Θ

QuantEcon, Inc.
Economics and Finance Consulting

February 13, 2019

To: Alissa Keny-Guyer, Chair, House Committee on Human Services and Housing
Honorable Members of the House Committee on Human Services and Housing

From: Randall Pozdena, PhD CFA, President, QuantEcon, Incorporated

Re: Testimony re SB 608 will worsen Oregon's housing crisis

It is my understanding that your committee will have a public hearing on SB 608 and that you are accepting testimony with regard to this Bill. SB 608, if enacted, will adversely affect housing markets in Oregon and aggravate the crisis of unaffordable and inaccessible housing. The purpose of submitting this memo is to urge you to resist any further intervention by the State in the rental market for real estate.

These are my personal views based on my professional training and 40 years of research and writing in housing economics and finance. *I have received no payment or encouragement from any entity for providing these views.*

Summary of my opinions

- If enacted, it appears that SB 608 would repeal the existing statewide prohibition on city and county ordinances regulating rents. I am opposed to any change in the law that will permit regulation of rent levels or rates of increase. I am also opposed to adoption of policies that interfere with the landlords' ability to manage their relationship with their tenants beyond those in current law.

- The current high cost and limited availability of housing in Oregon is a direct consequence of overly-restrictive Oregon land use policies. Further intervention in the operation of housing markets can do nothing to redress these distortions and effects.

- On the contrary, restricting landlords' ability to manage their private property in a manner consistent with their significant investments in and risks to that investment dilutes the landlords' property rights and, thus, constitutes a taking.

- The market will respond by withdrawing or reducing additional supply of rental housing. Landlords will also accelerate rental price increases above what otherwise would have occurred to try to offset the additional risks and transactions costs the Bill imposes.

Facts behind my opinions

- We economists have long concluded from observation that rent control has pernicious effects on both tenants and landlords. It introduces distortions in the balance of demand and supply (inefficiency) and creates inequities in otherwise well-functioning markets for housing services. An opinion survey of the membership of the American

Economics Association over 20 years ago found 93.5 percent agreement on this position, and recent surveys have similar findings.[1]

- Even interventionist economists such as Paul Krugman are in agreement that the adverse impact of rent control is "among the best-understood issues in all of economics, and—among economists, anyway—one of the least controversial".[2]

- More importantly, Oregon's current housing affordability and equity challenges do not have their origins in the manner in which tenants and property owners contract to obtain housing services. Rather, the affordability challenges are due to policies of the State that have made the supply of land for housing progressively more costly as population and income have grown. Site values per housing unit have increased by 900 percent between 1990 and today and have been linked to Oregon's implementation of "smart growth" policies in the 1970s.

- Central among the policies responsible for this growth is the imposition of Urban Growth Boundaries that rigidly circumscribe where housing and how much development may occur. Rising site values, rents and home prices are simply a warning that housing supply is not keeping up with demand; imposing rent control is tantamount to shooting the canary in the coal mine.

- It is axiomatic that when growing demand meets constrained supply that the price, availability, diversity and financial accessibility of housing services will suffer. Indeed, these were the conditions, in World War II, that raised fears of housing shortages when soldiers returned. Fortunately, a vigorous and responsive supply of development opportunities allowed a boom in affordable housing. As a result, by 1960, wartime government intrusion in the rental market had ceased everywhere but New York City.[3]

- If rental supply and demand cannot be equilibrated through prices (because of government rent controls) the market will achieve equilibrium through other means. Unfortunately, these means include such unsavory outcomes as discrimination, side payments, under-maintenance, tenant maintenance, finder's fees, conversion to unregulated uses, redirection of investment to other markets, etc.

- Any rent control policy that maintains rents below the free market level also puts tenants' long-term welfare at risk. This is because artificially low rents encourage a locational lock-in effect and reduce the job-search incentives of tenants. This creates adverse effects on the tenant job quality, commute options, income and employment in

[1] Alston, Richard M., J. R. Kearl, and Michael B. Vaughan, "Is There a Consensus Among Economists in the 1990's?" American Economic Review, May 1992, 82, 203–9.

[2] Krugman, Paul, "Reckonings; A Rent Affair" New York Times, June 7, 2000.

[3] Jenkins, Blair (2009). "Rent Control: Do Economists Agree?" https://econjwatch.org/file_download/238/2009-01-jenkins-reach_concl.pdf

the long run.[4] As a Brookings report in 2018 concluded, "*While rent control appears to help current tenants in the short run, in the long run it decreases affordability, fuels gentrification, and creates negative spillovers on the surrounding neighborhood.*"[5]

- The Bill's provisions have features akin to so-called "second generation" rent control policies because they allow upward rent adjustments to a limited degree each year and when tenants vacate a unit. Rent control advocates claim that this approach avoids the more serious distortions of conventional rent ceilings. In fact, as San Francisco's experience with this approach shows, it encourages a higher rate of growth in market rents. This is because, under rent control, a smaller fraction of units are vacant at any point in time to meet market demand. This increases the disparity in rents in the market and discourages turnover of rent-controlled units to new seekers of housing.

