

The revival of rent controls in a market driven world

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Rent Controls: An Overview

Rent controls were introduced across Europe around 1915/1916 in response to the impact of the First World War on the movement of labour that was necessary to meet wartime industrial requirements. As a result some places found themselves with massively increased populations which led to higher rents for both those coming into the area but also those who already lived locally. This generated a great deal of concern and in some cases unrest – to the point where governments across Europe felt that it was a political necessity to respond.

The type of rent control usually introduced was what is currently called 1st generation – i.e. rents were fixed at their current (or 1914) levels and there was no right to increase these rents either for the existing tenant or when the property was vacated. Moreover, controls were generally nationwide, although they were only effective in areas where demand was high.

At the time when rent control was introduced it was seen as a temporary wartime measure. However, low levels of housing investment during the war meant that there were increasing housing shortages. Rent controls were popular among voters (although not of course among owners) so controls. There was some decontrol in the 1930s which allowed rents to rise, but then controls were extended or re-introduced in 1939 and in most European countries controls – with modifications - continued after the war for quite extended periods.

The results were well documented. In the early years when rent controls remained unchanged and there was excess supply, when a property fell vacant potential new tenants made side payments or simply higher rents in areas where demand was high. There was also little or no reasons for landlords to improve or even maintain their properties so housing standards deteriorated and tenants had little power to require repair and improvement.

In some countries, especially as new tenancies were increasingly decontrolled, existing tenants in controlled properties did not move on. As a result, there was a great deal of under-occupancy in the controlled sector. When the properties were ultimately vacated, they were often sold to owner-occupiers who were prepared to upgrade the dwelling rather than letting it in the rental sector. Finally, there was very little new investment in the privately rented sector both because some controls often remained but also because better off households moved into owner-occupation so demand was mainly from low income households.

In other countries notably the Netherlands and Germany, much more sophisticated forms of regulation were introduced which made it worthwhile for landlords to remain in the sector, especially if owner-occupation was not given preferential treatment.

Importantly after 1945 many European countries developed large numbers of new rental housing which was let at submarket rents to lower income households, so the private rented sector increasingly became the 'residual' tenure for those unable to gain access to either owner-occupation or social rented housing.

Decontrol in the later part of the 20th century.

There was a considerable movement towards greater decontrol as the post-war quantitative shortages in housing were overcome from the early 1970s. The table below refers to the changes over a thirty year period to 2010.

Some countries moved from strong controls to almost no controls - including England, Finland and Norway. Others, notably the Netherlands, Germany and Sweden, have retained fundamentally the same system for forty years.

Over the last decade however there has been a growing interest, particularly at the city level, in re-introducing stronger rent controls in the face of rising rents and worsening affordability.

Degree of regulation in early 1980	Degree of regulation in late 2000s
High	
Spain	
Finland	
Netherlands	→ Netherlands
Denmark	
England	
Medium	
Sweden	→ Sweden
Germany	→ Germany
Norway	→ Switzerland
Switzerland	→ Denmark
	→ Spain
	→ France
France	→ Ireland
Low	
Ireland	→ Norway
	→ England
	→ Finland

The current extent of regulation

The majority of Western European systems have unlimited security of tenure and in tenancy rents set in line with an index – e.g. general prices. These arrangements have often been in place for decades.

England stands out as having both no direct rent controls and particularly short term tenancies (usually a year). The current government is intending to introduce unlimited security of tenure but with significant exceptions – eg when the landlord wants to sell. Scotland has already introduced unlimited security of tenure although again with a large number of exceptions. However, they are now looking to control rent increases in some areas.

Countries with relatively stable regulatory systems tend to have larger private rented sectors and therefore a stronger political will to favour tenants. Arguably, it is one reason for the move towards greater security in Britain as around 1 in 5 households now privately rent.

Countries which have had controls in place for decades and relatively large privately rented sectors often have stronger constraints on entry into other tenures. A number have two level regulation systems – e.g. Denmark (new properties since 1991 are not controlled); the Netherlands (market rents above a threshold around 750 euros per month).

Growth in the Private Rented Sector

Over the last decade – and in some countries since before the turn of the century - the privately rented sector has been growing, often significantly, in the majority of European countries. This reflects both increasing difficulty in entering owner-occupation and in some countries a reduction in social rented housing and transfers into private renting.

But despite this growth private rents have also been rising and there is increasing concern about affordability for lower income households. New build has generally been concentrated on the middle and upper end of the market.

There have also been new participants - notably institutional investors initially mainly local, looking for a secure return but since the turn of the century including new investors looking for short term capital gains. The potential for such gains often arises as a side effect of regulation as investors find gaps in the system.

Most institutional landlords however state that they are happy with a clearcut regulatory arrangement which provides longer term security and within-tenancy indexation (as long as there is proper enforcement of rules – and accepted exceptions). But as noted above, some, notably international private equity investors, are looking for short term capital gains.

