Application of Economic Theory (“Memorandum on Rent Control in Seattle, Washington”) Excerpt

What

Case study produced in an introduction to economics course at UIC. I was the sole author and researcher on the case study. In the paper, I attempted to detail a new theory of New York-style rent control and how it bifurcates housing markets into controlled and uncontrolled housing. It demonstrates a willingness to engage new ideas on key planning issues including housing availability.

Work Performed

- Solely wrote the memorandum.
- Created graphics to convey proposed scenario.
- Conducted literature review to support arguments.

Why

- Report & proposal writing
- Application of economic theories to potential scenarios

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Case Memo 1
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Rent control in Seattle, Washington

Summary

This memorandum evaluates the impact of rent control on the Seattle housing market. Economic modeling shows that introducing rent control into the City of Seattle would limit the price of housing while reducing the quantity available. A price ceiling creates excess demand and prevents the market from reaching equilibrium. American cities typically only introduce rent control in some of the housing stock, creating a bifurcated market of rent controlled-housing and market rate-housing. Economic modeling shows that prices remain stable in the small rent controlled-housing market; in the market rate-housing group both quantity decreases and price increases. However, additional economic studies have shown that modern rent control does not limit housing supply, create housing shortages, or hurts the local economy and tax revenues. Other available affordable housing policies - such as vouchers and inclusionary housing policies - do not adequately satisfy demand. Therefore, moderate rent control is recommended for implementation in Seattle.

Economic Models

Rent control is a type of price ceiling on the housing market. An effective price ceiling is one which sets the maximum price below market equilibrium. This action does not directly affect the supply and demand for housing in a region, but does reduce both the price and quantity of housing offered. **Figure 1** shows the impact of rent control on a housing market. In some cases, a

price ceiling may be ineffective, in which the maximum price is set at or above the equilibrium point; this has no effect on price or quantity in the market.

American cities typically implement rent control on a portion of the housing stock (between 10-40%). This policy creates a bifurcated housing market; this result can be shown in two separate curves. **Figure 2** shows the rent controlled market; because the rent-controlled housing stock is typically stable and does not increase, supply becomes fixed and is represented vertically. The price ceiling on this model creates a much larger excess demand; consumers seek more housing, and suppliers seek higher rents to maximize profits. This outcome is not Pareto efficient. **Figure 3** shows the remaining housing market; because a portion of the housing market is removed from the supply, both the quantity is reduced and the price increases. Therefore, rent control may have a negative effect on the remaining non-controlled housing market.

The above models rely on several assumptions including, but not limited to: all housing is of equal quality; housing supply can be increased over time; all consumers have similar incomes; landlords prioritize prolit-maximumization over other outcomes; that demand remains stable (neither decreasing nor increasing); and that both consumers and suppliers have equal and full access to information. The economic models show that, generally, rent control decreases the quantity offered, creates excess demand (leaving some people without housing), and decreasing profits for landlords, and may additionally increase prices on any housing without price controls.

Additional Information

A review of the literature concerning rent control creates a more nuanced view. Head & Lloyd-Ellis noted that renters in controlled housing become immobile, as they are unlikely to give up their affordable home. This reduces their ability to take advantage of economic opportunity elsewhere, but also increases long-term tenancy rates (2012, p. 1577).

When rent control was repealed in Massachusetts, prices on both rent-controlled and non-controlled units increased as more affluent consumers outbid the previous poorer tenants (Autor, Palmer & Pathak 2014, p. 663). This observation contradicts standard economic modeling, which predicts that price would decrease overall in a bifurcated market after rent control is removed.

In New York City (where over 30% of units are rent controlled), the vacancy rate was 2.88% which compares favorably to the national vacancy rate of 10.1%; this observation contradicts the assumption that rent control decreases the quantity of housing offered (Collins, p. 3). Boston saw a 25% in vacancy rates after deregulation, but also saw median rent double within a decade (Collins, p. 4). Furthermore, Collins noted that eras of stringent rent control have co-existed with construction booms in New York City; this contradicts the economic modeling where rent control may inhibit supply long-term as landlords believe they will not profit in a controlled market (p. 3-4). Collins also noted that landlords earned stable profits in rent controlled buildings (pp. 7, 12); the quality of housing was overwhelmingly sound and not dilapidated (p. 13); and that the decrease in property taxes could be countered by improved sales tax and a stimulated economy under rent control (p. 13).

Finally, the alternatives to rent control do not adequately satisfy the demand for affordable housing. Two common programs include housing vouchers (such as the federal

Section 8) and inclusionary housing (where developers have to offer or build a set percentage of their units at affordable prices; however, these programs typically have hundreds to thousands of applicants for every voucher or affordable unit available (Metcalf 2018, p. 63). The European example (as seen in Vienna) is for the municipality to build all housing for low and middle-income tenants; activist Catherine Bauer noted: "The land, construction, finance, and management of… low- and medium-cost dwellings were removed from the speculative market: housing became a utility." (Metcalf 2018, p. 61). Such a program would be a substantial undertaking and is atypical for an American city.

Recommendation

Standard economic models predict that under rent control housing markets will have reduced quality and excess demand. However, additional review of rent control in practice - formerly in Boston and currently in New York - do not concur with the predictions of economic models. Furthermore, the alternatives to rent control do not adequately reach the desired outcome. Therefore, this memorandum suggests that rent control should be considered and implemented in Seattle.

