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Federal Reforms Should Include Housing and Land-Use Deregulation

John L. Ligon

Abstract

Housing affordability has been a growing problem in the United States beginning with regulations starting in the 1970s combined with federal programs and subsidies beginning in the 1990s that have hampered supply and increased demand, thereby increasing prices. After prices bottomed out following the 2008 housing market collapse, the price of homes has begun rising again to the point that in some markets median home prices have exceeded pre-collapse prices, and housing is seriously or severely unaffordable in some highly regulated markets. While state and local deregulatory reforms would have the greatest impact, the federal programs and subsidies that are exacerbating the problem should be eliminated to increase housing affordability.

Despite several years of decline in the aftermath of the 2008 housing market collapse, home prices in most markets across the United States are steadily increasing. Prices in some select markets now exceed levels achieved at the height of the mortgage credit bubble in the mid-2000s. In the post-housing-crisis recovery, tight supply and strong demand have put upward pressure on prices, making housing across the U.S. less affordable. Government regulations, mostly imposed at the state and local levels, remain the most significant hindrance to housing supply, holding back inventory that would moderate high prices and improve affordability in many U.S. markets over time.

While state and local government regulations are the crux of the problem, those problems are exacerbated by federal programs like the federal mortgage insurance and guarantee programs. Limiting

Key Points

- Since bottoming out, some housing market prices have returned to pre-2008 collapse prices, while American households are taking on higher levels of mortgage debt to finance more expensive homes.
- Tight supply and strong demand have put upward pressure on prices, making housing across the U.S. less affordable. Government regulations, mostly imposed at the state and local level, remain the most significant hindrance to housing supply, holding back inventory that would moderate high prices and improve affordability in many U.S. markets over time.
- Highly regulated housing markets are the most volatile, experiencing more dramatic price volatility (with longer durations of boom-bust periods) across market bubble cycles.
- In approximately 38 percent of U.S. markets, housing is seriously or severely unaffordable: Median home prices exceed median household incomes by more than four times.
- Federal policymakers should eliminate programs hindering supply, thus allowing more Americans to enter the housing market and live closer to higher productivity areas.

This paper, in its entirety, can be found at **http://report.heritage.org/bg3301**

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the scope of these federal programs would moderate the interplay between local, state, and federal policies that affect housing affordability, even though the most significant improvement would be gained by deregulatory reform on the state and local level. For housing to be made more affordable for more Americans, regardless of any deregulatory reforms at the state and local levels, federal policymakers should eliminate federal programs that restrict land use, that constrain the supply of new housing inventory, and that encourage higher levels of mortgage debt, all of which increase housing costs.

Land-Use and Housing Development Regulations Increase Costs

Aside from geographical constraints,[1] the most significant limitations to developable land and new housing supply arise from government regulation. Unlike some nations, South Korea and the United Kingdom, for example, the U.S. does not have an explicit federal land-use regulatory system.[2] Such regulations are predominantly imposed by state and local governments in the U.S.[3] and generally involve some combination of at least the following restrictions:[4]

- Prolonged approval periods for attaining building permits;
- Building and construction fees;
- Allowance restrictions for new construction, including requirements for density on existing properties (primarily impacting the "building up" in urban areas); and
- Explicit growth boundaries.

Everything else being equal, these regulations limit the availability of land and housing development, thus restricting housing supply and increasing costs. Numerous economic studies confirm that highly regulated housing markets face restricted supply, which ultimately creates upward pressure on prices and costs in these markets.[5]

More restrictive (highly regulated) housing markets are also the most volatile: Highly regulated markets have experienced more dramatic price volatility (with longer durations of boom-bust periods) across market bubble cycles.[6] Households taking on higher levels of mortgage debt to finance more expensive

