Housing- Shaking the Foundations

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Housing is at the root of many of the rich world's problems

Since the second world war, governments across the rich world have made three big mistakes, says Callum Williams

The financial crisis of 2008-10 illustrated the immense dangers of a mismanaged housing market. In America during the early to mid-2000s irresponsible, sometimes illegal, mortgage lending led many households to accumulate more debt than they could sustain. Between 2000 and 2007 America's household debt rose from 104% of household income to 144%. House prices rose by 50% in real terms. The ensuing wave of defaults led to a global recession and nearly brought down the financial system.

From the 1960s to the 2000s a quarter of recessions in the rich world were associated with steep declines in house prices. Recessions associated with credit crunches and house-price busts were deeper and lasted longer than other recessions did. Yet the damage caused by poorly managed housing markets goes much deeper than financial crises and recessions, as harmful as they are. In rich countries, and especially in the English-speaking world, housing is too expensive, damaging the economy and poisoning politics. And it is becoming ever more so: from their post-crisis low, global real house prices have since risen by 15%, taking them well past their pre-crisis peak.

Traditionally politicians like it when house prices rise. People feel richer and therefore borrow and spend more, giving the economy a nice boost, they think. When everyone is feeling good about their financial situation, incumbent politicians have a higher chance of re-election.

But there is another side. Costly housing is unambiguously bad for the rich world's growing population of renters, forcing them to trim spending on other goods and services. And an economic policy which relies on homebuyers taking on large debts is not sustainable. In the short term, finds a study by the imf, rising household debt boosts economic growth and employment. But households then need to rein in spending to repay their loans, so in three to five years, those effects are reversed: growth becomes slower than it would have been otherwise, and the odds of a financial crisis increase.

Malfunctioning housing markets also hit the supply side of the economy. The rich world's most productive cities do not build enough new houses, constraining their growth and making them more expensive than they would otherwise be. People who would like to move to London, San Francisco or Sydney cannot afford to do so. Since productivity and wages are much higher in cities than outside, that reduces overall GDP.

So it is bad news that, in recent decades, the rich world has got worse at building new homes. A recent paper by Kyle Herkenhoff, Lee Ohanian and Edward Prescott argues that in America this process has "slowed interstate migration, reduced factor reallocation, and depressed output and productivity relative to historical trends". Constraints on urban growth also make it harder to reduce carbon-dioxide emissions, since big cities are the most efficient built forms. In America there are more building restrictions in places which have lower emissions per household.

Housing is also a big reason why many people across the rich world feel that the economy does not work for them. Whereas baby-boomers tend to own big, expensive houses, youngsters must increasingly rent somewhere cramped with their friends, fomenting millennials 'resentment of their elders. Thomas Piketty, an economist, has claimed that in recent decades the return to capital has exceeded what is paid to labour in the form of wages, raising inequality. But others have critiqued Mr Piketty's findings, pointing out that what truly explains the rise in the capital share is growing returns on housing.

Other research, meanwhile, has found that housing is behind some of the biggest political shocks of recent years. Housing markets and populism are closely linked. Britons living in areas where house prices are stagnant were more likely to vote for Brexit in 2016, and French people for the far-right National Front in the presidential elections of 2017, according to research from Ben Ansell of Oxford University and David Adler of the European University Institute. Political disputes sparked the protests in Hong Kong, but the outrageous cost of accommodation in the city-state has added economic fuel to the political flames.

This special report will argue that since the second world war, governments across the rich world have made three big mistakes. They have made it too difficult to build the accommodation that their populations require; they have created unwise economic incentives for households to funnel more money into the housing market; and they have failed to design a regulatory infrastructure to constrain housing bubbles.

Happily, they are at last starting to recognise the damage caused by these policies. In Britain the government now openly says that the housing market is "broken". Scott Morrison, Australia's prime minister, has pledged to make housing more affordable. Canada's recent election was fought partly on who would do more to rein in the country's spiralling housing costs. Carrie Lam, Hong Kong's chief executive, has put housing front and centre in her response to the protesters.

They need to learn from places where the housing market broadly works—and those places do exist. As this report shows, flexible planning systems, appropriate taxation and financial regulation can turn housing into a force for social and economic stability. Singapore's public-housing system helps improve social inclusion; mortgage finance in Germany helped the country avoid the worst of the 2008-10 crisis; Switzerland's planning system goes a long way to explaining why populism has so far not taken off there. Governments across the world need to act decisively, and without delay. Nothing less than the world's economic and political stability is at stake.

What is the future of the rich world's housing markets?

It is plausible that house prices could persistently rise faster than incomes

Moore's law states, roughly, that computing power doubles every two years. Time and again experts predicted its demise—surely, they reasoned, computers cannot continue getting exponentially more powerful. Yet it held for at least half a century.

