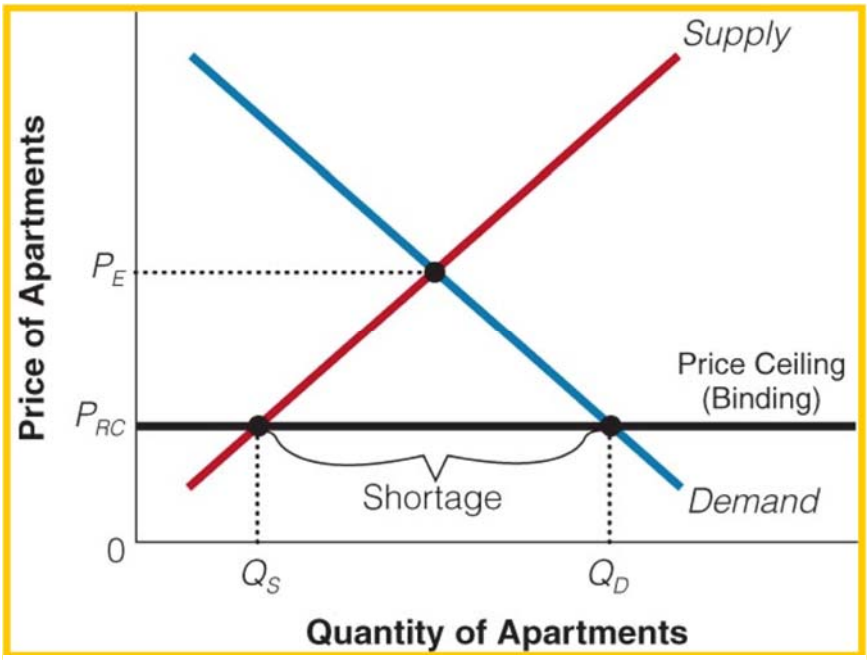
IS RENT CONTROL EFFECTIVE?

DAMANJIT HUNDAL

Rent control is a price ceiling that limits landlords from capriciously raising rental prices and is used to create affordable housing. By setting a maximum price, or a rate at which a landlord can increase the rent price year-to-year, a situation occurs where prices are being artificially lowered. This type of price control leads to a shortage of housing units. Some cities in California still adopt this policy to combat landlords from abusing the high demand placed in certain areas for living. Not all dwelling units are rent controlled. In some cities, units are rent controlled only if they were built before a certain time period. With a housing shortage in the rent controlled sector of a city, the excess demand for housing spills over to the non-controlled sector. The high demand and the low quantity supplied boost prices in this non-controlled sector. So, even though prices in the rent controlled sector might be low, the rents in the uncontrolled sector greatly rise creating a higher average price for rental housing as a whole. Price ceilings not only reduce the quantity of housing available, it also reduces the quality of the units.