Increasing Pressures

The growth in such investors has raised widespread concerns about what is perceived to be a shift towards regarding housing as a tradeable asset rather than as a home and especially the consequences of this, particularly for lower income households.

Financialisation – as it is often termed – is seen as a major reason for rising rents and gentrification in many European cities.

- A notable issue - especially in Germany and Sweden - is that of 'renovictions' where rents are enabled to rise in response to renovations and energy efficiency investment to the point where the existing tenants find the new rents (even though regulated) unaffordable.
- This is often identified as the Blackstone problem because of their investment in Sweden Germany and Denmark which introduced legislation to increase security of tenure. The more general issue has become highly political in a number of European countries and is a significant factor in the growing pressure to introduce new forms of rent control.

General Issues

Rent controls are generally popular with voters (e.g. 65% plus Londoners approve of rent controls – even though the Mayor has no powers to introduce them) – so it is increasingly a political issue.

Most of the regulatory initiatives are at least initially concentrated on stress areas - although there is a tendency for the system to spread to areas with lower demand (e.g. Germany; Ireland). Many are initiated at regional or city level although national governments generally set the framework rules.

Often the supply of tenancies is declining for other reasons – notably the growth of short term lettings especially in tourist areas. This has been a particularly important way round mainstream regulation particularly in cities with large numbers of tourists or short term employees.

Welfare systems are becoming less generous in many countries across Europe so that lower income households are finding it increasingly difficult to afford adequate accommodation in accessible areas. At the same time income distribution is becoming more unequal – increasing the numbers finding it difficult to pay the rent.

Examples of Rent Control Initiatives

In Germany there have been rent and security of tenure controls for decades. Since 2013 additional rent controls have been introduced in tight housing markets cities (now over 300 cities/municipalities) by which initial rents are limited to 10% above the local comparator. At the same time the allowable rent increase in existing tenancies was reduced from 20% to 15% pa. Stronger controls in Berlin including rent reductions were ruled out by central government.

In France 28 agglomerations with tight housing markets have been identified. Local authorities can apply to pilot rent control measures for five years. Paris was the first jurisdiction to implement the measure in 2019 based on reference rents, followed by three further cities in 2019 and more in line.

In the Netherlands the regulated housing sector where government can determine rent increases includes properties with rents below around 750 euros per month. A new system will cap rents on middle market properties with rents under 1,100 euros per month.

The private rented sector in Ireland was highly deregulated – but then moved to a general approach that rents should be in line with local market rents for similar properties. In 2016, Rent Pressure Zones ("RPZ") were introduced for a three year period during which rents could only rise according to a prescribed formula by a maximum of 4% annually. This has now been extended -although there is limited security of tenure. The government has introduced better quality good data collection systems which improve enforcement.

Scotland has lately moved from a pure market system to one with long term security although many exceptions. The government is aiming to introduce a zonal system which identifies stress areas.

In Spain Catalonia introduced a rent control law in 2020 but it was struck down by the constitutional court. National government has now introduced a right to housing law which enables regional governments to set rent controls on large landlords in stress areas, together with some incentive for small landlords to reduce rents.

Impact of Increasing Rent Controls

So far there is little evidence that the increases in regulation have impacted on investors' preparedness to invest. This may be in part because stronger constraints (such as the attempt to return to tighter rent control in Berlin and additional controls in Paris) have not been implemented.

But it is also because across countries rents appear not to have been fully constrained to the stabilised amounts. This is partly because tenants have not generally appealed the rents.

There is also evidence that implementation costs are quite high particularly because of concerns around data quality (and implicitly therefore avoidance and evasion of controls).

Conclusions

Much of Western Europe are used to rent stabilisation policies which have been in place for many years (generally involving free market rents between tenancies and index linked increases within tenancies).

But success depends as much on the economic environment. For instance, Germany had low inflation and falling house prices for decades so there was little avoidance except in the most prosperous cities. Berlin has come late to the issue as population and rents/prices which had been very low started to rise in this century.

In some regulatory contexts, agreed initial market based rents may sometimes be allowed to be significantly above comparator rents. Many systems allow generous rent increases related to investment in the property.

Over the last few years, the environment has become very different with better rented housing increasingly moving more up market leaving lower income households with poor quality housing and unaffordable rents.

In this context, issues around private renting have become much more politically sensitive with concerns about international investors entering the market. The result has been increasing pressure to introduce stronger rent stabilisation policies both nationwide as well as in many cities where local or regional authorities have capacity to regulate.

The initiatives are generally more sophisticated and adjustable than in earlier versions but are likely over time to reduce the incentive to supply privately rented housing. There is thus continuing concern about uncertainty and unforeseen /unintended consequences into the longer term.

A more fundamental issue is whether privately rented housing is suited for lower income households. But this raises major questions for governments everywhere about how to provide adequate affordable housing for all.

Christine Whitehead 5th March 2023