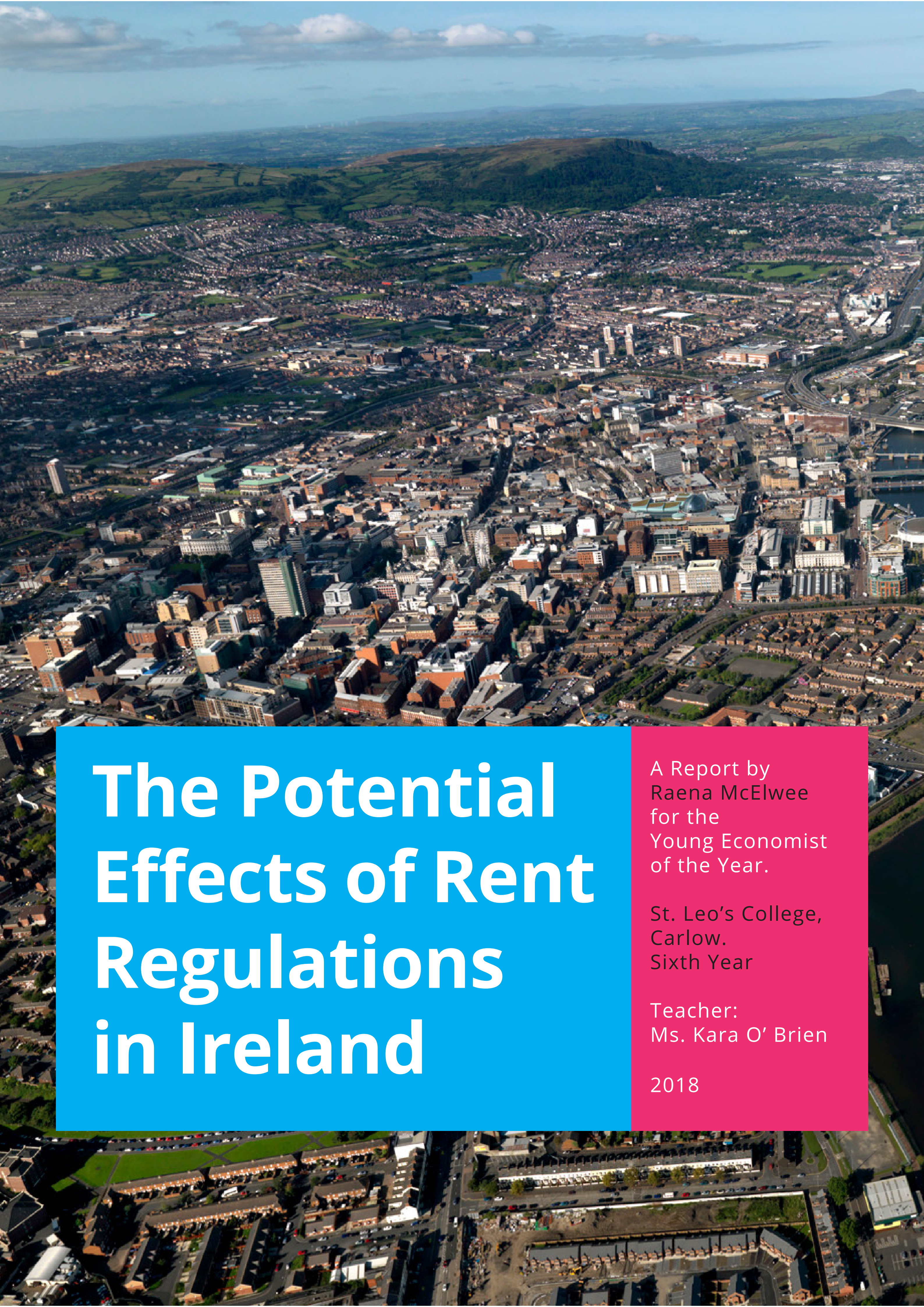

The Potential Effects of Rent Regulations in Ireland

A Report by
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for the
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of the Year.

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Sixth Year

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Cover Photo - Aerial View of Dublin City

Introduction

In this report, I hope to examine how rental regulations in Ireland, introduced in January 2017, will affect the rental and housing market.