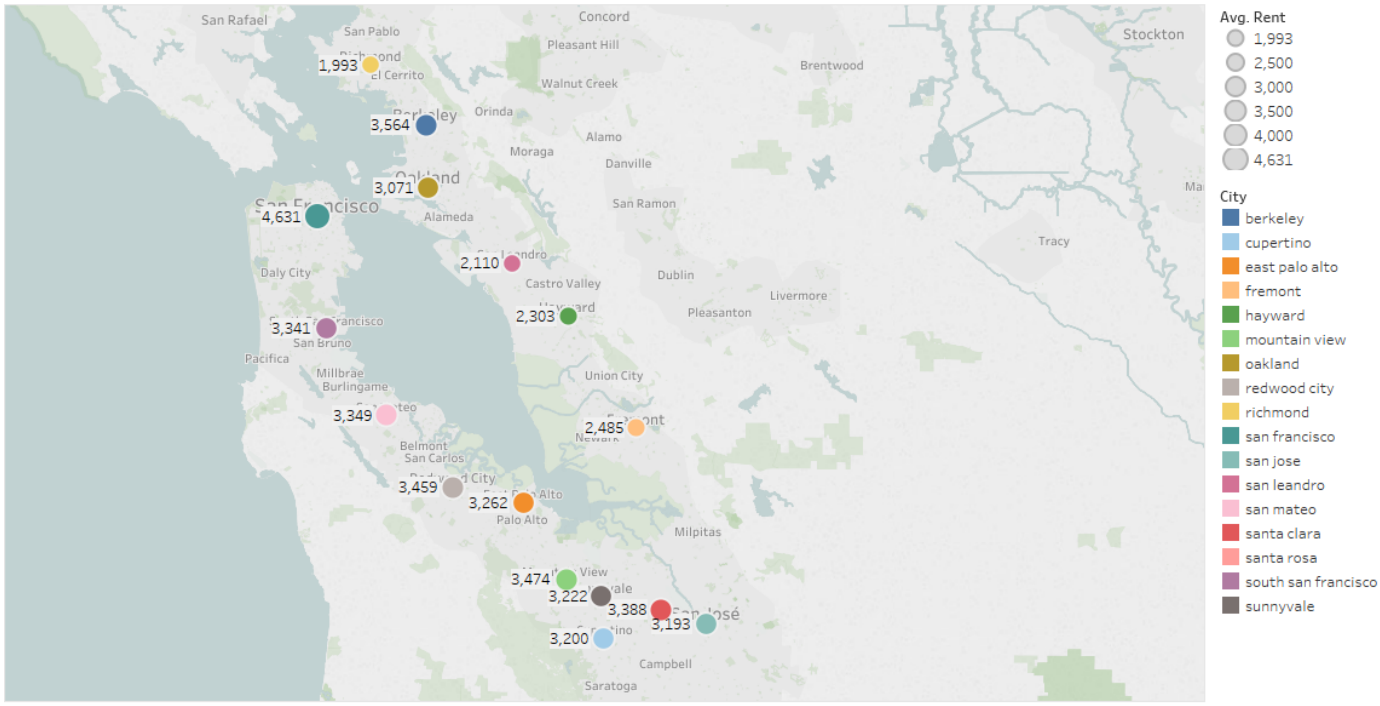


By creating a price ceiling, a shortage in supply occurs equaling to Q_D - Q_S. The price ceiling artificially lowers the price compared to what it would be in a free market.

Rent control discourages construction of homes and buildings because it limits the amount of profits owners can earn. It also discourages owners and investors in upgrading homes when needed because the benefits of upgrading might not outweigh the burden the costs create. Also, the high demands in these rent controlled housing leads to very low vacancy rates, not giving enough time for landlords to properly upgrade the house. The landlord would rather continue to rent a place with the minimum quality for habitability than keep the unit empty and upgrade it losing precious value and money.

The bay area is a particular region in California that government officials think rent control is needed. The high demand for housing in this area is caused by the natural beauty in the setting, the diversity and culture of the people, a strong regional economy, a very large job and technology sector, and high quality public services. Some of the challenges to carry construction in this area include geographical constraints due to the ocean, bay, and steep hills, the cost constraints of redeveloping already urbanized land, stringent zoning laws, and land use regulations that prefer lower density development and single-family homes over apartment buildings. These regulations are usually voted in, where the majority of voters are homeowners in the area who prefer these lower density developments in their own neighborhoods for a more relaxing setting. Due to the high demand and the supply constraints, rental prices in the bay area are considerably higher than the national average and even California's average. The national average rent for a 2 bedroom unit is $1,250, while in California the average rent is $2,000. Looking at the map below, the average rent in these cities are mostly above $3,000. In cities like San Francisco, Berkeley, Oakland, East Palo Alto, Los Gatos and San Jose, the average rent is all above $3,000/month. So government officials might look at these cities and promise to curb the rising prices to their constituents by implementing rent control and stabilization policies, but the outcome of these implementations often counter what it promises. It's like trying to turn a knob to shut down water flow, but the outcome of turning that knob produces higher flow causing more erosion and more problems.