Figure 1: Standard Rent Control Model

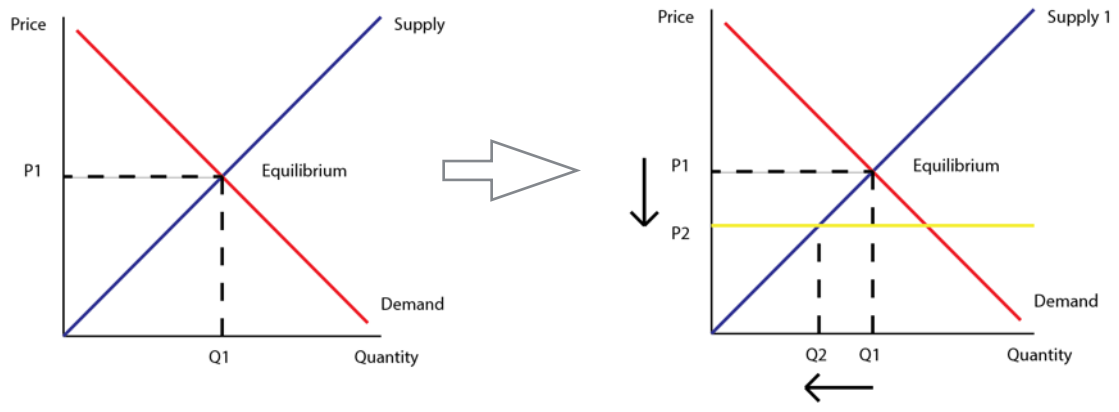


Figure 2: Bifurcated Market - Rent Controlled Housing

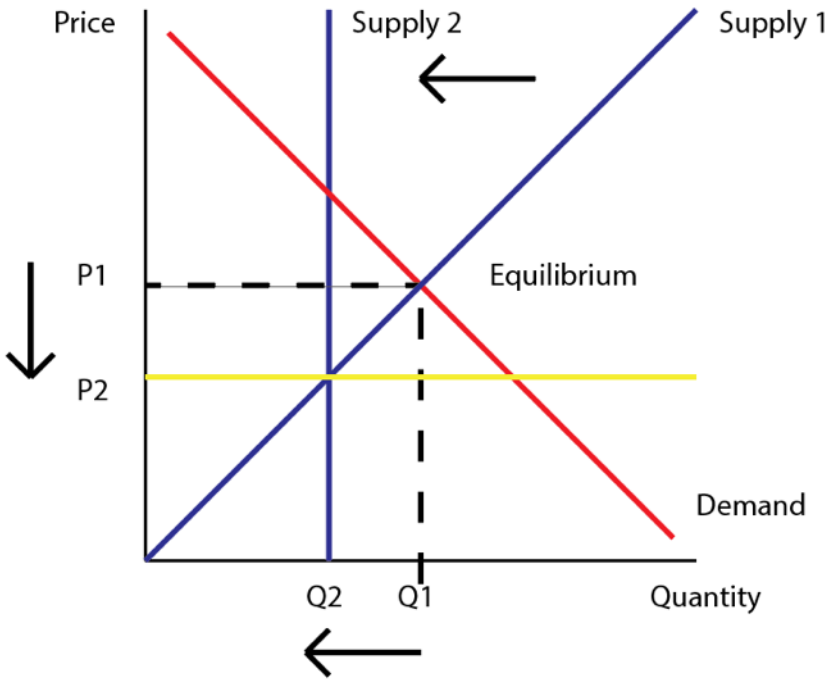
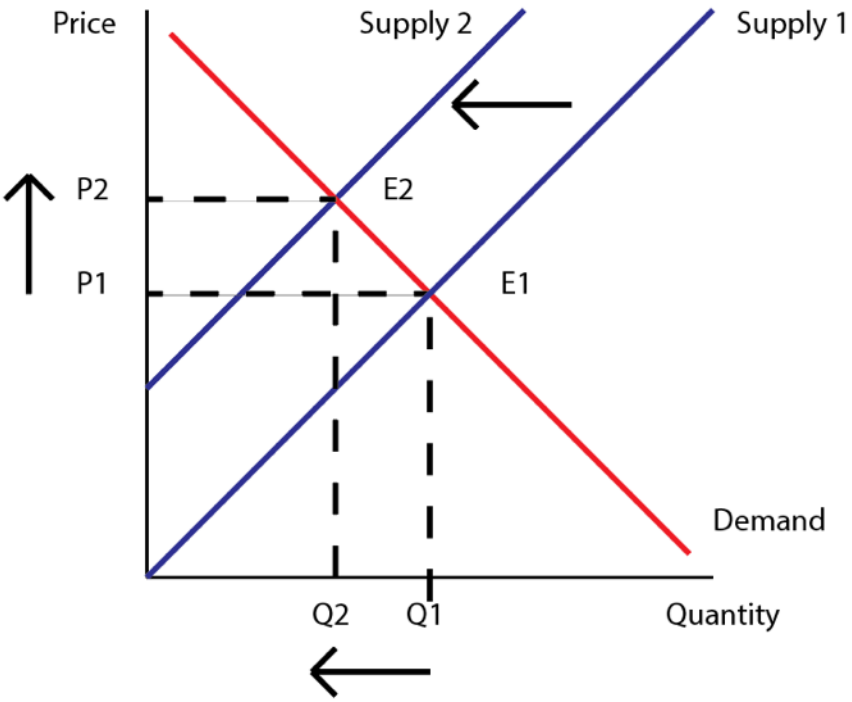


Figure 3: Bifurcated Market - Market Rate Housing



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