

A recipe for lower house prices

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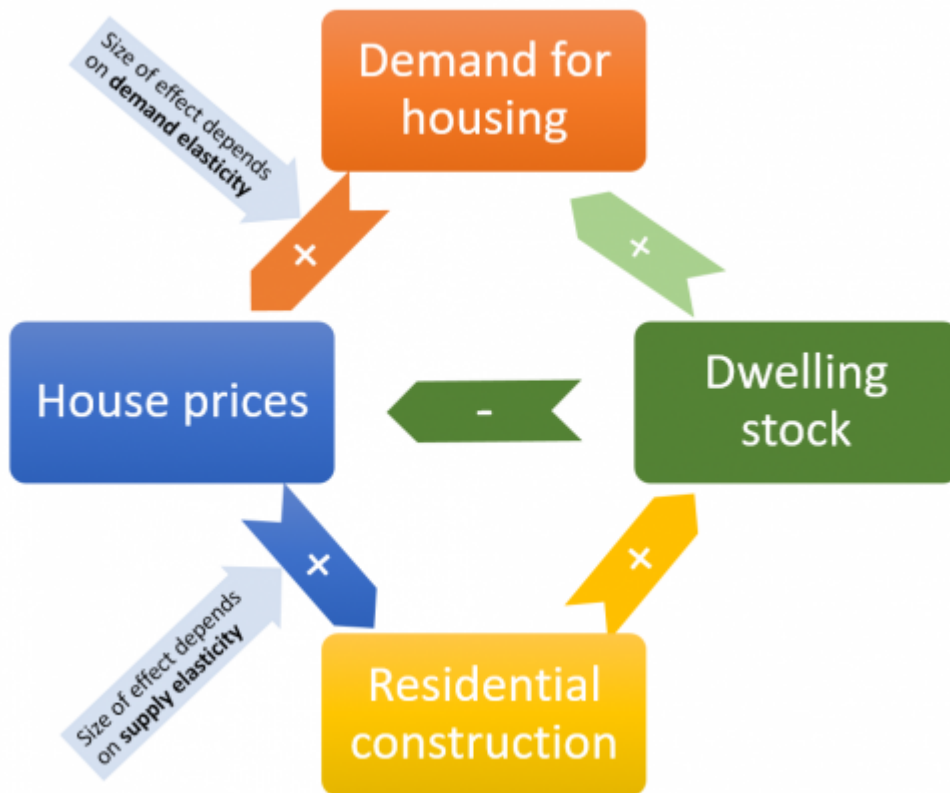
<https://www.oecd.org/housing/policy-toolkit/>

Does housing need to become always more and more expensive relative to other services, eating an ever-higher share of income? This situation puts a strain on household finances, making it complicated for people to move close to jobs and often generating macro-economic or financial risks. The economy's capacity to meet the demand for housing and supply dwellings where they are demanded is crucial to avoid these excessive price and rent increases, contribute to macroeconomic stability and facilitate residential mobility. The OECD has recently launched a report entitled "Brick by Brick: Building Better Housing Policies" to help analysts and policymakers make better housing policies. At its core, one of its chapters focuses on the fundamental drivers of housing supply and demand and the relevance of housing policies to ensure affordable and quality housing for all.

The empirical framework underlying the analysis builds on the famous stock-flow model for housing in which i) a positive (negative) shock to housing demand increases (decreases) house prices, ii) higher (lower) house prices boost (reduce) housing investment, and iii) higher (lower) supply of housing feeds back into house prices and partly offsets the initial demand

shock. In this framework, demand and supply elasticities jointly determine how much of a change in demand feeds into prices and how much into construction.

