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economic analysis of rent control

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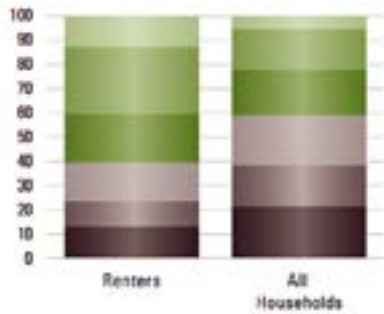
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In recent articles in the Quarterly, we have reviewed and analyzed the major changes to landlord tenant law in Portland and the state of Oregon.

RENTERS REFLECT THE DIVERSITY OF US HOUSEHOLDS, BUT ARE MORE LIKELY TO BE YOUNG, SINGLE, AND LOW-INCOME

SHARE OF HOUSEHOLDS (PERCENT)

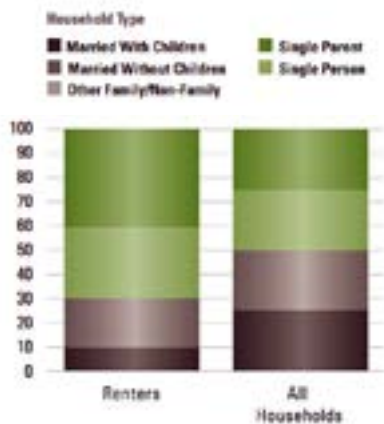
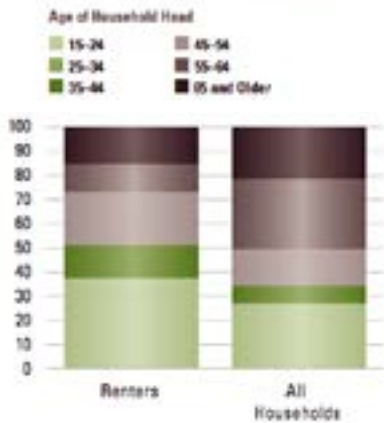


NOTES

Children are the householders' own children under the age of 18. Income quartiles are equal fourths of all households (both owners and renters) sorted by pre-tax household income. Other family/non-family includes unmarried partner households.

SOURCE

JCHS tabulations of US Census Bureau, 2010 Current Population Survey



As the regulations are new and we don't have much data to understand the effects, we are going to take a look at cities that have rent control laws and try to understand the intended and unintended effects that rent regulations can have. We will use rent control regulations as a guide to understand what Portland may expect from the recent increase of landlord and rental regulations. Rental housing is one of the largest and most important sources of housing in United States. Households of all demographics live in rental housing. New laws and regulations and their affects will be felt directly by a large part of our population. "Even during the homebuying boom of the early 2000's, [the percentage of households in] rental housing never fell below 30%" (Alexander, 2011).

Portland has enacted strict regulations on rental units and landlords, making renting very complex and risky to evict tenants and screen tenants; while also creating pricey penalties and relocation fees previously discussed in the Spring 2020 Quarterly. Senate Bill 608 enacting rent control is one of the most sweeping regulations Oregon landlords have ever seen. Statewide rent control caps rent increases to 7%+ CPI, while exempting buildings constructed in the last 15 years. The combination of state and local regulations is increasing cost and believed to be lowering the supply of multi-family development. (OLIS, 2019)

Rent control is one of the most debated ideas in real estate and housing policy. The goal is meant to help low- and middle-class income renters stay in their home and not fall victim to gentrification. We researched New York City, San Francisco, Cambridge and Los Angeles and the actual effects rent control legislation has had on these cities. It may come as a surprise but a healthy contingent of economists believe that rent control helps fuel higher rents and faster gentrification in these cities (Diamond, 2019).

Rent Control has a long and contentious history in the United States. Beginning on the East Coast in the 1920's and first appearing in New York City in the 1940's in response to the mass migration to the city during and after World War II (Gyourko, 1987). Spreading to the west coast in the 1970's with legislation passing in San Francisco and Los Angeles. In 2019 Oregon became the first state in the union to pass a statewide rent control act through senate bill 608.

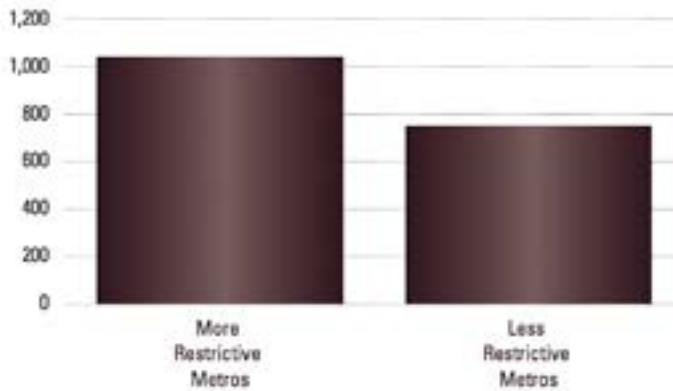
The broadly stated goal of rent control has always been to protect those in need of housing from losing their home due to rising rents. Rent control is designed to act as a safety net decreasing risk for tenants, preferably lower income tenants. Ideally rent control allows those working to not worry about losing their residence. Unfortunately, this is not what happens.

