁶ <http://www.businessinsider.com/how-much-the-average-home-costs-in-the-15-most-popular-big-cities-2017-2>

⁷ http://www.oregonlive.com/hg/index.ssf/2017/02/portland_home_bidding_wars_jan.html#0

⁸ Kisiel, Mackenzie. "Can Rent Control and Rent Stabilization Solve Portland's Housing Affordability Problem?" *Center for Real Estate Quarterly Report*, vol. 10, no.4. Fall 2016. Page 14.

The conditions in Oregon right now do not meet the criteria for when rent stabilization will not do more harm than good. Exacerbating the lack of supply will make housing more unaffordable, and conversions to owner-occupied units will have the greatest negative impact on the low-income renters the state is ostensibly trying to help with these new regulations.

There is an immediate need for relief for renters who are being displaced by the current situation in the state, but rent stabilization does not appear to be the correct tool for the job. Programs aimed at quickly increasing the supply of new housing, such as *streamlining permitting processes* and *allowing for even slight increases in density for single family neighborhoods*, would attract development across the city rather than exclusively in the downtown core. Furthermore, solutions such as *expanding housing voucher programs* and finding solutions that aim to fill the gap left by uncertainty in the LIHTC program would be significantly more effective than rent control in improving affordability for renters across the state.