Rethinking the economics of land and housing

BSP-IIPP public lecture

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RETHINKING THE ECONOMICS OF LAND AND HOUSING

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with the New Economics Foundation

Foreword by JOHN MUELLBAUER

WHY ARE HOUSE PRICES in many advanced economies rising faster than incomes? Why isn’t land and location taught or seen as important in modern economics? What is the relationship between the financial system and land?

In this accessible but provocative guide to the economics of land and housing, the authors reveal how many of the key challenges facing modern economies—including housing crises, financial instability and growing inequalities—are intimately tied to the land economy. Looking at the ways in which discussions of land have been routinely excluded from both housing policy and economic theory, the authors show that in order to tackle these increasingly pressing issues a major rethink by both politicians and economists is required.

‘This excellent book is both thorough and comprehensive. I am convinced that it will quickly become an important reference for the general public and for economists, and hopefully also for policymakers.’

—MICHAEL KUMHOFF, senior research advisor, Bank of England

‘A fresh and comprehensive look at the problems created by a failure to consider the role of land in the economy of the UK.’

—KATE BARKER, author of the Barker Review of Housing Supply

‘This important book analyses land and housing with excellent clarity. Read it and you will understand the crucial underlying drivers of rising debt, increasing inequality and financial crises.’

—ADAIR TURNER, chairman of the Institute of New Economic Thinking

‘A lucid and convincing explanation of why a free-market approach to the land problem makes little sense, why the state needs to intervene, and the wide range of policy options available.’

—DANNY DORLING, author of All That is Solid. How the Great Housing Disaster Defines Our Times, and What We Can Do About It

Cover design and Illustrations: David A. Geo
House price-to-income ratios in advanced economies

Source: OECD
House prices driven by land values

Real land and house price indices for UK, 1945-2008 (1945=100)

Source: Ryan-Collins, Lloyd & MacFarlane (2017: 8) based on data compiled by Paul Cheshire
“The rent of land, therefore, considered as the price paid for the use of the land, is naturally a monopoly price. It is not at all proportioned to what the landlord may have laid out upon the improvement of the land, or to what he can afford to take; but to what the farmer can afford to give.”

Smith, Adam (1776) *Wealth of Nations*, p162
## Land is not ‘capital’

<table>
<thead>
<tr>
<th>Land</th>
<th>Capital</th>
</tr>
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<tbody>
<tr>
<td>Finite supply</td>
<td>Supply constrained by labour/energy only</td>
</tr>
<tr>
<td>Fixed/immobile</td>
<td>Highly mobile</td>
</tr>
<tr>
<td>Appreciates in value with economic growth</td>
<td>Depreciates (wear &amp; tear and technological innovation)</td>
</tr>
<tr>
<td>Ownership enables extraction of economic rent derived from collective investment</td>
<td>Rentier profits constrained by competition, depreciation, innovation</td>
</tr>
<tr>
<td>Multiple &amp; conflicting economic uses: consumption good, store of value, source of collateral</td>
<td>N/A</td>
</tr>
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The withdrawal of public home building

Source: Office of National Statistics in Ryan-Collins et al. (2017, p82)
The low-supply equilibrium

1. Increase in numbers of homeowners
2. Increases the number of insiders with an interest in house price growth
3. House prices escalate as demand is not being met
4. More non-homeowners view housing as an investment and perceive disadvantage in not being a homeowner
5. Government assists homeownership
House prices and mortgage credit over 130 years in advanced economies

Source: Jorda, Schularick and Taylor 2017
Mortgage credit and non-mortgage credit (commercial and domestic) outstanding in 17 advanced economies, 1950-2013

Source: Jorda, Schularick and Taylor 2017
UK bank credit allocation and house prices since 1963

A house price-finance feedback cycle

Financial innovation - securitisation of mortgage debt

Increased supply of mortgage credit

Banks increase profits and capital base

Increased mortgage debt relative to incomes

Government equity loans & guarantees of house purchases

Expectation of future house price increases

Increased demand for mortgage debt

Increased land and house prices relative to incomes

Stagnating wages, pensions & social security increases demand for home as financial asset

Speculative domestic and overseas & buy-to-let purchases

Source: Ryan-Collins et al. (2017, p121)
Non-financial assets as % GDP in the UK

Wealth to income ratio in the UK including & excluding capital gains

Source: Ryan-Collins et al. (2017, p172), original source: Piketty and Zucman (2013)
Net property wealth in the UK by decile

Source: Ryan-Collins et al. (2017, p174)
Where things are different

House-price to income ratio, indexed against long-term average (100)

- Germany
- Japan
- Korea
- Anglo-Saxon average

Quarterly data from Q1-1995 to Q1-2015
Development Corporations to assemble land and capture public value
Germany house prices and credit allocation

Source: Bundesbank & Knoll et al (2017)

- Owned with mortgage
- Social rented
- Owned outright
- Private rented