By examining the theory of the effects of price controls and looking at an example in Salthill, Galway, I hope to come to a conclusion about the effects of the rent regulations in this country, and whether they really benefit us. Many economists argue that price controls do little to help a situation - they create artificially higher demand and hamper the incentive to supply in the private market.

I will also look at how rent regulations have affected other cities and countries in the past, including Britain, Paris and Massachusetts, and hope to draw a conclusion from their experiences as to how our rent regulations will affect us in the long run.

The issue of spiralling rent prices and close-to-2008 levels of house prices in cities is pressing and urgent. Steps must be taken to ensure that this housing crisis does not continue into the future, and that a viable housing and rental market is sustained in the long run. If prices to continue to rise at their current rate, everyone will be affected - students will not be able to attend city universities, people will be forced to commute for hours to go to work in cities, and families will be displaced from their homes, unable to pay rent and unable to find anywhere suitable in the area. Hopefully, a long-term solution will be found soon, and rents and housing prices will return to normal levels with adequate supply.

Cranes seen along the Dublin Skyline

Housing Crisis

In the first quarter of 2007, rents in Ireland grew on average by 12.4%.[1] In the first quarter of 2017, however, rents in Ireland grew on average 13.4%.[2] Rent prices in Dublin in the last quarter of 2017 were 19% higher than their previous peak in early 2008.

The generally accepted driving factor of rising rents is a shortage of supply, which seems unlikely to rise to levels of demand any time soon. Housing completions were set to reach between 18,000-18,500 units by the end of 2017, but this was far below the estimated demand of 30,000 units.[3]

The average cost of renting is €1,227 nationwide. However, rents tend to have stayed lower for those who have occupied the same unit since 2012 than those who have moved to new units.[4] This has made it harder for younger people seeking their first home to find affordable units.

In 2016, 460,000 adults were living at home with their parents, 47% of which were working.[5]

Focus Ireland counted the number of homeless in December 2017 to be at 8,587 individuals, with an increase of 20% between December 2016 and December 2017 in the number of homless accounted for. Of 8,587, 3,079 were children.

Houses under development in Ireland

Rent Regulations

Rent regulations in Ireland were introduced on January 26th 2017 by the then Minister for Housing Simon Coveney.[6]

The regulations have been applied to Rent Pressure Zones (RPZs) across the country in an attempt to control rising rent prices. RPZs are areas where the annual rate of inflation has been 7% or higher in four of the last six quarters.[7]

Rent regulations now affect Galway City, areas in Dublin, and various towns which serve as commuter towns to Dublin, Galway and Cork.

The regulations prevent the rent of residential properties in these areas from increasing by more than 4% per annum.

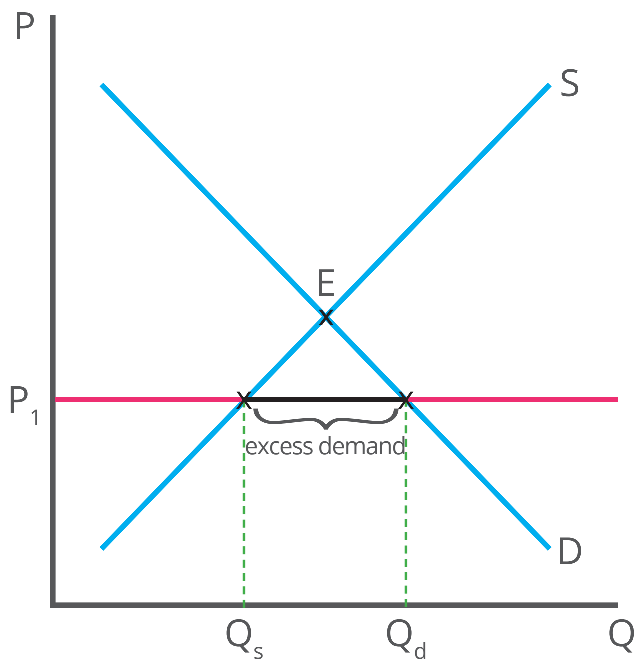
Rent regulations will affect the following towns:

- Cobh
- Maynooth
- Ballincollig
- Galway City Central
- Galway City East
- Galway City West
- Celbridge
- Naas, Co. Kildare
- Kildare
- Ashbourne
- Laytown
- Rathoath
- Bray
- Wicklow
- Dublin City Council
- South Dublin County Council
- Dun Laoghaire/ Rathdown County Council
- Fingal County Council
- Cork City Council
- Greystones, Wicklow County Council
- Drogheda, Louth County Council

Galway City, Galway

The Theory of the Effects of Price Controls

All of the laws of economics are based on the simple laws of supply and demand. The law of demand states that as price increases, demand decreases, and as price decreases, demand increases, all else being equal. The law of supply states that as price increases, supply increases (from the point of view of the supplier), and as price decreases, supply decreases, all else being equal.