More people are starting to wonder whether housing may have its own version of Moore's law. Over the past 70 years global house prices have more than quadrupled in real terms. They are far beyond their pre-crisis peak. It may seem mad, but a paper from David Miles, formerly of the Bank of England's monetary-policy committee, and James Sefton of Imperial College London finds that "in many countries it is plausible that house prices could now persistently rise faster than incomes". A growing population and rising incomes increase demand for housing, which runs up against a fixed supply of land in areas where the good jobs are, and limits to improvements in transport speeds.

As this report has argued, high property prices are associated with less economic dynamism and more financial instability. But although Messrs Miles and Sefton say that ever-pricier property is "plausible", they do not say it is inevitable. To keep housing costs down in the long term, governments need to get three things right.

The first is better regulation of housing finance. Switzerland comes close to treating home-ownership and renting equivalently in its tax system, meaning that people are not encouraged to funnel capital into the housing market. More countries should follow that example. President Donald Trump's tax reform of 2017, which limited mortgage-interest deductions, is a step in the right direction.

More radical reforms could be considered. German mortgage-lenders embrace an unusual appraisal technique. When assessing the value of a house, they rarely refer to market price; instead they consider "mortgage-lending value", an assessment of the probable price of a house over the economic cycle. A report from the Bank for International Settlements, a club of central banks, suggests that by discounting short-term price fluctuations, this valuation technique can stop bubbles from forming. Lenders in America once embraced the technique, points out Ed Pinto of the American Enterprise Institute, a think-tank, yet after the second world war it fell out of fashion.

The second group of reforms concerns transport. Until the mid-20th century, house prices were stable in part because the cost and ease with which people could get around improved roughly as quickly as economic growth. As getting from a to b became ever quicker, it increased the amount of developable land at an economy's disposal. But after the second world war improvements in transport slowed, meaning that more and more people were fighting over the same amount of space. That caused house prices to rise.

More recently, commuting times into the rich world's biggest cities have, if anything, been lengthening, raising the premium of living near or in city centres. A better train and road network, then, would allow more people to live farther afield. Driverless cars could also reduce the hassle of moving around. (And when video-conferencing is fully reliable, more people may be willing to live miles away from their office and call in for meetings.)

The third set of reforms concerns planning. This report has argued that governments are finally waking up to the fact that there is a structural undersupply of housing. They could learn from best practice internationally. Devolving taxes to the regional or local level, the norm in Switzerland, gives local governments a stronger incentive to allow development.

Cheaper housing would make politics less volatile

France has followed the Swiss example in increasing pressure on local governments to raise revenue from property taxes, “which can in turn lead to efforts to stimulate land development”, according to the oecd. Abolishing single-family-home zoning, which prevents densification, is another good option—and something Minneapolis did last year. Boosting the construction of public housing is also welcome. Singapore, where 80% of residents live in government-built flats, is in some respects the model to copy. The state regularly renovates the buildings and, more controversially, promotes mixing of different sorts of people, to help prevent the emergence of ghettos.

Rome wasn't built in a day
The gains from allowing more building would be enormous. According to one paper American gdp could be around 10% higher if there were plentiful new construction in just New York, San Francisco and San Jose. Cheaper housing would also make politics less volatile: a growing body of research shows that support for populist parties is particularly likely in countries where people cannot afford to move to the big cities, and are thus trapped in “leftbehind” places.

Some housing experts are sceptical about whether any democratic society would ever countenance such a building surge. They are too pessimistic. In Japan a series of reforms in the early-to-mid-2000s loosened the planning system, allowing applications to be processed more quickly and giving residents more discretion over how to use their land. Tokyo’s rate of housing construction has risen by 30% since the reform; in 2013-17 Tokyo put up as many houses as the whole of England. Tokyo is a more jumbled city than most rich ones, but current zoning laws ensure that it is not quite as higgledypiggledy as, say, Houston. In inflation-adjusted terms, house prices in the Japanese capital are 9% lower than they were in 2000, while in London they are 144% higher.

Ordinary people need to change their attitudes, too. In the West many almost instinctively oppose development, either because of the inconvenience associated with it or because they dislike the very idea of housing companies making profits. Better compensating people affected by housing construction would help win over more residents. Governments could also do more to explain why a shortage of housing is bad news for everybody, rather than celebrating whenever house prices go up. Bold action is needed. Until it is taken, housing will continue to weaken the foundations of the modern world.

How housing became the world's biggest asset class

It is only a recent phenomenon

In 1762 Benjamin Franklin set sail from England to Philadelphia after several years away. On his arrival he was shocked by what he saw. "The Expence of Living is greatly advanc'd in my Absence," he wrote to a friend. Housing, he thought, had become particularly expensive. "Rent of old Houses, and Value of Lands...are trebled in the last Six Years," he complained.

If Franklin were alive today, he would be furious. Over the past 70 years housing has undergone a remarkable transformation. Until the mid-20th century house prices across the rich world were fairly stable (see chart). From then on, however, they boomed both relative to the price of other goods and services and relative to incomes. Rents went up, too. The Joint Centre for Housing Studies of Harvard University finds that the median American rent payment rose 61% in real terms between 1960 and 2016 while the median renter's income grew by 5%. In the 18th century farmland was the world's single-biggest asset class. In the 19th century the factories used to power the Industrial Revolution took the number-one spot. Now it is housing.