1. Albert Saiz, "The Geographic Determinants of Housing Supply," *The Quarterly Journal of Economics*, Vol. 125, No. 3 (August 2010), pp. 1253–1296, http://www.jstor.org/stable/27867510?seq=1#page_scan_tab_contents (accessed October 16, 2017).
2. Casey J. Dawkins and Arthur C. Nelson, "Urban Containment Policies and Housing Prices: An International Comparison with Implications for Future Research," *Land Use Policy*, Vol. 19 (2002), pp. 5–10, https://s3.amazonaws.com/academia.edu.documents/46572982/s0264-8377_2801_2900038-220160617-28206-1jtr7fg.pdf?AWSAccessKeyId=AKIAIWOWYYGZ2Y53UL3A&Expires=1522278697&Signature=CLYkV7e%2BdSAGD12tsyeWTlTQqRw%3D&response-content-disposition=inline%3B%20filename%3DUrban_containment_policies_and_housing_p.pdf (accessed October 24, 2017).
3. Joseph Gyourko, Albert Saiz, and Anita A. Summers, "A New Measure of Local Regulatory Environment for Housing Markets: The Wharton Residential Land Use Regulatory Index," *Urban Studies*, Vol. 45, No. 3 (2008), http://journals.sagepub.com/doi/pdf/10.1177/0042098007087341 (accessed March 20, 2018).
4. David D. Foster and Anita A. Summers, "Current State Legislative and Judicial Profiles on Land-Use Regulations in the U.S.," Samuel Zell & Robert Lurie Real Estate Center of the Wharton School at the University of Pennsylvania *Working Paper* No. 512, September 20, 2005, http://realestate.wharton.upenn.edu/working-papers/current-state-legislative-and-judicial-profiles-on-land-use-regulations-in-the-u-s/ (accessed October 16, 2017).
5. Edward Glaeser and Joseph Gyourko, "The Economic Implications of Housing Supply," *Journal of Economic Perspectives*, Vol. 32, No. 1 (2018), https://pubs.aeaweb.org/doi/pdfplus/10.1257/jep.32.1.3 (accessed March 22, 2018); Edward L. Glaeser and Bryce A. Ward, "The Causes and Consequences of Land Use Regulation: Evidence from Greater Boston," *Journal of Economics*, Vol. 65 (2009), pp. 265–278, https://scholar.harvard.edu/glaeser/files/the_causes_and_consequences_of_land_use_regulation_evidence_from_greater_boston_2009.pdf (accessed September 25, 2017); and Edward L. Glaeser, Joseph Gyourko, and Raven Saks, "Why Is Manhattan So Expensive? Regulation and the Rise in Housing Prices," *Journal of Law and Economics*, Vol. 48 (October 2005), pp. 331–369, http://repository.upenn.edu/cgi/viewcontent.cgi?article=1007&context=penniur_papers (accessed September 25, 2017).
6. Glaeser and Gyourko, "The Economic Implications of Housing Supply," pp. 15–18, and Edward L. Glaeser, Joseph Gyourko, and Albert Saiz, "Housing Supply and Housing Bubbles," *Journal of Economics*, Vol. 64, No. 2 (2008), pp. 198–217, https://dash.harvard.edu/bitstream/handle/1/2962640/housing%20supply.pdf (accessed September 25, 2017).

TABLE 1

Land-Use Regulations Result in Less Affordable Housing Markets

Housing markets that are more regulated—as indicated by higher scores in the Wharton Residential Land Use Regulatory Index (WRLURI)—also tend to have higher ratios of median home prices relative to median household incomes, a standard measure of home purchase affordability.

	WRLURI	**RATIO: MEDIAN HOME PRICE TO MEDIAN HOUSEHOLD INCOME** (3.00–4.99; 5.00–6.99; 7.00+)		
Metropolitan Statistical Area	Index Value	March 2001	March 2006	March 2012
Providence, RI	1.76	3.48	5.82	3.98
Boston, MA–NH	1.50	4.35	5.96	4.40
Monmouth–Ocean, NJ	1.17	4.08	8.17	5.64
Philadelphia, PA	1.04	2.43	4.12	3.26
San Francisco, CA	1.01	6.59	10.23	6.46
Seattle, WA	0.96	4.16	5.89	4.08
Denver, CO	0.85	3.76	4.22	3.59
Phoenix, AZ	0.73	2.92	5.40	2.68
Fort Lauderdale, FL	0.71	2.96	6.64	3.07
New York, NY	0.68	4.45	7.12	5.24
Riverside–San Bernardino, CA	0.62	3.45	7.57	3.64
Harrisburg–Lebanon–Carlisle, PA	0.54	2.50	2.97	2.78
Los Angeles, CA	0.54	5.18	11.06	6.79
Springfield, MA	0.54	2.98	4.54	3.67
San Diego, CA	0.50	5.13	9.03	5.85
Hartford, CT	0.47	2.87	4.09	3.31
Washington, DC	0.38	2.81	5.40	3.52
Minneapolis–St. Paul, MN–WI	0.35	2.88	3.89	2.59
Portland, OR	0.30	3.48	5.26	3.84
Milwaukee–Waukesha, WI	0.29	3.03	4.08	3.36
Detroit, MI	0.11	2.75	3.01	1.53
Allentown–Bethlehem–Easton, PA	0.10	2.63	4.10	3.11
Akron, OH	0.08	2.68	2.92	2.31
Chicago, IL	0.08	3.27	4.32	2.82
Atlanta, GA	0.05	2.68	3.02	2.14
Pittsburg, PA	0.05	2.10	2.41	2.27
Scranton–Wilkes–Barre–Hazelton, PA	0.04	2.12	2.74	2.48
Salt Lake City–Ogden, UT	–0.09	3.30	3.81	3.07
Grand Rapids–Muskegon–Holland, MI	–0.12	2.73	3.06	2.32
Tampa, FL	–0.17	2.57	4.83	2.51
Cleveland–Lorain–Elyria, OH	–0.18	2.88	3.19	2.39
San Antonio, TX	–0.23	2.16	2.61	2.49
Houston, TX	–0.26	2.11	2.38	2.31
Rochester, NY	–0.30	2.08	2.31	2.37
Dallas, TX	–0.33	2.38	2.74	2.43
Oklahoma City, OK	–0.40	2.11	2.45	2.39
Dayton–Springfield, OH	–0.50	2.28	2.57	2.06
Cincinnati, OH–KY–IN	–0.56	2.64	2.84	2.42
St. Louis, MO–IL	–0.71	2.39	3.07	2.45
Indianapolis, IN	–0.75	2.76	2.68	2.45
Kansas City, MO–KS	–0.79	2.84	2.71	2.43