- The Bill's essential elimination of "no cause" lease agreements eliminates a voluntary arrangement that confers benefits on *both* the tenant and the landlord, as described by this *FindLaw* citation:

    > *A month by month lease (also referred to as a month-to-month lease) is an arrangement in which the lease may be altered or terminated by either party after giving notice, typically at least 30 days in advance. This type of a lease offers [the tenant] more flexibility since [the tenant] will not have to pay a penalty or lose a deposit if [the tenant} decide[s the tenant] wants to live elsewhere. However, the landlord may raise [the tenant's] rent, change the rental terms, or even evict [the tenant] for any reason, with a similar minimum advance notice.*[6]

- Such lease agreements have evolved over many years to equitably balance the value of the rental agreement to both parties. A bilateral, no cause rental agreement confers a valuable option on the renter since it affords greater mobility and lower costs of terminating the lease than a fixed-term lease. Balancing this is the analogous option that is conferred on the owner to flexibly terminate or change the rental agreement terms on or before the renewal date, or evict the tenant without specific cause.

- To change this balance in a one-sided manner by creating an additional impediment to eviction constitutes a taking of value from the owner if applied to existing such rental agreements. It will incentivize the owner to change new agreement terms or cease leasing the property under these to avoid this taking of value in the future. In the latter case, both parties lose flexibility that the long history of this practice suggests is valuable.

---

[4] See, for example, Krol, R. and S. Svorny (2004), "The effect of rent control on commute times, *Journal of Urban Economics*, vol. 58, issue 3, 421-436.

[5] Diamond, R. (2018). "What does economic evidence tell us about the effects of rent control?", Brookings Institution report, October 28. https://www.brookings.edu/research/what-does-economic-evidence-tell-us-about-the-effects-of-rent-control/

[6] http://realestate.findlaw.com/landlord-tenant-law/what-is-the-difference-between-a-month-by-month-lease-and-a-fixed.html

- There is no evidence that evictions are used excessively in Oregon housing markets, *for any reason*, let alone to simply terminate month-to-month leases. According to data obtained from *Redfin*, the *total* eviction rate for the Portland metro area in 2014 was less than 20 per 1000 rental households. The eviction rate related to termination of month-to-month leases is thus a small fraction of these rates. Among other metro areas with recent, large increases in the median rent to median income, Portland's eviction rate appears to be low-to-average.[7]

- The *Refin* analysis hypothesizes that evictions are amplified in areas that experience rapid increases in the rent-to-income ratio. Although they do not demonstrate this relationship statistically, if true, then the solutions to the no-fault eviction "problem" are policies that reduce the cost pressures on housing—not interference in the pricing or terms of rental agreements.

Conclusions

- If Oregon truly wishes to make rental (and other) housing more affordable, it should reject SB 608 and, instead, revise its land use policies that artificially constrain availability of sites for development of housing.

- If Oregon is truly concerned about fair treatment of tenants and landlords in lease agreements, it should reject SB 608. Oregon should allow renters and landlords to enjoy the mutual benefits such agreements afford both parties. Passage of SB 608 will make both parties worse off in both the short- and long-run. The one-sided loss of landlord rights will stimulate rental rate increases and discourage rental unit supply.

Sincerely yours,

About the Author

This report was authored by Randall Pozdena, President, QuantEcon, Inc., an Oregon-based consultancy. He received his BA in Economics, with Distinction, from Dartmouth College and his PhD in economics from the University of California, Berkeley. Former positions held by the author include professor of economics and finance, senior economist at the Stanford Research Institute (SRI International) and research vice president of the Federal Reserve Bank of San Francisco. He authored the housing economics text, *The Modern Economics of Housing* and has taught housing finance at the UC Berkeley Graduates School of Business and Portland State University. He also has served on numerous State, local, non-profit, and private boards and investment committees. He is a member of the CFA Institute and the Portland Society of Financial Analysts. Contact information: Randall J. Pozdena, PhD, QuantEcon, Inc. , PO Box 280, Manzanita, Oregon 97130; pozdena@quantecon.com

---

[7] https://www.redfin.com/blog/2016/12/millions-of-renters-face-eviction-why-todays-housing-market-is-partially-to-blame.html