In capitalism's early days house prices did see short-term booms and busts: 17th-century Amsterdam experienced a few housing bubbles, as did 19th-century America. Three main factors, however, explained long-term price stability. First, mortgage markets were poorly developed. Second, rapid improvements in transport meant that people could live farther away from their place of work, increasing the amount of economically useful land. Third, there was not much land regulation, meaning that housebuilders could build when they wanted and in the way that suited them. "For most of us history," say Edward Glaeser of Harvard University and Joseph Gyourko of the University of Pennsylvania, "local economic booms were matched by local building booms."

After the second world war, however, housing markets underwent a revolution. Governments across the rich world decided that they had to do more to care for their citizens—both as a thank-you for the sacrifices and to ward off the communist threat.

To this end, they vowed to boost home-ownership. A country of owner-occupiers, the thinking went, would be financially stable. People could draw down on equity in their house when they hit retirement or if they found themselves in difficulty. In the late 1940s and the 1950s manifestos of Western political parties became more likely to identify home ownership as a policy goal, according to research by Sebastian Kohl of the Max Planck Institute for the Study of Societies. Over time, the notion that owneroccupation was superior to renting became common, even apparently self-evident.

Policies to promote owner-occupation proliferated. In America the Veterans Administration made mortgages with no down-payment available to veterans in the mid-1940s. Canada established the Central Mortgage and Housing Corporation for returning war veterans. In 1950 the Japanese government established the Government Housing Loan Corporation to provide low-interest, fixed-rate mortgages. Changes to international financial regulations also encouraged banks to issue mortgages.

In a research paper Òscar Jordà, Alan Taylor and Moritz Schularick describe the second half of the 20th century as "the great mortgaging". In 1940-2000 mortgage credit as a share of gdp across the rich world more than doubled. More people clambered onto the "housing ladder". America's home-ownership rate rose from around 45% to 70%; Britain's went from 30% to 70%.

In previous centuries, a rise in demand for housing did not translate into structurally higher house prices. What had changed in the second half of the 20th century? One factor was transport speeds, which continued to improve but more slowly: trains and cars got only a bit better. So instead of moving farther and farther out to find accommodation, more people needed to look for somewhere to live closer to work. Land prices rose, and that fed into costlier housing.

The price of preservation

In the 1950s and 1960s governments constructed large amounts of public housing, in part to rebuild their cities after the devastation of the second world war. Yet at the same time many of them tightened land regulation, gradually constraining private builders. In the 1940s and 1950s, for instance, Britain passed legislation to prevent urban sprawl. It provided for "green belts", areas encircling cities where permission to build would be hard to obtain. Around the same time cities elsewhere, including Sydney and Christchurch, explored similar plans. From the 1960s American builders, too, began to have serious difficulty obtaining approval for building new homes.

According to calculations by *The Economist*, the rate of housing construction in the rich world is half what it was in the 1960s (see chart). It has become particularly hard to build in high-demand areas. Manhattan saw permission given to 13,000 new housing units in 1960 alone, whereas for the whole of the 1990s only 21,000 new units were approved. A recent paper from Knut Are Aastveit, Bruno Albuquerque and André Anundsen finds that American housing "supply elasticities"—ie, the extent to which construction responds to higher demand—have fallen since the pre-crisis housing boom.

Why did the rich world turn against new construction? The post-war rise in home ownership may have had something to do with it. In 2001 William Fischel of Dartmouth College proposed his "homevoter hypothesis". The thinking runs that owner-occupiers have an incentive to resist development in their local area, since doing so helps preserve the value of their property. As home ownership rises, therefore, housing construction might be expected to fall.

Research supports that idea. One paper studies a ballot in 1988 in San Diego, finding that precincts with a larger share of homeowners had more votes cast in favour of growth controls. Another finds that parts of New York City with high home-ownership rates were more likely to implement measures which made development more difficult.

There is little doubt that the rich world is a less friendly place to build than it once was. But to what extent is land regulation responsible for today's sky-high prices?

Politicians are finally doing something about housing shortages

But will it reduce housing costs?

To get a sense of why London has such expensive housing, visit Tottenham Hale. You might expect that, next to an Underground station where central London is accessible within 15 minutes, there would be plenty of houses. In fact, there is a car wash. The land on which the car wash sits is officially classified as "green belt" land, which means that building houses on it is almost impossible. Across just five big cities in England there are over 47,000 hectares (about 116,000 acres) of similar land, which is not particularly green, is close to train stations with a good service to their centres, and yet cannot be built on. That is enough space for over 2.5m new homes at average densities.

For decades the green belt was sacred. The British public imagine it, wrongly, as idyllic pasture where horses drink from streams. Politicians dared not talk about it. This is now changing. "It is time to burst the myth that the green belt is green," Siobhain McDonagh, a Labour mp, argued last year, "and start using the non-green sites for the homes that our children so desperately need." A cross-party group of mps called upon the government to loosen planning in parts of the green belt. Ministers say that they are looking seriously at the issue.