SOURCE: Joseph Gyourko, Albert Saiz, and Anita Summers, "A New Measure of the Local Regulatory Environment for Housing Markets: The Wharton Residential Land Use Regulatory Index," October 22, 2006, p. 46, http://realestate.wharton.upenn.edu/wp-content/uploads/2017/03/558.pdf (accessed January 23, 2018), and Zillow Research, Data, More Metrics, Mortgage Affordability, Rent Affordability, Price-to-Income Ratio, https://www.zillow.com/research/data/ (accessed January 26, 2018).

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homes are another side effect. Indeed, misguided federal policies, such as increased use of taxpayer-covered mortgage insurance and guarantee programs,[7] have generally magnified this housing cost problem.

Long-term Decline in U.S. Housing Affordability

Over the past half century, housing has generally become less affordable across the U.S., and highly regulated markets remain less affordable than those areas with minimal land-use and development regulations.[8] From the early 1970s through the mid-1990s, as states and local governments slowly implemented land-use and housing-development regulations, housing gradually became less affordable. Since the 1990s, however, when the federal government began to implement its own "smart growth" policies,[9] in addition to the incredible expansion of demand-side affordable housing (mortgage credit) policies, housing affordability has steadily decreased.

This combination of regulations and subsidies was central to the dramatic increase in home prices during the mortgage credit bubble in the mid-2000s.[10] As a consequence, median home prices have outpaced median household incomes, a price-to-income ratio that increased from 2.75 to 3.44 between 1990 and 2017.[11]

There has been a resurgence in prices since post-crisis lows in 2011 and 2012. The recovery in home prices has largely resulted from strong demand combined with the lack of housing supply.[12] At present, home prices in many housing markets across the U.S. exceed the peak levels reached prior to the collapse of the housing market in the mid-to-late 2000s.[13] Although there is variation across markets, approximately 38 percent of markets are "seriously" and "severely" unaffordable due to these demand–supply conditions.[14] In fact, in highly regulated markets, such as Boston and Portland, Oregon, median home prices remain *five times* above median household incomes, and even worse, home prices outpace incomes nine times in numerous California housing markets.[15]

While homeowners benefit from increased home equity, the higher home prices also make it more difficult to purchase a home. Furthermore, increasing prices can keep people from selling their homes in order to relocate or "purchase up," keeping sales down in such housing markets.[16] Overall, the sharp