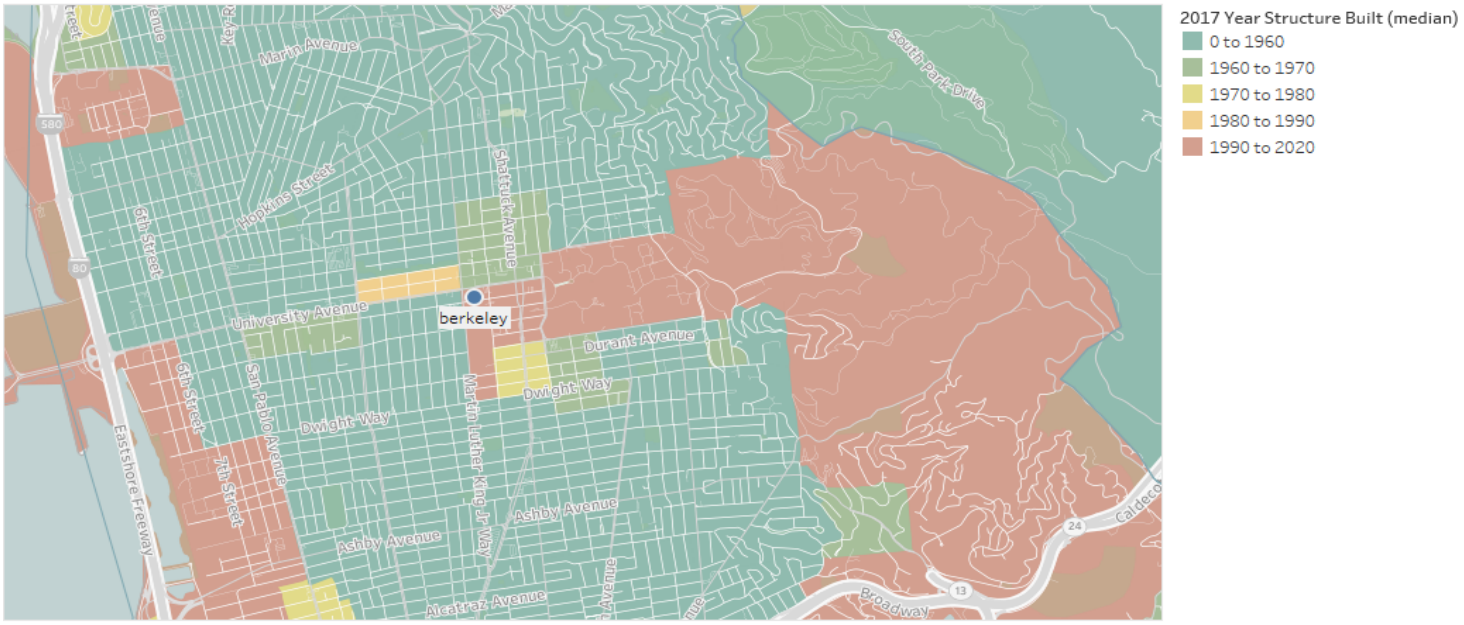
Average Rent in 2BR Unit in Bay Area Cities



Map based on Longitude (generated) and Latitude (generated). Color shows details about City. Size shows average of Rent. The view is filtered on City, which keeps 17 of 17 members.

The cities that are put on rent control have special circumstances that make officials adopt these policies because they think that something needs to be done. In a free competitive market, high demand would be eventually met by more supply because developers would have incentives in profits for building more housing units. However, in certain cities, building more units can be met with many constraints as noted above. Not too long ago, I was a UC Berkeley student transitioning from living in the dorms to off-campus housing. What I thought to be an easy transition turned out to be a journey filled with stress, frustration, agony, and often times, defeat. Throughout the process of looking for housing near the UC Berkeley campus, I would often go to open houses where more than 15 other groups were also looking at the same unit. The sheer number of competition was not the only problem, the low quality of these houses made people second guess spending a large sum of money on rent for an inferior product.