Britain is not the only place where change is afoot. In 2017 Germany reformed its urban-planning law and lifted barriers to densification. Consultants to the government in

Auckland detect a genuine interest in boosting housing supply. In Canada, the Ontario government is streamlining the planning process in order to increase housebuilding. In October California pushed through a broad zoning-reform bill. After decades of nimbyism, there is clearly a backlash, led by millennials unable to afford a house. Many politicians now realise there could be political mileage in building more houses. Some activists have even coined an acronym—yimby, "Yes In My Back Yard".

Many of those activists argue that overtight land regulation is the root cause of high house prices. To get a sense of the argument, compare Singapore with Hong Kong. Singapore has a fairly elastic planning system. The government owns most of the land. When house-price growth is too strong or the population is rising quickly, the state can release extra land faster than a barman at the Raffles hotel can mix a Singapore sling. In Hong Kong, by contrast, the supply of developable land is controlled by a small clique of oligarchs. What will buy you a cramped bedsit in Hong Kong will buy you a decent-sized pad in Singapore.

It is a similar story in America. The part of the country with the most elastic housing supply, Pine Bluff, a midsized city in Arkansas, has an average house price of $90,000. The cost of a house in one of the most restrictive parts, San Luis Obispo in California, is $725,000, even though building costs across America do not vary much. Common land-use regulations across America include zoning rules which allow only single-family houses and prevent the construction of apartments (94% of residential land in San Jose is zoned in this way, for instance). Since 1950 ordinances which establish exclusive zones, so that homes are not allowed in commercial areas, have become more popular.

Academic research supports the circumstantial evidence. Christian Hilber of the London School of Economics and Wouter Vermuelen of cpb Netherlands Bureau for Economic Policy Analysis found that if south-east England (the wealthiest and most regulated region) had been as open to new construction as the north-east (the least regulated), house prices in the south-east would have been 25% lower in 2008. Edward Glaeser of Harvard University finds similar results for parts of America.

A big refurbishment

Yet what a few years ago was an almost universally accepted view among housing economists—that housing is so costly because there is not enough construction—has come under attack, in particular from Ian Mulheirn of the Tony Blair Institute, a think-tank. Members of this vanguard argue that the obsession with supply restrictions misses a more important cause of high house prices: global financial markets. As interest rates have fallen across the rich world, people can take out bigger mortgages and keep their monthly repayments at a manageable level. Landlords are willing to pay more for a house to rent out, because yields on other assets have fallen.

Some evidence seems to back up the view that economists 'obsession with housing supply is misguided. In the 2000s both Ireland and Spain experienced soaring house prices, even as construction took off. A recent blogpost from researchers at the Bank of England found that most of the rise in British house prices since 2000 was down to cheaper borrowing.

In fact, both causes are important. The loosening in global financial conditions since 2000 has certainly pushed up house prices—as have low unemployment, high immigration and the rise of platforms such as Airbnb, which divert home ownership away from ordinary people. Prices have not risen because building has suddenly became vastly more difficult.

At the same time, however, the long-term rise in house prices is largely down to constrained supply. And if builders struggle to erect new dwellings quickly, a given increase in demand is largely channelled into price rises. Giovanni Favara of the Federal Reserve Board and Jean Imbs of the Paris School of Economics find that, though looser finance has led to higher house prices, that was true "to a lesser extent in areas with elastic housing supply, where the housing stock increases instead".

Even the most ardent demand-siders agree that building more would reduce housing costs. In policy terms, that matters. Governments have more control over the domestic planning system than they do over global financial conditions. Those who manage their land better are rewarded with more stable housing markets.

Game of zones

Broadly speaking, three types of planning systems exist across the rich world: discretion-based; autocratic; and rules-based. The first type is commonly found in Commonwealth countries. Local residents have plenty of power to stop development plans, and they frequently do. It may be no coincidence that those countries have in recent decades seen the fastest growth in house prices, says Paul Cheshire of the London School of Economics. Parts of America follow similar rules. In San Francisco every permit is appealable and, since very few large-scale projects match existing building and planning codes, delays are common.

Autocratic planning systems do a better job of boosting housing supply. Russia has raised its annual rate of housebuilding from 400,000 a year in the early 2000s to over 1m. Singaporeans who protest against development are routinely ignored, says one with a house located near Tengah forest, some of which will soon be razed to make way for apartment blocks.

The third group—rules-based planning systems—are commonly found in European countries such as France and Germany. If developers tick all the boxes then construction is permitted, even if local residents object. These systems have generally done a better job of delivering housing. Since the 1950s Germany has built twice the number of houses as Britain, despite having only a slightly higher population.