Figure 1. Stock-flow model of housing



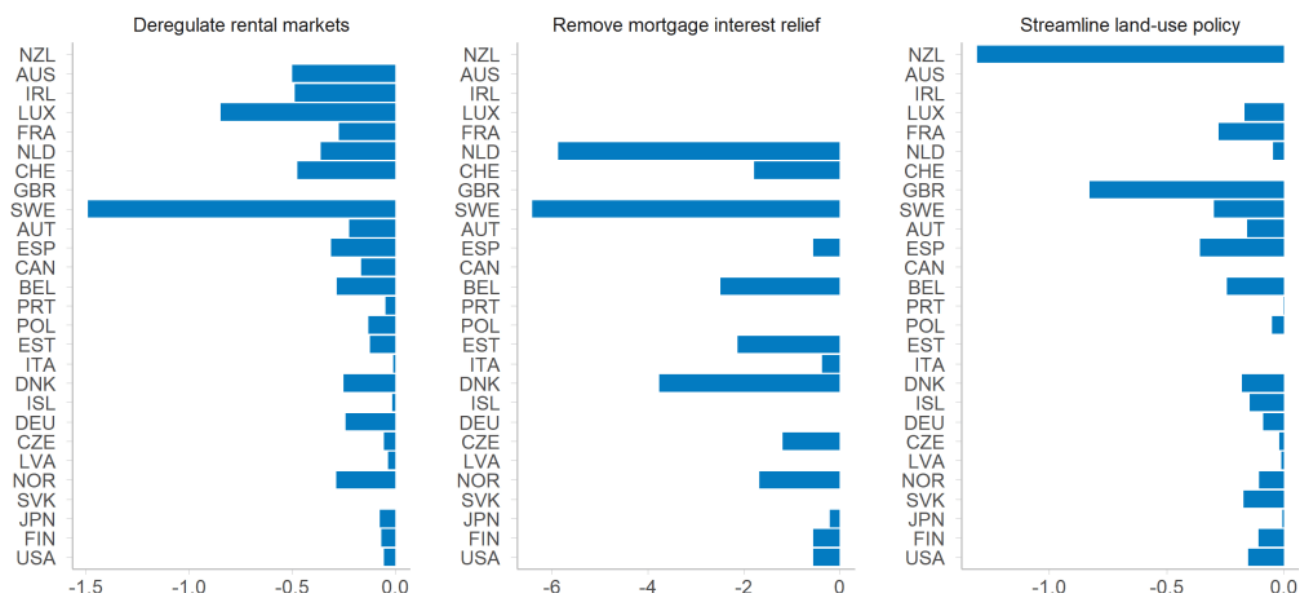
These elasticities depend to a great extent on housing-related policies.

- Eliminating mortgage interest deduction, for instance, mitigates house prices increases amid demand pressures (lower demand elasticity).
- A high degree of decentralisation of land-use decisions is generally associated with more restrictive land-use policy settings consistent with the home-voter hypothesis (lower supply elasticity).
- Strict rental market regulation inhibits new construction by reducing the incentives to invest in rental housing (lower supply elasticity).

These housing-related policies differ considerably across countries. Accordingly, expected benefits from moving towards

best policy practices also vary across countries and policy tools. Figure 2 illustrates the expected reductions in house-price to income ratios.[1]

Figure 2. Housing affects society and the economy in multiple ways



Note: Simulated change between 2020 and 2050 in the number of years over which cumulated average household disposable income equals the average price of a 100m² dwelling (in years).

Source: OECD (2021), Brick by Brick: Building Better Housing Policies, OECD Publishing.

Residential construction is simulated to expand by more than 20% in Sweden if rent control becomes as flexible as in New Zealand, increasing the housing stock in 2050 by around 11%, which could reduce house prices in Sweden by around 1.5 years of disposable income for the typical 100m² dwelling. Sweden, alongside the Netherlands, would also be the largest beneficiary in terms of housing affordability from eliminating mortgage interest deductibility. New Zealand, in turn, could boost affordability the most by streamlining the governance of land-use policies across levels of government.

These examples illustrate the great potential of housing policy reforms. Many more are discussed in the report. A dedicated Policy Toolkit including an online Dashboard and

Country Snapshots allows policymakers to compare their country's housing outcomes and policies. Finally, a Policy Action Tool helps implement such reforms by anticipating synergies and trade-offs across various outcome dimensions.

[1] Measured by the reduction, compared to the baseline of no policy-change, in the number of years over which cumulated average household disposable income equals the average price of a 100m² dwelling.