



## Israel IVS Forum

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# International Views and Approaches

# Addressing housing challenges, brick by brick

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## HOUSING: A WEB OF INTERCONNECTED CHALLENGES

House prices have soared in many parts of the world since the turn of the millennium, and they have continued to rise since the onset of the pandemic. As a result, households now spend more out of their budget on housing, including by paying rent or mortgage installments, than they do on transport, health care and education on average among OECD countries. The middle class alone already spends on average close to a third of their budget on housing.

Rising prices and costs are making housing unaffordable for many. This is especially so among the most vulnerable social groups, who face the added predicament of often living in overcrowded spaces and far from where they work. They also often live in lower-quality buildings where amenities are scarce, conditions are precarious, and insulation is poor. They therefore typically end up spending relatively more out of their income on heating and cooling than their more affluent counterparts do. Energy poverty is also not uncommon among those most vulnerable in the sense of not being able to afford their energy bill. Moreover, homelessness is on the rise in many OECD countries, even though it is driven by much more than affordability.

Part of the problem is that the stock of dwellings has not grown fast enough to meet the rise in demand. The situation is all the more severe in the most sought-after cities around the world, where the quality of life is better and jobs are more attractive. This mismatch between supply and demand ultimately leads to higher prices.

Demand also changes over time, as has become evident since the start of the Covid-19 pandemic. The migration of people with “teleworkable” jobs away from city centres towards suburban or peri-urban areas - the so-called “race for space” - and the corresponding hollowing out of central business districts are cases in point. To some extent, these demand dislocations are temporary and will be reversed as economies open up and recover, but more durable changes in habits and behaviour should not be underestimated. If they are indeed here to stay, these pandemic-related shifts in demand patterns will require a rethink of urban development strategies, mass urban transport systems and the supply of services and amenities that will be needed within metropolitan areas. They will have profound consequences for the real estate sector as a whole, not only the residential segment, because of the concomitant shifts in demand for commercial property and office space.

Beyond issues related to the evolution of supply and demand, it is important to consider the environmental footprint of housing, which is large. Almost one-fifth of emissions of greenhouse gases worldwide comes from the housing sector. The ratio rises to almost 40 percent if we look at emissions of fine particulates, which are especially detrimental to people’s health. These numbers make a clear case for treating housing as an integral part of solutions to decarbonise our economy as a means of achieving agreed climate change targets. A promising start is the energy performance of buildings, which varies a great deal depending on the age and quality of construction.

In other words, housing challenges are manifold: they are about efficiency as much as affordability and sustainability. Well-functioning housing markets, where supply responds to evolving demand, finance is adequate and investment is carried out in line with high environmental standards, are essential for tackling these interconnected challenges.

It was with this objective in mind that the OECD launched in June a Housing Policy Toolkit to help analysts and policymakers make better housing policies. The Toolkit contains a report entitled Brick by Brick: Building Better Housing Policies that summarises the main findings of two years of analysis and evidence on several aspects of housing, including the design of a range of policies, and a host of country experiences. The Toolkit also features a Dashboard of indicators covering housing outcomes and policy settings, and it is accompanied by Snapshots of the housing sector in different countries.

## **STRENGTHENING THE FOUNDATIONS: WHAT CAN POLICY DO?**

First and foremost, policy can unlock supply. Investment in new developments is often constrained by a lack of finance for both developers and potential homeowners. Finance is

also important for renovations, retrofitting and improvements in buildings. In many countries, the housing stock is old and needs upgrading. Development of new funding options can help, such as energy efficient mortgages that combine housing loans with incentives for homeowners to improve the energy efficiency of their dwelling and for buyers to acquire energy efficient properties.

Removing regulatory impediments to the expansion of supply is also part of the policy toolkit, especially where regulations are overly restrictive. Rules and norms related to zoning, such as limits on building height and density, tend to restrict housing investment, causing prices to rise. They also encourage urban sprawl, which implies longer travel distances and greater reliance on cars, a phenomenon that is not without consequences for the environment. Moreover, regulations on the use of land are widespread around the world and often restrict the areas that can be developed for housing purposes. Because the local governments set most of these regulations, it is important to enhance cooperation among the different spheres of government that are responsible for housing policies.