As well as planning rules, the tax system matters. Switzerland demonstrates this well. It has a decent claim to be the world's most democratic country, reliant as it is on referendums to decide all sorts of issues. (In 2018 it held ten national referendums, on everything from whether or not to penalise farmers who dehorn their livestock to whether or not insurance companies should be allowed to hire private detectives.) Local governments are unusually powerful. Yet nimbyish residents appear to hold little sway. Each year Switzerland builds twice as many houses as America on a per-person basis.

To explain this apparent paradox, a paper by Mr Hilber and Olivier Schöni of Laval University points to the Swiss tax system. In countries such as Britain, though many taxes are levied at the local level, the proceeds are redistributed across the country. Local governments therefore see little economic benefit from allowing home construction, even as they must cope with the disruption. As a result they are unlikely to try too hard to override the nimbys.

By contrast, in Switzerland local taxes stay where they are levied, so local governments have a fiscal incentive to allow development. The process for acquiring planning permission can be slow, explains Melk Nigg, an architect in Zug, a canton close to Zurich which has the joint-highest rate of housing construction in Switzerland. But it is predictable. In the past century Swiss house prices have risen by less than those in any other rich country.

Can such policies be adopted elsewhere, especially in English-speaking countries? It is largely a question of politics. Right-leaning parties in particular recognise that, since homeowners are widely perceived to be more likely to vote for conservatives, unless they can create a new generation of owner-occupiers they will eventually be voted out of office. As the rate of home ownership falls, owner-occupiers lose political power relative to renters, meaning that liberalising planning policy has a lower political cost. And as more people come to see the urgent necessity of cutting carbon-dioxide emissions, support may grow for a new generation of houses with more efficient heating and insulation.

Nonetheless yimbys must tread a fine line. On the one hand, only a long-lasting construction boom has any chance of noticeably improving housing affordability. On the other hand, building on that scale would create much controversy, because of the disruption and because neighbourhoods would change. The continued rise of the yimbys is far from assured.

A decade on from the housing crash, new risks are emerging

Shadow banks originate around half America's mortgages

During the broadcast of the 39th Super Bowl in 2005, there was an advert for mortgages from a firm called Ameriquest. "Don't judge too quickly," ran the slogan. "We won't." Ameriquest also sponsored the half-time show, where Paul McCartney opened with "Drive My Car". Two years later and the firm was no more, part of the wider crisis in the mortgage market which prompted a global recession and nearly caused the financial system to collapse.

Eleven years after that, at the 50th Super Bowl, a similar advert appeared for a different lender, Rocket Mortgage. A magician, a cyclist and even a toddler try to use the app to apply for home financing. "Push button, get mortgage," the slogan read. By the Super Bowl in 2018 Rocket said it was the country's largest mortgage lender, leading some Americans to wonder whether any lessons had been learned at all from the global crash.

Certainly the regulatory system for banks has been transformed. In the 2000s most financial regulation was "microprudential", focusing on the soundness of individual banks. Now "macroprudential" regulation is the norm. The idea is to ensure that the financial system as a whole can withstand nasty surprises. "Macropru" is useful in a world of low interest rates. When borrowing is cheap, households can bid up house prices to unsustainable levels. But since raising interest rates does not square with the needs of the broader economy, targeted measures are required.

Since the early 2000s the number of rich countries using macro-prudential policies has doubled. In Britain not more than 15% of new mortgage lending can be for houses worth more than 4.5 times the borrower's income. Singapore and parts of Canada now restrict purchases by foreigners.

All this can put the brakes on rapid credit growth. For high-risk borrowers, getting a mortgage is harder than it was, which is one reason why home ownership among the young has fallen. Banks have scaled back their mortgage operations. "The mortgage business... has experienced increasingly lower returns as new regulations add both sizeable costs and higher capital requirements," wrote Jamie Dimon, the boss of jpMorgan Chase, in 2016.

But new risks are emerging. In recent years non-bank mortgage lenders (a group of non-deposit-taking lenders that includes Quicken Loans, which offers Rocket Mortgage) have proliferated. They now originate around half of America's mortgages (see chart). A growing number of economists argue that regulators need to keep a closer eye on these firms.

Many non-bank mortgage lenders are seizing market share because they offer genuinely useful products. Safe Rate, based in Chicago, offers a new type of mortgage. When local house prices decline, so do borrowers 'monthly mortgage repayments. The benefit for the borrowers is that they save money and are less likely to default. The advantage for investors is that, by preventing foreclosures, more mortgages will be kept going and it is less likely that house prices across a region will spiral downwards.

Some non-banks, however, exist purely as a means to get around strict bank regulations. In America non-banks are more loosely regulated and supervised than traditional banks. One paper found that an increasing regulatory burden accounted for some 60% of non-bank growth in 2007-15. (In countries like Britain the difference in regulatory burdens between banks and non-banks appears smaller and the growth in their lending is lower.)

