

# A case for rent deregulation

**I**T IS TO BE noted that in Finland, following regular market deregulation since 1991, between 1992 and 1996 an estimated 50,000 rented private dwellings came on to the market. This deregulation of rents was motivated by a desire to expand the private rental sector, so that it could become a true alternative to owner-occupation.

Considering Finland's five million population and two million households, compared with Malta's 400,000 population and one-eighth of a million households, Finland's 50,000 extra dwellings would correspond to an additional 3,125 extra dwellings for the Maltese Islands.

The effects of the Maltese housing market due to rent control over the past 60 years since 1939 are well known. These rent controls have been controversial, due to the adverse effects of lower maintenance by owners; longer tenancy rates; vacant properties; higher prices in the uncontrolled sector; and a worsening of the social housing problem.

## Lower maintenance

Landlords reduce the maintenance of their controlled units if unable to offset fully their costs by raising rents. The present measure of increasing the rental amount by 10 per cent of the maintenance incurred is capped by the condition that ultimately the rental value cannot exceed double its original amount.

Thus if rental value is presently Lm40 a year, its greatest increase possible is up to Lm80. This means that over the life of the tenancy maintenance in excess of Lm400 will not be recognised in rental increases. With a reduction in maintenance quality of controlled units falls.

Generally the probability of a unit deteriorating increases with the size of the implied subsidy from rent control. It is to be noted that recently the courts have not acknowledged that the landlord is in duty bound to carry out the repairs. This is due to the landlord not having right of access, but it is the tenant who is in a position to remove any danger.

From the 1995 census of the 33,781 leases, 27,015 units (82 per cent), are leased out for less than Lm100 a year, while 17,343 units (51 per cent), at less than Lm50. Is it here that the bulk of the 7,731 occupied sub-standard and inadequate dwellings are found? This could further be confirmed when noting again from the 1995 census of the 7,731 sub-standard and inadequate occupied dwellings 77.5 per cent are located in the Inner and Outer Harbour Regions.

In these regions four-fifths of all the leases are less than Lm100 per annum and three quarters of all the leases less than Lm50 are found. Tenant maintenance may offset some reduction in landlord maintenance, while tenants with the strongest tastes, may move to the free sector.

Controls influence the supply of housing in the free sector. Although new construction or leases are exempt from rent control regulations, potential investors in rental housing are wary of future controls affecting their units.

This may be noted by the 1995 amendment to the rent law, under which new rental units have been liberalised. The results achieved to date of any investments in the rental markets prove that the public is equally hesitant to invest shortly



MOST of the leases of below Lm50 a year are found in the Inner and Outer Harbour regions

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after removal, anticipating the possibility of future amendments.

To achieve the desired result this rental law has to be entrenched in the Constitution, otherwise it may take years for investors to stop demanding a risk premium, as the rental market would be still considered unsure.

The few investors in rental housing, due to existing restrictions require a risk premium to compensate for this uncertainty, pushing up the rents in the uncontrolled sector. Furthermore owners of rental housing may convert their prop-

erties to alternative uses or prefer to leave them vacant, if they fear future controls.

The number of vacant dwellings at 35,723, being 23 per cent of the total housing stock, divided at 8.4 per cent partially vacant and 14.7 per cent vacant, is one of the world's highest. Vacancy rates in the free property markets tend towards five per cent.

This rate is however, not freely achieved by solely liberalising the market, but also by the imposition of property tax on vacant properties. Of the vacant properties 20 per cent require maintenance of which 55 per cent, i.e., more than half, are located in the Inner and Outer Harbour Regions.

Also 6.5 per cent are in a dilapidated condition, of which again more than half, at 54 per cent, are in the Inner and Outer Harbour regions. This, in the two regions where 75 per cent of rented accommodation is found, reinforces the view that landlords prefer to leave their premises vacant, even falling into disrepair, in the hope that the future may beckon a brighter investment than the present restrictive rental scenario.

The 3,150 additional dwellings mentioned earlier, over an four-year period are equivalent to 800 annually. Most of these would be provided from the existing vacant housing stock.

## Longer tenancy

Rent regulations give security of tenure, thus giving longer tenancies. Some landlords considering their properties as lost if not burdening investments due to the management involved of their estates, being everyday and also death duties.

These long tenancies cause a mismatch of the necessary accommodation area in relation to the household size. No incentive exists for the tenant to shop around to obtain premises suitable for his budget and present-day requirements. He may live in the same house from his birth up to his death, after when a close relative may further inherit the tenancy.