Rent control acts blindly and keeping rental rates low for anyone living in units defined as rent controlled. Income, occupation, and other personal factors are not taken into account. A study by the National Multifamily Housing Council found that "rent stabilization and control policies do a poor job at targeting benefits. While some low-income families do benefit from rent control, those most in need of housing assistance are not the beneficiaries of rent control" (Sturtevant, 2018). Adam Davidson of the NY Times points to a study by N.Y.U.'s Furman Center for Real Estate and Urban Policy, stating, "A majority of people in rent regulated Manhattan apartments make far above the poverty level." This is a common story in rent-controlled cities. The major benefit for rent control is for the households that are willing to stay put, not necessarily lower income households.

Rent control incentivizes tenants to stay in place regardless of their housing or job needs. A Stanford study of San Francisco in 2017 states, "Rent control increased renters' probabilities of staying at their addresses by nearly 20%" (Diamond, 2019). In some studies people were occupying much larger than needed units or vice versa. New young families are staying put in smaller units and possibly avoiding becoming home owners due to the cost protections afforded due to rent control (Diamond, 2019). This lack of mobilization negatively affects the supply and demand balance. Apartments that are then exposed to the market will have higher demand and high prices. Over time rent control will help far less than intended.

Additionally, rent control creates a ripple effect, taking supply off the open market and increasing the demand for unregulated apartments. The percentage of unregulated apartments varies depending upon the specifics of the city and state regulation. In Oregon, any building that is 15 years or younger is exempt from rent control. However, the unregulated sector will likely shrink over time as more apartment reach the 15-year threshold. Rent controlled units in NYC account for 45% of the total inventory, rent controlled units accounts for 75% of housing inventory in San Francisco and 80% of the inventory in Los Angeles (Katz, 2018). These restrictions on inventory are most common in the country's most expensive rental markets.

HOUSING COSTS ARE HIGHER IN AREAS WITH RESTRICTIVE LAND USE REGULATIONS
AVERAGE GROSS RENT, 2009 (DOLLARS)



As rent control decreases risk for renters, it increases risk for owners. Owners of multi-family units have less control over their investment and many studies have shown that rent controlled areas typically have high cases of deferred maintenance (Weiner, 2014). All business decisions must take into account the return on investment. Investors have a hard time justifying investing capital into properties where potential income is limited. Unfortunately, the regulation creates a Catch-22 and will lead to less desirable and neglected properties.

The long term effect of deferred maintenance is that the value of the neighborhood begins to decline. For any city, this will lead to a loss of revenue as property values and property taxes fall. We saw this direct affect when Cambridge, MA disbanded rent control. A study from Massachusetts Institute of Technology (MIT) estimated that the city had lost out on 2 billion dollars of taxable revenue over 10 years due to rent control (Autor, 2014). The income generated from this taxable revenue could be used towards schools, job training or other targeted affordable programs.

Real estate owners are business savvy and will find a way to earn a return on their investment. In many places, owners are allowed to evict tenants for a demolition of the property or can change the use of the property to for-sale condos or even creating tenancy-in-common (TICs) ownership structures. These change of uses or transfers allow the building to side step rent control. The study out of Stanford also stated that in their research, "Landlords treated by rent control reduced rental housing supply by 15%, causing a 5.1% city-wide rent increase." The obvious problem of the change of uses is that rental supply in the city is again restricted which in turn increases the demand and therefore price of rent. Could Portland see an increase in condo associations and TICs? Doubtful, but it could be possible.

In conclusion, we can see from the many studies on the subject that cities and states that enact broad rent controls end up doing more harm than good. Rent control does not specifically help the people most in need, it helps those that are able to stay put the longest, regardless of income level. Regulations such as rent control, tenant screening, and mandatory relocation fees only increase costs, decrease supply, and drive up prices. If the Portland metropolitan area and the state of Oregon want to see actual progress and equity in housing, they need to get creative and incentive the development of more housing units. The increase in supply will satisfy the demand and allow rents to moderate. More importantly, state and local leaders need to target households in actual need and help them find safe and affordable housing. Blanket policies along with vilification of developers and landlords does more harm than good.

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