Quantity supplied and quantity demanded naturally meet at equilibrium point E in a free market at the market price.

With a price ceiling at price P_1, for example rent controls (where prices cannot increase past a certain price), prices are likely lower than they would be in a free market. They are usually put in place by an external body in an attempt to stop rising prices.

As shown in the diagram, demand will exceed supply as price cannot rise to the equilibrium point, point E, (as is would in a free market), and there is a shortage of the good (excess demand).

There is little incentive for a supplier to supply a good when they cannot sell their good for a higher price, causing a fall in supply. Likewise, demand increases as prices are artificially lower. Excess demand exists between points Q_s and Q_d.

Rent Regulations

So what happens theoretically?

As shown in the previous graph, when price ceilings are implemented, excess demand occurs.

There are two types of regulations,
1. Rent controls, which put a cap on how much rent can be charged, and
2. Rent stabilisation, which caps annual rent increases.

Ireland has adopted rent stabilisation at 4%.

When rent regulations are introduced, similar patterns tend to be seen. Initially, prices either stabilise or fall when controls are implemented. People stop worrying about renting units and new renters find units to rent at an affordable price.

Soon, however, supply begins to fall. All of the previously available units are occupied, as prices are lower and demand is high as a result. However, new units do not appear on the rental market at the rate they may have been before rent controls. This is due to two reasons:

1. New rental stock begins to fall. Developers find it less attractive to build new units as the return for their units in rent is diminished, and the cost of building does not decrease in any way (especially land prices). This results in a fall in new developments and a fall in overall market supply.

   The rate of deterioration of rented units tends to speed up under rent regulations as well. Demand is high, so landlords understand that people will be willing to take lower and lower quality units for the same price. Repairs tend to be done at a slower rate as landlords are less likely to risk losing tenants. This was seen in Cambridge in the United States, as is referenced later in the Case Studies section of this report.

2. Rent regulations can discourage those who have larger-than-necessary units from moving to smaller, cheaper units as time passes. The artificially lower costs of renting a unit in a regulated area could, in time, become cheaper than a unit of a similar size in an area with less demand that is not under rent regulations.

   For example, a co-habiting couple with children renting a three-bedroom house may relocate to a smaller, cheaper unit after their children leave home to save money. However, under rent regulations, there is no reason for the couple to move once their children leave home, as rent is cheap. The time and effort required to find and move to a smaller unit is not worthwhile for the money saved.

   As is clear, people tend to hold onto larger units than necessary under rent regulations and, as a result, total market supply falls. Young couples, for example, struggle to find large units necessary to start a family and are forced to rent smaller, inadequate units while spare rooms and empty units lie unused in regulated areas.

Let’s look at an example...

Let’s take the example of the aforementioned couple who are renting a three-bedroom house in inner city Galway.

Galway City, since January 26th 2017, is an RPZ (a rent pressure zone).

The following property, put on the Irish rental market on 30th July 2017 via Daft.ie, will be used as an example.[8]

Property A

- Salthill, Galway City
- 3 Bedroom House
- Rent - €1800 per Month
- 10 minutes from City Centre

The following table shows how the rent would naturally grow outside of rent regulations in a free market (average rent increases in Galway since 2015 have been 10.1% annually[9]), and also how it would increase under rent stabilisations of 4%.

As you can see, by 2027, the rent would be significantly higher without rent regulations than with rent regulaions. While the figures are not perfect, as it is likely that rent would not continue to increase at ten percent annually for 10 years, it can give an indicator as to the rents this family would be paying in a free market.

The couple would be paying €24,052 more for deregulated rent than regulated rent.

Let’s say that by 2027 the couple’s children will have left home and there are two vacant bedrooms in the house. Under normal circumstances, tenants would leave this property to find a smaller unit elsewhere.