Year Built (Median) in Berkeley



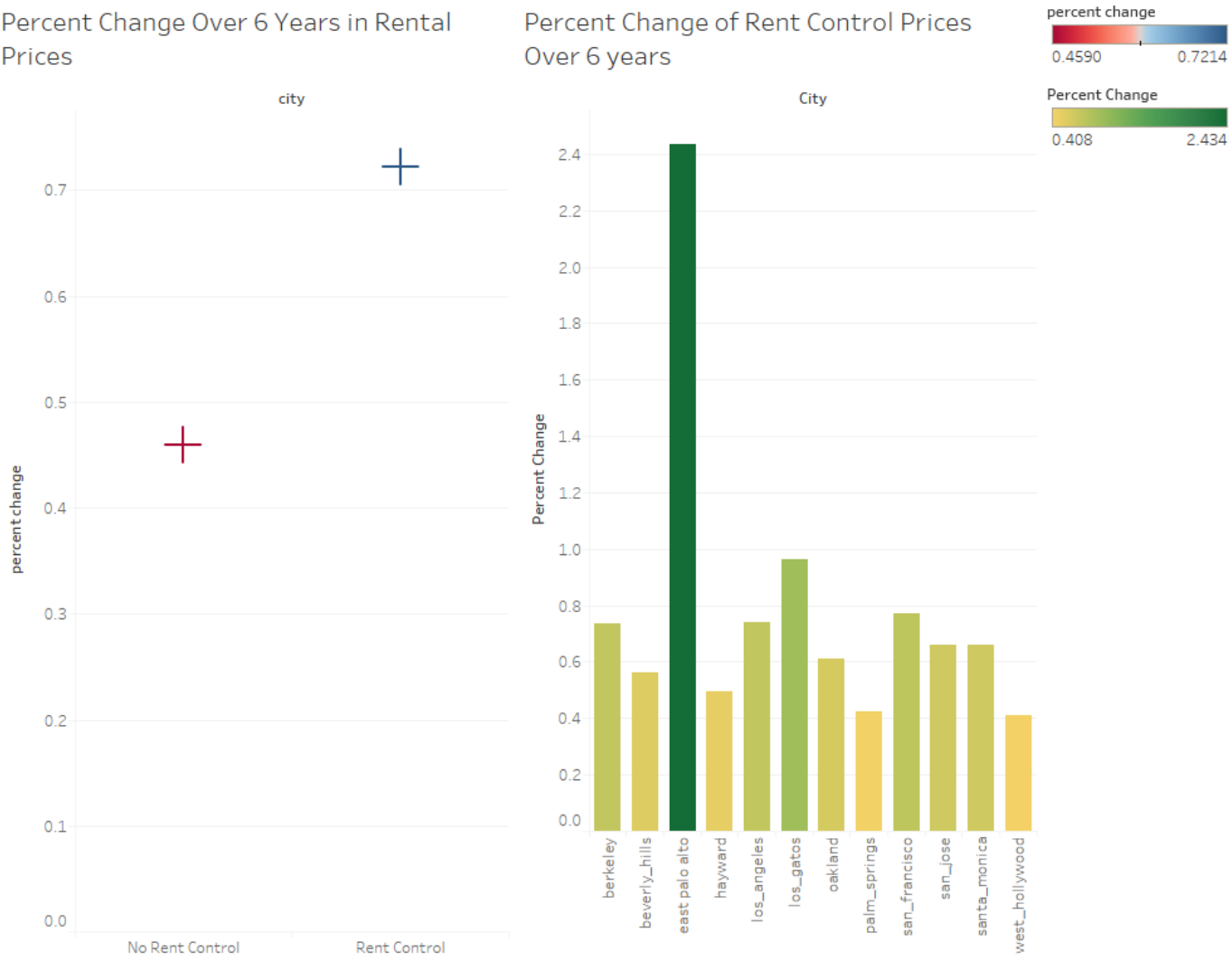
Map based on Longitude (generated) and Latitude (generated). The marks are labeled by City. Map coloring shows 2017 Year Structure Built

In the plot above, I've shown the year in which units were built in Berkeley, with the majority of housing being built before 1980. The region which is colored red belongs mostly to the UC Berkeley campus. Buildings with two or more units built before June 30, 1980 have both eviction protection and rent increase limitations, whereas buildings built after that date have only eviction protection. Eviction protection means that tenants can only be evicted if they have done something to violate Good Cause Ordinance. Landlords cannot just kick tenants out because of retaliation or other unjust causes. The rent control limitation applies to the majority of rental housing in Berkeley because most properties were built before 1980. Predictably, the house that I would later find to live in was built in 1913. The house had 8 bedrooms and rent for the whole house was initially $6200/month, with my responsibility being about $700/month. It was located a mile uphill away from campus with limited bus transportation. It had carpets in some rooms that were only a few millimeters thick ladened with black spots, a musky smell that radiated through all the rooms, bathrooms without any air filtration system, and walls so thin you could hear the other person writing down notes in their room. Overall, it was barely livable and it was apparent that the landlord did not make any effort whatsoever to make any upgrades or make any more investments on the house. Why would he? In 1999, Berkeley was under full vacancy decontrol, which meant that landlords could raise the rental price of a unit to market value after the tenant moves out. If someone was paying $700/month when they initially moved in and the landlord increased the rent with inflation each year, they might be paying about $900/month after 10 years living in the same place. Once that tenant moves out, the market value of that unit might drastically rise to $3,000/month or more. In Berkeley, where there is a low vacancy rate and high competition to live, landlords don't worry about whether a tenant wants to live there for a long time. If tenants move out quicker due to quality complaints, then great, the landlord can set rents at market value once that tenant is out. I repeatedly worried about this scenario when I was living in the house, because I thought if I would complain about the quality, the landlord would kick our whole group out and quickly replace us with another group. I did not know much about real estate at that time, so my fear of eviction was rightfully placed. Since 1999, 85% of rent controlled units have been turned over at least once and the rents have increased to the typical market value of the dysfunctional Bay Area housing market.