Mortgage credit in America is not rising as fast as it was in the early 2000s. According to official data, only a small share of Quicken's loan-book is in trouble. Yet many non-banks remain highly reliant on short-term funding from traditional banks, so if wholesale markets froze again, many Americans would quickly lose access to mortgage finance. Rather than keeping mortgages on their balance-sheets, non-banks tend to sell them on—not the best incentive to be ultra-cautious, says Amit Seru of the Stanford Graduate School of Business. Non-banks also seem particularly likely to serve less creditworthy borrowers. Until regulators start properly grappling with non-bank lenders, the job of regulating America's mortgage market will be only half-done.

Owner-occupation is not always a better deal than renting

Each year American owner-occupiers pay around $200bn in maintenance costs on their homes

The question hardly seems worth asking. Is it a better deal to rent a house or to buy one? Buying a house is a wise investment for the future, the argument goes, whereas renting one amounts to little more than throwing money down the drain. A closer look at the economics, however, shows that this view may be mistaken.

For one thing, renters often devote a smaller share of their income to rent than owner-occupiers devote to repayments of mortgage interest (in both cases, this is money handed over to someone else and never seen again). Whether one is cheaper than the other depends in part on interest rates. In the early 1990s, when interest rates were higher than they are today, the average ratio of mortgage-interest repayments to income was higher than the rent-to-income ratio in many countries.

That calculation nonetheless underestimates the cost of owner-occupation. Whether a home-owner is paying off a mortgage or not, they face a number of costs that renters do not, points out Ian Mulheirn of the Tony Blair Institute, a think-tank. For instance, a residential-property transaction in an oecd country incurs a median bill of about 8% of the value of the house (transaction costs for renting tend to be trivial).

Owner-occupiers must also account for wear and tear. Each year in America they pay around $200bn in maintenance and improvement costs (about 1% of the value of the houses in their possession). Home ownership also carries opportunity costs. In recent decades housing has proven to be a good investment; that may well continue. But capital locked up in a house could have made an even higher return if invested elsewhere.

What happens when you factor all this in? Take the example of the British housing market. In the run-up to the financial crisis of 2008-10, rapid increases in house prices and rising interest rates meant the user cost of owning actually rose well above rents. But over the long run the two tenures have cost about as much as each other. This is as economic theory would predict. Renting a home, and buying the right not to have to rent a home, are economically equivalent actions.

Home ownership is in decline

That is not a big cause for concern

More than nine in ten Singaporeans are homeowners, a higher rate than in any other rich country. And what a nice place it is to live. The city-state is rich, stable and has virtually no crime. The streets are clean.

Singapore seems to confirm what conservatives have long believed: that home ownership makes for richer, happier folk. Lee Kuan Yew, its first prime minister, was a big fan, arguing that it gave ordinary people “a stake in the country and its future”. Margaret Thatcher’s “right-to-buy” programme in the 1980s, allowing Britons in social housing to buy their property at knock-down prices, is said to have been influenced by the Singapore model.

It might be seen as worrying, then, that for the first time in a century home ownership in the rich world is in decline. Yet having more renters might not be such a bad thing.

For most of the past millennium, the only people with a good claim to be homeowners were landed gentry and farmers who worked the fields. Then, from the mid-20th century onwards, home ownership was democratised. A combination of rising household incomes and government policies helped more people get onto the property ladder. In most countries home ownership peaked around the year 2000.

America has some of the most generous fiscal incentives to become a home-owner. Official estimates suggest that the government forgoes over $200bn a year (over 1% of gdp) subsidising homeowners through the tax code, with policies including a tax deduction on mortgage interest and not taxing the income homeowners implicitly earn by avoiding paying rent. Mark Zandi of Moody’s Analytics adds that subsidies to mortgages provided by Fannie Mae and Freddie Mac—two government-sponsored enterprises that support much of the country's mortgage finance—and the Department of Housing and Urban Development amount to a further $9bn or so a year.

America is especially generous, but schemes to boost home ownership are common. Most rich countries do not charge capital-gains tax on the sale of an owner-occupied house. Inheritance-tax regimes routinely make exemptions for housing. Many countries subsidise mortgages and down-payments. Yet for all this, the factors pushing home ownership down are now stronger.

One possibility is that younger folk may be less interested in home ownership. After all, many millennials desire "asset-light" lives in which they rent cars, music and clothes, rather than owning them. Why not housing too?

The private sector has spotted an opportunity. Silicon Valley types are bullish on "co-living", where people rent a dwelling and share common spaces such as kitchens, washing facilities and gyms. Hmlet, a co-living firm, is expanding in home-ownership-obsessed Singapore. Sharing a kitchen might sometimes be annoying, but Hmlet's properties are well kitted out.

The attraction of co-living is, however, exaggerated. The majority of people would still prefer to be homeowners. Surveys from America suggest that the share of people who think that home ownership represents a good investment is growing.

Economic factors may be a bigger cause of the decline in home ownership. With weak earnings growth since the crisis, young folk have struggled to accumulate savings for a down-payment. Tighter regulation of mortgage markets since the financial crisis has made it tougher for first-time buyers to acquire finance. Baby-boomers, looking for a return on their savings, are pushing aside prospective first-time buyers and becoming landlords. As millennials have taken on more student debt, buying a home has become trickier.