7. John L. Ligon, "Fannie Mae Should Rethink Its Plans to Expand Role in Housing Finance Sector," The Daily Signal, June 29, 2017, https://www.dailysignal.com/2017/06/29/fannie-mae-rethink-plans-expand-role-housing-finance-sector/.
8. Wendell Cox and Hugh Pavletich, "14th Annual Demographia International Housing Affordability Survey: 2018," Demographia, 2018, p. 26, http://www.demographia.com/dhi.pdf (accessed March 20, 2018).
9. Wendell Cox and Ronald Utt, "Smart Growth, Housing Costs, and Homeownership," Heritage Foundation *Backgrounder* No. 1426, April 6, 2001, http://www.heritage.org/housing/report/executive-summary-smart-growth-housing-costs-and-homeownership.
10. John L. Ligon, "A Pathway to Shutting Down the Federal Housing Finance Enterprises," Heritage Foundation *Backgrounder* No. 3171, December 21, 2016, http://www.heritage.org/housing/report/pathway-shutting-down-the-federal-housing-finance-enterprises.
11. Zillow Research, Data, https://www.zillow.com/research/data/ (accessed October 23, 2017).
12. Since May 2012, the demand for homes in the U.S. has steadily increased; the number of days homes remain on the market decreased from 111 to 73 between May 2012 and May 2017; the number of new home listings has remained roughly the same for the past couple of years, decreasing slightly from 577,821 in June 2015 to 561,740 in June 2017. Svenja Gudell, "June 2017 Market Report: Inventory Is Down, but Listings Aren't," Zillow Research, July 20, 2017, https://www.zillow.com/research/june-2017-market-report-15956/ (accessed October 16, 2017), and Svenja Gudell, "July Case–Shiller Results: Home Prices Still Gaining," Zillow Research, September 26, 2017, https://www.zillow.com/research/july-case-shiller-results-16707/ (accessed October 23, 2017).
13. Svenja Gudell, "August 2017 Market Report: More Than Half of U.S. Homes Have Rebounded to Pre-Recession Peak Values," Zillow, September 21, 2017, https://www.zillow.com/research/august-2017-market-report-16651/ (accessed September 22, 2017).
14. By one count, there are 175 housing markets (populations exceeding 250,000) across the U.S. with 54 considered major housing markets (populations exceeding one million). Generally, housing is considered unaffordable when home prices are three times (or greater) compared to household incomes. "Seriously" unaffordable housing markets would correspond to price-income ratios exceeding four, and "severely" unaffordable housing markets with price-income ratios above five. Cox and Pavletich, "14th Annual Demographia International Housing Affordability Survey: 2018."
15. Zillow Research, Data.
16. Robert C. Ellickson, "The Irony of Inclusionary Zoning," *Southern California Law Review*, Vol. 54 (1981), pp. 1184–1187, http://digitalcommons.law.yale.edu/cgi/viewcontent.cgi?article=1467&context=fss_papers (accessed September 25, 2017), and Robert C. Ellickson, "Suburban Growth Controls: An Economic and Legal Analysis," *The Yale Law Journal*, Vol. 86 (1977), pp. 385–511, http://digitalcommons.law.yale.edu/fss_papers/470/ (accessed March 20, 2018).

increase in home prices across the U.S. has at best resulted in mixed effects in many housing markets, limiting the available inventory of affordably priced homes while nominally benefiting homeowners with higher home equity. The dramatic increase in home prices has certainly restricted opportunities for affordable entry points to homeownership, especially for those looking to purchase homes valued in the bottom two-thirds of the market.[17]

Improve Housing Affordability by Eliminating Federal Land-Use Regulations

Federal government intervention in jurisdiction over the land use and development patterns of local housing markets further exacerbates problems caused by regulations at the state and local level. Thus, federal policymakers should take the necessary steps to eliminate any federal regulatory programs that restrict land use and development in housing markets across the U.S. Specific reforms should include rescinding the Affirmative Furthering Fair Housing rule promulgated by the Department of Housing and Urban Development (HUD),[18] as well as eliminating the "sustainable" and "livable communities" initiatives managed by both HUD and the Environmental Protection Agency.[19]

Such federal smart-growth programs place onerous regulations on the development patterns in local housing markets and restrict individual choice in housing by forcing "people to live at higher densities, in multi-family units, townhouses, or clustered single-family developments, while restricting the expansion of suburban commercial development."[20] Similar programs that have been in place for the past several decades waste federal taxpayer dollars,[21] as these funds tend to target areas that remain low productivity areas. Also, contrary to advocate concerns of overdevelopment in the U.S., 95 percent of land in the continental U.S. remains undeveloped.[22]

In addition, federal policymakers should eliminate the federal mortgage guarantee and insurance subsidy programs that encourage high levels of mortgage debt used to finance expensive homes. Absent getting the federal government out of the home-financing market altogether, federal policymakers should ensure appropriate pricing of risk for mortgages across the U.S., as well as decreases in the loan limits in the federally backed mortgage insurance and guarantee programs.[23] Limiting the scope of these federal mortgage insurance and guarantee programs, particularly within those high cost and highly regulated local markets of the U.S., would moderate the interplay between local, state, and federal policies that affect housing affordability.