Berkeley is a special city because students do need a place to stay to attend college, preferably close to campus so that they don't spend valuable time commuting back and forth from campus to home. Berkeley also is close to many job opportunities, where employees commute to their work, oftentimes outside of Berkeley. UC Berkeley only guarantees one year of living in student housing, so most students have to find off-campus housing in their second year. Students not only have to compete with other students, but other people that are looking to live in Berkeley. Most of the space near the UC Berkeley campus is already developed, so creating more supply in this area is very hard. With limited supply, and high demand for living, prices in this area would skyrocket in a free market, until suppliers decide there is enough incentive to build in the area. Imposing price ceilings further limits any more supply in the area causing a shortage, further developing higher demand. So Berkeley is faced with a dilemma, either let prices skyrocket in a free market, or impose rent control to curb increasing prices. In either case, prices will increase as explained earlier. The simple solution would be to increase the supply to dilute the demand. But, as mentioned before, suppliers don't have enough incentives to build in this area. They would rather develop in other cities where constraints are not a problem and enjoy easier profits. So some form of tax incentives and subsidies need to be provided to suppliers to build more. Otherwise UC Berkeley needs to provide housing for their students by creating more developments. Rent control alone is not effective due to the low quality and quantity of housing, and something needs to be done along with it to increase the supply.

Comparing the increase between rents in rent controlled cities versus cities where rent control is not implemented, it can be easily seen that rents increase at a higher rate in rent controlled cities. In rent controlled cities, rents over a 6 year period changed by 72.14% compared to 45.90% in cities where rent control is not enforced. This is further proof, that cities that implement rent control, where the initial promise is to limit the rate at which rents increase year to year, are the same cities that have a higher percentage increase in rents from year to year. Rent control is not effective alone, an effort needs to be made to increase the housing supply in these areas so that housing can become affordable. In a

competitive market, competition between suppliers will reduce the price to the minimum needed to profitably operate and maintain rental housing. The solution would be to create incentives to bring more suppliers in these markets.



Another reason why rent control is not effective is that people that are in a low-income situation cannot live in cities where rent control is enforced because they do not have the means to pay the rent as it will cause a high burden on their overall income. The people living in rent controlled units will occupy that unit longer, creating a limited amount of options for low-income people. People that have the means to live in higher rent areas are more likely to stay put in their current unit, knowing that rent prices will only gradually increase thus providing them with lower burden on their income compared to if they were to move out of their unit and into a place where it is marked at market value. So the people that suffer the most in these rent control cities are the same exact people that were thought of when implementing rent control policies.

Living in a rent controlled city myself, brought to my attention the problems and challenges to create affordable housing. Demands in these cities are not likely to waver, so supply needs to be increased by providing incentives to suppliers and developers. This would also improve the quality of rent controlled units, because landlords are now competing with units that are just built and modernized with better appliances and utilities. Government officials have their heart in the right place in trying to implement rent controls in certain cities, but paradoxically the outcome is quite the opposite of the intended effect. The affordable housing problem is an apparent one that directly interacts with many people trying to find housing in high demand cities. Different policies besides rent control need to be implemented so that both tenants and landlords are happy. A free market might theoretically work, but maybe there are other options to provide affordable housing to people who don't want their rents to cause a high burden on income.

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BONUS PICTURE