How low could the home-ownership rate go? It seems unlikely that rates in the English-speaking world will ever approach Germany's (with a rate of just 44%) or Switzerland (40%). Home-ownership rates are the product of history and culture. Countries with a history of weak real house-price growth—Germany and Switzerland fit the bill—have lower owner-occupation, because fewer people see buying a house as a worthwhile investment. Densely built places also tend to have lower home ownership. People are generally less keen on owning a flat in a high-rise block than they are in a detached house (55% of Germans live in apartments, a high rate by international standards).

Politicians across the rich world bemoan the emergence of Generation Rent. "American home ownership rate in q2 2016 was 62.9%—lowest rate in 51 yrs," tweeted Donald Trump when he was campaigning for president. "we will bring back the 'American Dream! " 'Boris Johnson, Britain's prime minister, seems equally concerned about his country's falling rate of owner-occupation.

But lower home ownership need not be a cause for concern. For one thing, owning a home is not necessarily the route to riches that many people believe it to be (see article). The evidence that home ownership is good for society is, in fact, fairly weak. There are many counter-examples to Singapore. Romania probably has the world's highest home-ownership rate, at 96%, but it has its fair share of social problems. Switzerland, at the other end of the scale, nonetheless has low crime and high social trust.

Academic studies offer only weak support for the idea of promoting home ownership. One paper suggests that owner-occupiers have better-tended gardens. But if nice shrubbery were a goal of public policy, it might be a better use of public money to subsidise wheelbarrows and trowels. Another study in America found that homeowners 'children were far more likely to graduate from high school—even after controlling for parents 'earnings. Researchers have struggled to discern which way the causality runs, however: does home ownership make good parents, or do good parents become homeowners?

Other evidence, meanwhile, finds that home ownership carries costs. The stresses of paying back a big mortgage are real. And the mad dash in the 1990s and 2000s to create "property-owning democracies" ended with the global financial system on its knees.

Home ownership does subtler sorts of economic damage, too. Indebted homebuyers are 30% less likely to become entrepreneurs, according to one study. Responsibility for a large mortgage debt may make people loth to take on further risk. When the home-ownership rate in an American state has risen, a sharp rise in unemployment has followed, according to David Blanchflower of Dartmouth College and Andrew Oswald of Warwick University. Homeowners are less willing to move to find work.

As the rented sector has grown in size, and as Generation Rent becomes a more powerful constituency, governments are putting more effort into improving the sector. One increasingly popular measure is rent control. London's mayor, Sadiq Khan, has advocated restricting rent rises in the capital. Berlin's legislators recently voted to freeze rents for five years. Paris reintroduced rent controls last year, having scrapped them in 2017. Such interventions are misplaced. Rent control generally dissuades investment in new construction, the last thing many of these cities needs.

More promising than rent control, however, is a move towards improving tenancies. Many politicians in English-speaking countries have Germany in mind. There, renting is not seen as a second-class tenure. It is fairly secure: the average tenancy lasts for 11-12 years, compared with 2-3 years in Britain. Some 3m Germans are members of tenants ' organisations, which can bargain on their behalf with landlords (the mascot at one association in Munich is dressed like Superman and calls himself the "Rentstopper").

Emulating the German experience will be tricky. In Germany landlords treat tenants well not just to be nice, but because they have an incentive to do so. In recent decades Germany has seen little house-price appreciation. Since making money through capital gains is difficult, German landlords 'best hope of getting a decent return is through keeping their tenants in place for as long as possible. Only if house prices in other countries were more stable would their landlords start to behave in this way, too.

Still, governments can make some reforms. Britain has abolished letting fees, a murky system of charges slapped on by estate agents using a methodology that renters and landlords rarely understood. Spain is moving to give renters longer tenancies as standard. New Zealand is passing rules to ensure that certain basic standards for rental accommodation are met.

Perhaps the most promising development, however, is growing private investment in the rental sector. Since 2010 global institutional investment in residential property has more than doubled in real terms, not only because investors are looking for yield in a low-rate world but also because the number of potential customers is rising. Across America the share of the rental sector owned and operated by companies is rising, according to research by Hyojung Lee of Virginia Tech. By one estimate, the annual number of homes in New York City bought by professional investors has doubled in a decade.

An expansion of corporate housing will raise average standards in the rental sector. Big firms may be more professional than mom-and-pop landlords, and may also benefit from economies of scale which allow them to provide better-quality accommodation at lower prices. “Build-to-rent” apartment blocks often include goodies such as gyms and free Uber rides with the rent.

That said, corporate landlords have a more transactional relationship with their tenants. A study of Atlanta, Georgia, published by the Federal Reserve Bank of Atlanta in 2016, found that large corporate owners of single-family rentals were 8% more likely than small landlords to file eviction notices. To help the poorest or most vulnerable members of society with their housing needs, governments may need to do more.

Governments are rethinking the provision of public housing

Is it better to give people money or build them houses?

