

Comments on Prosper's "Planning deregulation, housing supply and affordability"

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[Prosper](#) – specifically Jesse Hermans and Emily Sims – have published a thoughtful article on the role of planning restrictions on housing affordability. They generously cite and constructively criticise my research. This note is a response. It overlaps with my earlier note '[Misunderstandings about Planning Restrictions](#)' which discusses related issues in greater length.

Some overall comments

Prosper's article clarifies many areas of agreement. Specifically, there is broad agreement that our cities need to be denser; that high housing prices are unfair and socially harmful; and that increased housing supply reduces the cost of housing.

Disagreements are treated fairly. The paper doesn't knock down straw men. It respects the relevant research and evidence. Overall, this is a constructive attempt to advance the conversation and to narrow some of the points of disagreement. This distinguishes the paper from others with similar conclusions.

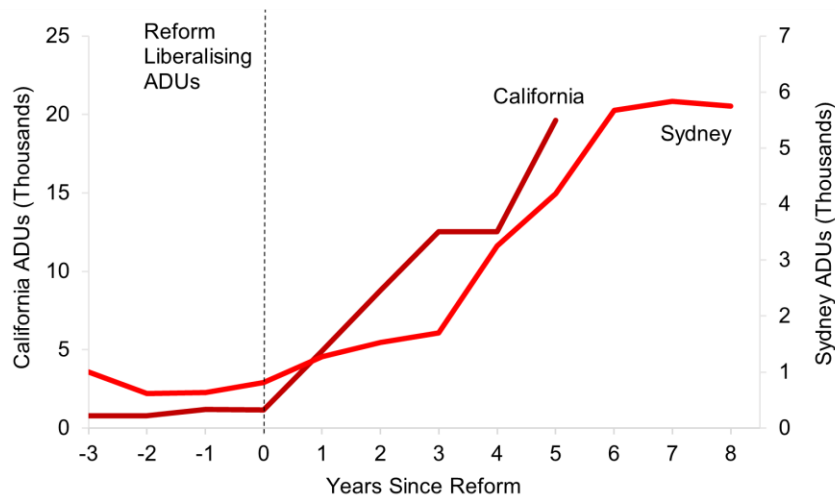
Does planning limit supply?

Prosper's most provocative and important conclusion is that the evidence that planning deregulation would "deliver additional development and increased affordability is weak." In contrast, I would describe this evidence as very strong.

Prosper's conclusion stems from addressing a narrow subset of this evidence which they then criticise. However, the relevant evidence is much wider and more varied.

While a lot of sophisticated research finds zoning restricts supply, this effect is also clear from everyday observation. Some examples:

- The media routinely report rezonings resulting in huge increases in land values. [Prosper](#) or [Cameron Murray](#) also provide examples.
 - Large land revaluations are analogous to the high market value of taxi licences when the supply of taxis was limited. They show that legal permission to build is scarce and valuable.
- A variation on this is the site values or 'residual land value' of apartment buildings. These are commonly quoted within the industry on a per apartment basis, recognising that, with permission to build higher, the land is more valuable.
 - As an aside, the site values compiled and regularly updated by [Knight Frank \(p3\)](#), are broadly similar to the estimates in [Jenner and Tulip](#), as theory would predict.
- Builders, developers and architects complain that they want to provide more housing but they are not allowed.
- In July 2009, NSW removed limits on the construction of granny flats. Construction over the next few years increased about 5-fold. The same thing happened in California more recently. (Source: [Matthew Maltman](#))



- More telling evidence from California is their “[builders remedy](#)”. Due to a peculiarity of the zoning law, zoning restrictions were recently suspended in the city of Santa Monica. In the few days until the loophole was closed, more construction was approved than in the previous two decades.

On top of these simple observations is a mountain of academic research. This finds less building in jurisdictions with tight restrictions; more building when restrictions are eased; prices exceed marginal costs for both detached houses and apartments; substantial economic harm from zoning restrictions; and so on. There are many surveys and summaries of this research; for example Gyourko and Molloy ([2015](#)), Hamilton ([2021](#)), Been ([2018](#)), Furman ([2015](#)), Glaeser and Gyourko ([2018](#)), Schuetz ([2022](#)), Gray ([2022](#)), Erdmann ([2019](#)), Beyer ([2022](#)), Schleicher ([2021](#)) and, for a UK focus, Hilber and Vermeulen ([2015](#), Section 2). They all conclude that zoning restricts supply and this increases prices. The individual papers cited in these surveys typically contain shorter literature reviews with the same message, as do numerous official reports from many different countries. (In Australia, the most recent official reports are the Commonwealth Productivity Commission’s [Report on housing](#), the [Falinski Inquiry](#) and the NSW Government’s White Paper ‘[Rebooting the economy](#)’). The Economist magazine ([2021](#)) has complained that “no one needs any more papers showing that stringent zoning regulations raise housing costs. It is time for solutions.”

The research could be described as “mixed” or “contested” if one gave a substantial weight to badly-designed uninformative studies. However, the surveys above place more weight on research that is robust to criticism. The simple misunderstandings one sees in social media are not taken seriously in the research literature.