## Higher prices

The higher rental amounts for the affordable property in the uncontrolled market being asked for is noted in the table.

By comparing column 2 with column 4 of the table, the differences existing between the open market value and the capitalised values of affordable properties demonstrates the higher rental amount being asked for in the uncontrolled sector, due to the present restrictions.

From column 7, the present uncontrolled rental amount being requested for a one-bedroomed is calculated at 45 per cent higher, 67 per cent higher for a two-bedroomed and 75 per cent higher for a three-bedroomed.

These increases compare very badly with a study carried out in the US, which concluded that if rent controls were removed, rents in the uncontrolled sector should fall by 15-25 per cent. The present uncontrolled rental market of affordable properties constitutes only 1.5 per cent for one-bedroomed, 0.5 per cent for two-bedroomed and 0.5 per cent for three-bedroomed affordable premises as compared to the total rental market, according to the 1995 census.

This rent to income ratios are to be compared with the two per cent paid out by 82 per cent of total tenants, paying less than Lm100 a year and the 0.75 per cent paid out by 51 per cent of total tenants paying less than Lm50.

Column 5 also shows that Maltese households are paying a

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AFFORDABLE APARTMENT	PRESENT OPEN MARKET VALUE	PRESENT OPEN MONTHLY RENTAL 1939	CAPITAL VALUE AT 4 % OF RENTAL	RENTALS AS % OF MEDIAN HOUSEHOLD EARNINGS	SPATIAL FLOOR AREAS SQM	% INCREASE IN UNCONTROLLED RENTS
1-bed/r	Lm15,500	Lm75 (Lm1.15)	Lm22,500	22	45	45
2-bed/r	Lm19,000	Lm105 (Lm1.85)	Lm31,500	25	75	67
3-bed/r	Lm23,000	Lm135 (Lm2.65)	Lm40,500	32	105	75

# Rent deregulation would improve housing affordability

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high proportion of their median earnings in the uncontrolled rental sector, which varies from 45 per cent up to 75 per cent. This being much higher than what is paid typically in the EU countries varying from 15-30 per cent of household expenditure.

The 1939 rental values in column 3 again give an indication of the present high rental amounts in the uncontrolled rental market. The index of inflation for 1939 is taken at 80 and 600 for the year 2000.

This implies a 750 per cent growth over this period. This gives amended present monthly rental values of Lm8.63, Lm13.88 and Lm19.88, for one-, two- and three-bedroomed premises respectively, well below the present market uncontrolled rentals, also indicated in column 3.

Reducing the present uncontrolled rental values by the percentage increases in table 7, the new monthly rentals become Lm51.75, Lm62.85, and Lm77.15, still substantially higher than the updated 1939 values.

It is true that the index of inflation has not been tracking accurately the rise in the standard of living, together with the capital appreciation of property, especially the land element, which to date has outperformed national growth, together with an improved housing quality, all may explain the difference in above rental values.

## Social effects

As noted, regulation increases the rental amount due in the uncontrolled rental market. This has an effect of further increasing prices in the home-ownership market. As noted elsewhere a worsening housing affordability problem has been with us for a number of years. To alleviate this problem the government over the years has granted housing subsidies to a greater spectrum than just the needy.

This has created a problem, as those most in need are not all being helped. We still have families living in sub-standard conditions, with the system currently failing some of the poorest members of our society. An existing dilemma regarding social housing applicants, is that there appears to be more households below the poverty line than social housing applicants while further not all social housing applicants are below the poverty line.

According to these findings rent deregulation is urgently required. It would improve the condition of our housing stock and improve the affordability of affordable homes.

This by creating a rental market devoid of any restrictions, which is

known to have caused substantial increases in the uncontrolled market, while releasing a high proportion of present vacant premises onto the property market.

This deregulation in turn would lessen the need for Government housing subsidies who in turn can then concentrate on providing social housing to the poorest members of our society.

Instead of rent regulation, regulations should now concentrate on maintaining minimum housing standards, as a dwelling implies a choice of various building disciplines, on which a consumer can make a bad choice.

This would be more in line with

EU housing policy, which tends to subsidise less and switch away from subsidising building to household rental costs.

Housing systems should become more market oriented; and that home ownership should be encouraged but that housing in other tenures should be encouraged to facilitate mobility and flexibility.

On the other hand any resulting housing problems are distinctive and have to relate to economic and social cohesion and alleviated on a regional policy.

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