In the past ten years the homeless population in Los Angeles has risen by 50%. In New York it is 60% up over the same period. San Francisco is widely thought to have America's worst homelessness problem. Just metres from the headquarters of Twitter and Uber, people lie in the street, stupefied, or defecate in front of the passing traffic. The term "housing crisis" is bandied about too readily. But it is an apt way of describing what is happening in America's most prosperous cities.

It does not have to be this way. Tokyo is as much a global city as San Francisco, yet you can go days without seeing a single person living on the streets. The inhabitants of Zug, a short drive from Zurich, are as rich as the local *Kirschtorte*. Astonishing wealth, a waterside location and lots of high-tech firms mean that Zug bears more than a passing resemblance to San Francisco. But in Zug there is practically no rough sleeping.

Homelessness is the extreme manifestation of a problem that governments have tried to tackle for decades. At any one time, at least some people struggle to afford decent housing on private markets. Governments have spent vast sums trying to help the poor into housing and improving conditions. Yet they are failing in their objectives. This is prompting a rethink.

Governments began intervening heavily in housing markets following the second world war. They promised to build millions of homes themselves, which they would then rent to their constituents at below-market rates. In America the Housing Act of 1949 authorised the construction of over 130,000 units of public housing a year for six years. In 1950-70 Britain built some 3m units of social housing, and over the same period West Germany put up even more. The Japanese government was equally enthusiastic.

The boom ended as governments triumphantly declared that the housing shortage had been solved. At the same time fewer people wanted to live in big blocks of homogeneous flats, especially poor-quality ones: the dash for volume had often caused governments to cut corners. A gas explosion at the Ronan Point block in London in 1968 marked a turning-point in attitudes to public housing in Britain. In the mid-1970s Pruitt-Igoe, an infamous project in St Louis, Missouri, was demolished. Around this time, economists started to think differently about the best way to provide welfare.

Rather than build houses for the poor, many argued, why not give them the money they would need to buy housing on the open market? Recipients of cash payments could then choose the sort of accommodation that suited them best. Others contended that the private sector would deliver superior housing to what the state could provide. Cash benefits also promised to be better targeted at the poor: withdrawing a monthly housing payment to someone who suddenly becomes well off is easier than kicking them out of their home.

Who is it helping?

What followed was a shift from supply-side to demand-side measures. In the early 1970s Britain started to wind down its programme of social-housing construction, but in its place gave money to poor tenants. France did something similar in the latter part of the decade. In Germany from the late 1980s, housing assets owned by municipalities were transferred to for-profit owners. In America between 1977 and 1997, the number of households receiving housing vouchers increased from 162,000 to over 1.4m.

Though economists generally prefer cash benefits over the in-kind sort, a growing number are starting to argue that providing cash assistance for housing has not proven to be as effective as expected. Giving people money increases their purchasing power. In a normal market, the increase in effective demand leads suppliers to respond accordingly. Yet the supply of housing in many cities is inelastic: when demand for housing rises, extra supply does not necessarily follow. Instead, the price of housing—which, for most poor people, is rent—goes up.

In many cases, therefore, housing benefits help landlords as much as the poor. Some research in England has found that half of the gains from housing benefits accrue to landlords. A paper from 2006 looking at France concludes that a one-euro rise in housing benefits raises rents by 80 cents.

If governments respond to rising rents by increasing housing benefits, costs can quickly spiral. Over the long run, cash payments for housing can even cost the government more than providing housing directly (though this is difficult to calculate reliably). Meanwhile, it is not clear whether the private sector is able to fill the gap when the state stops building houses itself. If not, then overall new housing supply falls, making it more expensive for everyone.

Faced with growing numbers of people unable to afford housing, there are stirrings of a global movement back towards direct provision. Last year Kanye West, a rapper, reportedly built prototypes of dome-shaped houses inspired by Tatooine, a planet in “Star Wars”, which were to be used as low-income dwellings (though after a fight with local residents, the prototypes appear to have been demolished).

Housing co-operatives are also becoming more popular. A short drive from Zug a group called “mehr als wohnen” opened “Hunziker Areal”, a housing complex, in 2014. Rents in its apartment blocks are generally far lower than the local average. Residents have a say in how the community is run. There are bikes in a “mobility station” for people to borrow and residents can tend a vegetable patch. It is a world away from what many Americans or Britons think when they hear the term “public housing”.

Governments have bigger plans. In 2018 Britain built more public housing than in any year since 1992. The South Korean government aims to increase the share of public-rental housing from 7% of the total stock to 9% by 2022. In Germany in 2018-19 the government set aside some €5bn ($5.6bn) to promote the construction of public housing.

The best way to make housing more affordable would be to make the supply more responsive to increases in demand. A big underlying reason why homelessness in Tokyo is so low is that housing is reasonably affordable. Meanwhile, Zug builds more than twice as many homes per person as San Francisco. Research suggests that a 10% fall in rents in a high-cost city such as New York results in an 8% decline in the number of homeless residents. Until governments keep overall housing costs under control, the rest is tinkering.