

Comment on Bengt Turner and Steve Malpezzi: Rent Control: A review of selected literature

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It is hard to make useful comments on a literature review. One could, of course, point at works that are not included in the review, but the Turner and Malpezzi list of references contains more than 170 items, and an even longer list of 500 items is available from the authors upon request. And to criticize the review for being too exhaustive seems awkward. Instead, I will point at a completely different literature review, one that I would like to read.

The Turner and Malpezzi review deals with the effects of rent control on the demand for housing, the price and quality of housing, and the deadweight burden associated with rent control. Those issues are highly relevant—but as a citizen, I would be equally interested in the effects of rent control on income distribution and segregation. After all, the introduction of rent control is often (or always?) motivated by distributional concerns, and politicians—at least in Sweden—usually dismiss deregulation by referring to the segregation that would emerge in a free market. A review of scholarly investigations into these matters seems highly warranted. Do rent controls favour the poor or the rich? And do rent controls cause more or less segregation than a free market would do?

Let us look at the income distribution issue first, and start with the straightforward redistribution from incumbent landlords to tenants as a group. This is the kind of redistribution we first think of when we consider regulation or de-regulation of the housing market, and it is clearly covered by the studies in the Turner and Malpezzi review. There are, however, two caveats that need to be elucidated. First, is a redistribution from landlords to tenants the same as a redistribution from the rich to the poor? If the rental housing stock is mainly owned by pension funds, or the public sector, this is not necessarily the case. In fact, the City of Stockholm has been careful not to sponsor only housing projects targeted at the poor, but also to own a fair amount

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of attractive, prime-location rental dwellings in the centre of the city. In those cases, rent control obviously implies redistribution from taxpayers as a group, to the individuals who manage to secure rental contracts in those units.

Second, even if the landlords were rich individuals, and rent control thus could be motivated from a distributional point of view, the redistribution is not always as large as one may first think. Some of the loss is shared between the landlords and the taxpayers in the form of lower property taxes. The mechanism is simple. With no rent control, market prices of houses are high, and landlords will pay correspondingly high property taxes. With rent control, market prices of houses are lower, and thus the property tax base has been partly transformed into something much more subtle and evasive: the capital value of a lease in a rent-controlled apartment—an asset that is not taxable. Even the landlord, distributing this asset among eager applicants, might receive something in exchange (for example gratitude or control or some other claim on the tenants) and might thereby be able to recover at least part of the fall in the house price in the form of some non-taxable asset.

A review of these aspects of the redistribution between landlords and tenants, regarded as homogenous groups, would thus make for some interesting reading. An even more interesting issue is redistribution within the group of tenants. There is plenty of anecdotal evidence of rich people living in attractive, rent-controlled dwellings and paying only a fraction of what they would have paid for the same housing in an unregulated market. Every year, there seems to be a handful of top politicians, and a handful of wealthy businessmen, who are caught with their fingers deep in the cookie jar. Are these anecdotes representative, or are they merely conspicuous (but quantitatively insignificant) oddities brought out by the media and political adversaries? I would like to see a literature review of the empirical knowledge available on this point. And if there is no empirical knowledge, this would be an interesting piece of information too.

I am aware of a few empirical studies indicating that existing rent control schemes actually seem to benefit the rich. For instance, Pollakowski (2003) finds that the existing rent control in New York City provides no or only little benefit to the residents of lower and middle-income neighbourhoods, while providing a substantial subsidy only to the residents of the relatively affluent areas of Lower and Mid-Manhattan. A study by Early (2000) indicates a more complex pattern.

The average household in a rent-controlled unit in New York City is incurred a loss from rent control, i.e., when all price and quantity effects are accounted for, the average rent-controlled tenant would have been better off with no rent control. And the average household not living in a rent-controlled unit is incurred an even larger loss from rent control, i.e., the average non-controlled household would have been much better off if there had been no rent control. At the same time, these averages hide a large individual variation, and the overall distributional pattern is not very clear-cut. I would like to be gently guided through these, and other, studies to get a picture of whether different data and different research methodologies nevertheless yield some kind of consensus results regarding who gains and who loses.

The empirical problems are, of course, formidable. Apart from the endogenous price and quantity effects analysed by Early (2000), there are various life-cycle effects that have to be accounted for. Thus, even if it turns out that the households living in attractive rent-controlled apartments have low incomes, we would like to know whether these tenants are, in fact, the children of rich parents, living in chic neighbourhoods while they are “poor” students at law school—and very likely to be high-income earners later, when they have moved on, career-wise and housing-wise. What we would thus need is not only information about the tenant’s (present and future) income, but also about the tenant’s father’s income.

It all boils down to how the attractive apartments are allocated among the prospective tenants. Life-time income is highly correlated with connections (or social capital). How does that affect the allocation mechanism in the housing market? What kinds of insider-outsider problems do various types of rent control create? We all know anecdotes about union leaders or politicians providing nice housing for their children, and a survey of the empirical knowledge about allocation patterns is, I think, highly warranted. Here, too, the possible non-existence of empirical knowledge is interesting in its own right.

The allocation mechanism is also central to the second of my two questions, namely whether rent control causes more or less segregation than a free market. If apartments are allocated by connections, and connections are highly correlated with income, we might even observe exactly the same income segregation in a free market as in a controlled one—the only difference being that in the latter, the rich would pay lower rents, and the landlords correspondingly lower taxes.

Income segregation is not the only type of segregation relevant to social policy. The Stockholm housing market is rent-controlled and ethnically segregated, presumably because landlords prefer to hand out their scarce assets to others than immigrants. A study by Giffinger (1998) indicates a similar pattern in Vienna. The insider-outsider problem might be especially relevant to immigrants, and it is therefore possible that ethnical segregation is actually greater in a rent-controlled than in a free market.

It all depends on the allocation mechanism. Presumably, systems for allocation vary across cities and over time. And there is probably some discrepancy between notional and actual systems; what matters is not the political rhetoric, but the actual functioning of the system. A review of the literature on these issues could help the citizen see whether the bewildering mass of systems have some common features in terms of their actual functioning, and whether some conclusions could be drawn from such a fact.

References

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