The couple also wouldn’t need a unit so close to the inner city than previously required when having children that attended the nearby school.

The couple could move to a location outside the city, where rent would be cheaper in a free market. However, since the rent stabilisation only applies to locations within Galway City, units outside the RPZ could have similar or higher rents to those within the RPZ. If this was the case, there would be little reason for the couple to move further out from the city, where amenities are better.

Without the 4% cap on annual rent increase, it would make more sense for the couple to move out as they can save money on rent and increase their real income.

Rooms may then lie unsued in the RPZ while supply diminishes as tenant turnover decreases. First-time tenants may have to look for locations further and further out of the city, and for higher prices outside of the RPZs, decreasing standards of living.

	At an increase of 4% annually		At an increase of 10% annually	
	per month	per year	per month	per year
	€	€	€	€
2017	1,800	21,600	1,800	21,600
2018	1,872	22,464	1,980	23,760
2019	1,947	23,363	2,178	26,136
2020	2,025	24,297	2,396	28,750
2021	2,106	25,269	2,635	31,625
2022	2,189	26,280	2,899	34,787
2023	2,278	27,331	3,189	38,266
2024	2,369	28,424	3,508	42,092
2025	2,463	29,561	3,858	46,302
2026	2,562	30,744	4,244	50,932
2027	2,664	31,973	4,669	56,025

Case Studies

How have rent regulations affected other countries?

Rent regulations have taken many forms in various countries and cities throughout history. The first forms of rent regulations were enforced around the time of the two world wars in Europe and America, in an attempt to stop rising rents caused by a shortage in supply.

Britain

In 1915, Britain introduced rent control after the start of the first world war to avoid spiralling rents after a sudden shortage of housing. Rents would be restricted to their prices in August 1914. In 1957, amendments were made to the rent regulations, whereby rents would be decided upon by an external body, and not by the landlord. In 1988, the complete deregulation of rents was intrduced in the Housing Act 1988.[10]

Glasgow Rent Strike, 1915

The Commons Library Briefing Report for the UK parliament in 2017, amidst growing debate about the reintroduction of rent control, stated the following:

> *"The application of rent controls coincided with a decline in the private rented sector. The sector had made up nine-tenths of the housing stock in 1915 but had reduced to one-tenth by 1991. Rent control has been widely identified as a factor in this decline; it is argued that there is a direct correlation between reduced rental returns and reduced investment in the sector. However, several other causes behind the sector's decline over the period have been identified, including:*
>
> - *the availability of alternative forms of investment other than rental property; and*
> - *factors making it easier for people to own their own property such as rising real-terms incomes, and the increased availability of mortgages.*
>
> *The private rented sector began to grow again after 1989 and is now the second largest tenure in the UK after owner-occupation."*

Case Studies

Paris

Paris introduced rent controls in 2015 in its densely-populated inner-city region to try and curb rising rents. A price for a residential rental unit would be decided by an official observatory, and landlords were allowed to charge up to 20% higher than this price.
As soon as the regulations were introduced, rent prices outside of this inner-city region (known as the Petite Couronne) began to increase at a faster rate. As a result, authorities intended to expand the rent regulations to other areas of the city.[11]

The likely cause of this spike in rents in the Petite Couronne would have been a shortage of supply caused by the new regulations in the inner city, increasing demand for housing just outside of this region.

Similarly, rent prices in areas outside of RPZs where rent regualtions are implemented will increase as supply falls in these areas. Rent regulations may also push up housing prices within RPZs.

In November 2017, it was decided that the rent regulations will be abolished in August 2018, due to a disagreement about the unfairness of the geographical placement of the regulations.[12]

Cambridge

Cambridge, Massachusetts, deregulated rents in 1995 after a state-wide ballot voted to remove a 25-year old policy that intended to provide affordable housing to lower-income tenants. Massachusetts completely deregulated rents in 1998, after some elements of the policy that had remained to protect the elderly, disabled and poorer citizens were removed.[13]

Cambridge's regulations capped rent increases on units built before 1969, and the removal of units from the rental market was restricted.