Deregulations at the state and local level would have the most significant impact on expanding the housing supply in markets across the U.S. Such deregulatory efforts at the state and local levels would likely ease the restrictions on housing supply and over time expand the inventory of affordable housing and moderate prices, which would likely make it easier for more Americans to live and work closer to areas with higher productivity. Aca-

17. Peter J. Wallison and Edward J. Pinto, eds., "The Taxpayer Protection Housing Finance Plan: Gradually Winding Down Fannie Mae and Freddie Mac and Improving the FHA," American Enterprise Institute, January 23, 2018, p. 36, https://www.aei.org/wp-content/uploads/2018/02/Taxpayer-and-Home-Buyer-Protection-Housing-Finance-Plan-1.26.18.pdf (accessed March 22, 2018).
18. Senator Mike Lee, "The Atrocious Housing Rule Ben Carson Can End," The Daily Signal, January 18, 2018, http://dailysignal.com/2018/01/18/atrocious-housing-rule-ben-carson-can-end/, and Senator Mike Lee, "We Don't Need a National Zoning Board," The Daily Signal, May 16, 2016, http://dailysignal.com/2016/05/16/we-dont-need-a-national-zoning-board/?utm_content=bufferccd02&utm_medium=social&utm_source=twitter.com&utm_campaign=buffer.
19. Department of Housing and Urban Development, "Program Offices," https://www.hud.gov/program_offices (accessed October 19, 2017), and Environmental Protection Agency, "Smart Growth," https://www.epa.gov/smartgrowth (accessed October 19, 2017).
20. Joshua Utt and Wendell Cox, "The Costs of Sprawl Reconsidered: What the Data Really Show," Heritage Foundation *Backgrounder* No. 1770, June 25, 2004, p. 1, http://www.heritage.org/report/the-costs-sprawl-reconsidered-what-the-data-really-show.
21. Peter Sperry, "Top Ten Ways to Avoid Wasting the Surplus," Heritage Foundation *Report*, September 8, 1999, http://www.heritage.org/budget-and-spending/report/top-ten-ways-avoid-wasting-the-surplus.
22. U.S. Department of Agriculture, "National Resources Inventory," 1997 (revised in 2000) and 2012, https://www.nrcs.usda.gov/wps/portal/nrcs/main/national/technical/nra/nri/ (accessed October 19, 2017), and Ronald Utt, "Will Sprawl Gobble Up America's Land? Federal Data Reveal Development's Trivial Impact," Heritage Foundation *Backgrounder* No. 1556, May 30, 2002, p. 8, http://www.heritage.org/environment/report/will-sprawl-gobble-americas-land-federal-data-revealdevelopments-trivial-impact.
23. Ligon, "A Pathway to Shutting Down the Federal Housing Finance Enterprises," pp. 11 and 13.

demic research suggests that robust deregulatory reforms at the state and local levels of government, especially in select high-cost markets on the coasts, would likely result in a more efficient allocation of labor across the U.S. and consequently boost overall economic growth.[24]

Conclusion

For at least the past half century, government regulations that restrict land availability and housing development—predominantly those imposed at the state and local level, but exacerbated by interventions at the federal level—have increased costs and made housing less affordable across the U.S. Between 1990 and 2017, median home prices relative to median household incomes increased significantly. Moreover, in approximately 38 percent of the markets across the U.S., housing is seriously or severely unaffordable: Median home prices exceed median household incomes by more than four times. Thus, irrespective of deregulatory reforms by state and local governments, federal policymakers should eliminate the various federal programs that increase housing costs by restricting land use, constraining the supply of new housing inventory, and encouraging higher levels of mortgage debt—thus making housing more affordable for more Americans.

*—**John L. Ligon** is Senior Policy Analyst and Research Manager in the Center for Data Analysis, of the Institute for Economic Freedom, at The Heritage Foundation.*

24. Using data from 220 metropolitan areas across the U.S. between 1964 and 2009, economists Hsieh and Moretti estimate that constrictive regulations on land use and housing development resulted in 50 percent lower economic growth in the U.S. The authors' estimates also suggest that removing land-use regulations, particularly in the highly productive metropolitan areas of New York, as well as San Francisco and San Jose, could boost aggregate output in the U.S. by 8.9 percent. Chang-Tai Hsieh and Enrico Moretti, "Housing Constraints and Spatial Misallocation," National Bureau of Economic Research *Working Paper* No. 21154, May 2017, pp. 2 and 18–25, http://www.nber.org/papers/w21154.pdf (accessed October 16, 2017).