Governments can tackle the affordability challenge by investing more in social housing. They may build homes for such use, and they can support the targeted population by subsidising housing costs. Investment in social housing can also be carried out as part of broader efforts to rehabilitate degraded urban areas, which contributes to tackling segregation and to revitalising the urban fabric. This is important because investment in social housing has been trending down in OECD countries over the years. However, investment in social housing needs to be designed judiciously; for example, entitlements should be portable, so that beneficiaries are not trapped in the place where they are entitled to a subsidised home and can move should better job opportunities arise elsewhere.

Mobility is particularly important in the post-pandemic world. The geography of jobs may change depending on how the different sectors of the economy recover from the crisis. In this context, labour mobility should not be constrained by impediments to residential mobility. This is the case not only of poorly designed social housing programmes, and it may arise where rental markets are underdeveloped and transactions are costly as a result of high fees and taxes on the purchase and sales of homes. A good direction for policy reform is therefore to move away from a reliance on transactions towards recurrent taxes on immovable property. Doing away with deductibility of interest paid on mortgages from the income tax is another policy move that can reduce pressure on demand and therefore prices, in addition to making homeownership less attractive relative to other tenure options, such as rental.

Reducing the environmental impact of housing requires decisive policy action. Part of the solution is to improve construction technology, and much is already happening in this area. Take for example the increased use of lumber in construction, which increases the potential of dwellings to act as carbon sinks. There is also much room to invest in energy efficiency. Setting standards is the way to start. Appropriate certification of energy efficiency performance is also important in this area so that home improvements can be reflected in the price of houses, the cost of finance and the private returns to investment.

An important distinction needs to be made here. While energy efficiency regulations may increase construction costs, they also add value to the homes that are built to higher standards. However, this increase in house prices is very different qualitatively from that which is caused by the regulations mentioned above that constrain housing supply. This is all the more important because buildings have a long lifespan, and today's choices will shape to a large extent environmental impacts for quite some time.

There may be trade-offs to deal with, but also complementarities to exploit, when designing housing policies. This is because the challenges in this area are complex and the policy objectives are multiple. For example, investment in social and affordable housing has multiple benefits: protecting low-income or vulnerable households, expanding the housing supply, which can help to contain the increase in house prices and rents, and preserving the environment, to the extent that investment is based on high energy efficiency standards. This policy option is no panacea, but it illustrates the potential for synergies across policy domains.

As for trade-offs, a case in point is the easing of restrictions on landlord-tenant relations, such as rent control. In many cities, caps are imposed on the level of rents or by how fast they can rise. This is done as a way of making housing affordable, even though there are many unintended and undesirable consequences associated with these regulations, including a disincentive for owners to invest in the rental market and on housing renovations. Easing those restrictions can therefore encourage investment, which helps to increase supply and lower prices, but it comes at the cost of penalising vulnerable incumbent tenants in the short term. The good news is that this adverse effect can be offset at least in part through well thought-out social housing programmes. The upshot here is that when faced with such trade-offs comprehensive policy packages, rather than piecemeal initiatives, can go a long way to address housing challenges.

These are just a few examples of policies that can be deployed to address the many challenges societies are facing today in the housing space. However, there are other areas that need attention, and will continue to do so, as the housing sector evolves and new challenges emerge. The role of housing in the economic recovery from the pandemic is a

case in point. Another one is the changing landscape of housing finance with the entry of new participants and financial institutions in housing markets. This may affect access to new borrowers and also the cost of loans and mortgages through competition and financial innovation. Digitalisation is another critical area. It is already reshaping construction technologies at the same time as it is changing working habits by making teleworking widespread in many occupations and sectors of the economy. The emergence of on-line short-term rental platforms is influencing demand and the use of the residential capital stock in addition to blurring the boundaries of the housing and hospitality sector.

Addressing the current housing challenges and preparing for the emerging ones will require sound evidence, innovative solutions and continued dialogue among all the relevant stakeholders, within government and beyond. After all, a house is more than bricks and mortar; it is also a home, an investment opportunity, and a place of work and social interactions.

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