Does extra supply lower housing costs?

Most of the evidence above shows that looser zoning increases housing supply. However, the central question is whether it reduces housing costs.

The answer is yes if the demand curve for housing slopes down. Central estimates are that every 1% increase in the housing stock reduces the cost of housing by about 2.5%. I acknowledge that those estimates are not specifically based on variations in zoning, but on a broad range of changes in supply. It is difficult to see why prices might respond differently to zoning changes than to other supply changes and I know of no evidence or even arguments to the contrary. Nevertheless, I acknowledge that this makes the argument indirect and not directly proven. But given how uncontroversial a downward sloping demand curve is, that does not make the evidence “weak”.

At one point Prosper implies that demand for property in central Melbourne is highly elastic but this doesn't seem material to their argument.

Is the research flawed or incomplete?

Prosper give several reasons for doubting the research on zoning – in italics below. My responses are indented:

“the ‘Glaeser and Gyourko’ methodology also captures location premiums... (Phibbs & Gurrán 2021)”

This is a clear and simple misunderstanding of the approach. Location premiums, like any factor that boosts demand, are not an alternative to the zoning effect; they are a complement. High prices reflect the interaction of high demand and inelastic supply. Local amenity will increase the demand to live in a location, but that only makes prices rise sharply if some obstacle like zoning prevents supply from responding. Conversely, zoning would have no effect on prices without location preferences – people would be indifferent about living where the restrictions didn't bind.

“the ‘Glaeser and Gyourko’ methodology produces substantial ‘zoning effects’ in housing data where no zoning regulations exist (Murray 2020).”

Glaeser, Gyourko and subsequent researchers try to compare (as near as is possible) otherwise identical houses that only vary by the size of their block of land. The common finding is that people pay very little for the extra land. Essentially, home buyers pay a lot for the location and little for extra yardage. So a lot of suburban land is wasted. Subdivision (and extra housing supply) would be highly profitable but is prevented by zoning.

In contrast, Cameron Murray finds that land on large agricultural holdings is less expensive than land for small residences near the town centre. He thinks this is the same result as above and hence it that the effect does not depend on zoning. But he is not controlling for other factors. Distant land costs less than central locations but that does not create an incentive for subdivision or increased housing supply.

As an aside, the objections to Cameron Murray's argument have been pointed out to him several times yet he does not address them. That contrasts to the balanced and constructive approach of Prosper.

“There is a lack of robust empirical research to support [the mainstream view] (Freeman & Schultz 2017; Schill 2005).”

Note the dates of these publications. Since then there has been what [Noah Smith](#) calls “A steady drumbeat of new research [that] continues to confirm that building new housing ... makes housing more affordable.” See the dates of the literature surveys above. The assessments of Freeman, Schultz and Schill are no longer true, if they ever were.

Ireland and Spain built lots of houses but their prices rose.

The booms in Ireland and Spain reflected strong demand. Introductory economics says that will raise prices. In contrast, zoning relaxation would represent a shift in the supply curve, lowering prices.

My [‘Misunderstandings about Planning Restrictions’](#) counters further arguments.

The quota vs monopoly models

As Prosper notes, the monopoly model reflects what Stephen Hoskins calls “profit effects” or the effect of planning on directly-affected property, while the quota model reflects “scarcity effects” or the effect on other properties. Modern models of housing (especially calibrated AMM models, like [Hoskins](#)) contain both and we should not see them as competing alternatives. This is not a conceptual disagreement. Of course, there is an empirical question as to which is more important, which much of the research mentioned earlier tries to answer. The standard answer is that removal of restrictions raises the price of the directly-affected land, though not of directly-affected floorspace. Furthermore, it increases supply, so reduces the price of other properties, assuming no externalities. The effect on land prices is ambiguous however floorspace will be less expensive.

Prosper’s description of the monopoly model (the “profit effect”) may confuse some readers. Although individual land owners have a monopoly over their own plot of land, their pricing power is minimal. Different dwellings are highly substitutable, so similar houses near each other sell at about the same price. If extra housing is supplied in one segment of the housing market, prices fall throughout the market.

A related issue is Prosper’s emphasis that land prices reflect the highest and best use of a site, which often will not change when other properties are rezoned. It would be more precise to say that land prices reflect THE VALUE OF the highest and best use. While the physical use of a property might be unaffected by what happens elsewhere, the price will fall if inexpensive substitutes become available.

Other

I agree with Prosper that Auckland provides a clear, simple and powerful test case. The effects of recent reforms are unfolding, so whatever we say now will soon be out of date. Nevertheless, data through late 2022 show that the liberalisation of planning was followed by a boom in higher density construction and lower housing costs relative to what is likely to have happened otherwise. The most up-to-date analysis I am aware of is [Matthew Maltman’s](#).

In terms of policy implications, Prosper’s main objective is to increase and broaden rates of land tax. Most economists support this. However, it is a separate issue from planning restrictions. Pro-housing advocates and Georgists both dislike land rent. The pro-housing advocates want to reduce it; Georgists want to tax it. There is no reason why we can’t do both.