Around a third of the city's properties were rent-controlled before deregulations. The average price gap between regulated and non-regulated properties was approximately 40%.[14]

After deregulation, decontrolled rents overall jumped by over 50% between 1994 and 1997. A study conducted by David P Sims found that *"chronic maintenance problems — such as holes in walls or floors, chipped or peeling paint, and loose railings — were more prevalent in controlled than in noncontrolled units during the rent control era and that this differential fell substantially with rent control's elimination."* [15]

Tenant turnover was also seen to increase after the removal of rent controls. Approximately 40% of tenants living in controlled units moved out after 1995.

Conclusion

I believe that it is clear from this report that rent regulations will not solve the problem of the rental crisis in Ireland. These regulations will ony serve to dampen supply in the rental market, arising from a disincentive to supply, which is the stem of the problem. The placement of regulations in the rental market will also exacerbate housing prices - as supply falls for rental accommodation, demand can only increase in the ownership market.

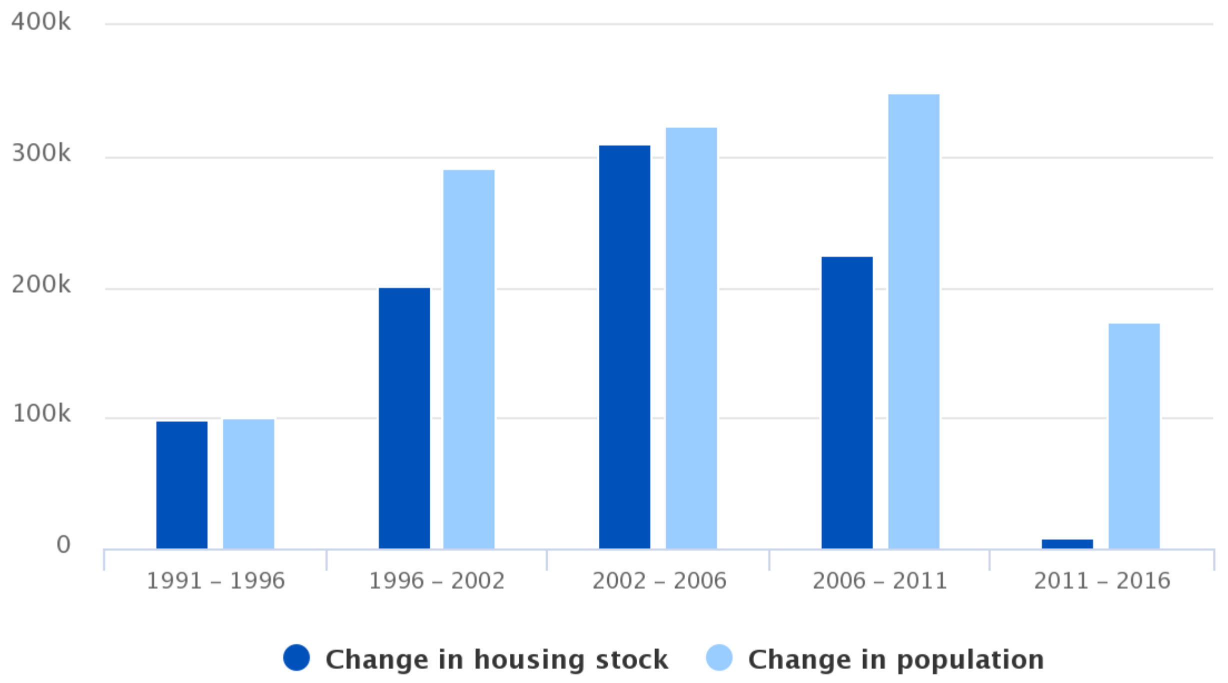
Why are rents soaring at an unprecedented rate in Ireland in the first place? Is it greedy landlords teaming together to take their tenants' incomes, or is it an economic problem of supply and demand?

If landlords were colluding, they would be operating in some sort of monopolistic structure and collectively driving rents up. The likelihood of this, however, is slim. On December 01, 2016, the Residential Tenancies Board published that it had 174,158 registered landlords and 705,183 occupants. It would be difficult for a landlord to increase their prices above market price without losing tenants to another landlord.

Prices will increase when supply decreases (as a result of an non-price determinant) and demand remains unchanged or increases, according to the laws of demand and supply. So has housing stock fallen, or has demand, via a growing population, increased?

The graph below shows that housing stock has not grown at the same rate as the population has increased between 2011 and 2016 than in comparison to previous years. There has been little increase in supply of housing in Ireland since the end of the Celtic Tiger in 2008, but population has continued to grow steadily.[16]

Figure 1.2 Change in population and housing stock, 1991 – 2016



Source: CSO Ireland

The Economic and Social Research Institute of Ireland predicts that the population will grow between 14% to 23% by 2030, and if housing stock does not increase quickly the shortage of supply in the market will continue to get worse. More pressure will fall on state resources to find temporary housing for a growing population.[17]

While prices may be increasing, it is clear that demand has not diminished. The Daft Rental Report for the fourth quarter of 2017 noted that there were less that 3,150 properties available to rent in the country, one of their lowest since their records began in 2006.

Demand to buy housing, rent's next substitute, has increased with the government's Help to Buy Scheme, which grants money to first time buyers to help them secure their deposits necessary for a mortgage. However, it appears to have had little effect on supply.

The Central Bank also relaxed mortgage deposit requirements from 20% to 10% for any mortgage credit above €220,000 for first time buyers. Easier access to credit caused demand-pull inflation in housing prices in the first two quarters of 2017 - and there was an increase of 14% in the number of mortgages drawn out between the first quarters on 2016 and 2017. However, this increase in housing prices did not continue in the second half of 2017 - housing prices rose on average by only 2% in Dublin, compared to 9.5% between January and June.[18]

It is likely that this increase in demand in housing, not matched by an increase in supply, has also pushed up demand for rental accommodation. If prospective buyers cannot buy a house, their next alternative is to rent - and the proportion of renters to homeowners is increasing in Ireland.

Why is supply not increasing, if prices keep increasing?

It seems that housing completions for 2018 are set to increase, and have been increasing in the past few years. The Construction Industry Federation of Ireland expects housing completions to reach 20,000 in 2018, with an overall increase of 42% between 2015 and 2017. However, commencements in 2016 were only 13,234.[19] The rate of housing completions in Ireland is way below demand, however, which is estimated to be around 30,000 units for 2017.[20] CIF Ireland also calculates that Ireland will demand approximately 110,000 more construction workers within the next three years to keep up with construction activity, with 50,000 workers already hired between 2013 and 2018.

The ease at which construction loans for developers in Ireland can be obtained has decreased since the end of the Celtic Tiger. Leverage levels for developers (the ability for a company to meet its financial obligations) have increased to around 50% - 65% [21], and the increase in regulations surrounding property loans have made it harder for developers to obtain the necessary credit for building. Financial institutions have become more cautious when lending money to construction firms after the crisis in the banking sector after 2008/09, when conditions for obtaining credit were much too relaxed. Supply of housing exceeded demand, and prices for housing fell, meaning developers could not meet repayments on loans that many should not have received in the first place.

The National Asset Management Agency has provided 2,472 residential properties for social housing providers to date, comprised of houses and apartments.[22] NAMA also plans to provide €750 million worth of lower interest rate loans to developers (around 4-6%) with the hope of funding construction for 6,000 homes.[23]

It seems clear that there are a number of steps that can be taken to alleviate the issue of supply in the housing and rental markets. Easier access to credit should be made available to developers to allow for residential construction. Promoting labour in the construction sector after the poor image it gained in the economic crisis and encouraging school-leavers to take up training in construction fields will ensure that there is not a labour shortage as construction increases in the coming years. Social housing may be a solution, but it is important to continue to promote a healthy, self-sustainable private construction sector in Ireland to ensure housing into the future, whatever the political climate. Avoiding rent regulations will incentivise supply of rental accommodation in the private sector, and with increased supply, rental prices should fall in the long run.

Ireland should look to building upwards in cities such as Dublin, Cork and Galway. The current height restrictions buildings in Dublin City should be lifted to allow for developers to construct taller buildings - which is a big incentive, considering land prices are so high in Dublin City. Building upwards should also alleviate urban sprawl, and eventually decrease rental and housing prices as supply increases. If urban sprawl is inevitable, then efforts should be made to improve public transport facilities, so the lack of housing in cities does not affect the living standards and economic growth in Ireland, as time taken to travel to and from work discourages labour in cities.

Constuction in the Dublin Docklands, January 2018

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