

A tale of two systems –

The change of Norwegian housing policy from quantitative regulations to support of a free housing market.

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Abstract

The objective of housing policy is to influence the housing conditions.

The macroeconomic policy and development has been the main factor behind the successful housing investment development. Housing investment has mainly been financed through the Norwegian State Housing Bank. A low-interest policy with substantial tax reliefs for housing has strongly stimulated housing investment and made it possible for households with ordinary incomes to afford good quality housing. At the same time a rational allocation of building resources was achieved through strict cost, size and quality control. By 1980 a fairly balanced housing situation was achieved and the pressure for liberalizing housing and finance markets was increasing.

During the 1980-ies deregulation of housing and finance policies took place and free trading in the housing and credit markets was established. Generous access to reasonable loans created booms in the housing market. Housing policy has been directed towards specific social needs. Housing and building legislation have been modernized to support the performance of free housing markets.

The paper tries to compare the outcome of this “two systems” on:

- Stability and change in house prices and construction activity levels*
- Housing quality and costs*
- Distribution of housing*
- Supply of social housing*

1.The issue – long-term experiences of different housing policy systems

Long-term experiences of housing policy and financial systems have appeared as important issues in the light of financial crises and general economic recession. Housing policy in Norway has been characterised broadly as previously strictly regulated and in later years as rather liberal - a tale of two systems. The post-war period in Norway housing policy has been frequently discussed from this dualistic point of view often based on the personal political view of the discussants – “the housing policy was much better before” or “a free market is the

best approach”. The reality may be a bit more intricate to sort out, but simplifications are necessary to trace and utilize some experiences and draw some conclusions. The analytical challenge is to sort out some fruitful simplifications that can add to our understanding of housing development in general and specific challenges of housing policy in particular.

The housing, building and financial sectors in Norway have throughout the post-war period been principally private but regulated and stimulated by the public sector. In the immediate post-war period up to around 1980 housing investment, interest and prices were subsidized and regulated. These regulations were in order to achieve the official goal of decent and affordable housing for all. By 1980 the housing conditions were greatly improved due to large programmes of housing investments. At the same time the political pressure for liberalizing the financial and housing markets had been growing and with a liberal-conservative government in power from 1981, important deregulations in the housing and the financial sectors took place. Since then quite some experiences have been gained. Thus the time has come to try to summarize some comparative lessons learned and relate to present housing policy issues.

The principal criteria to assess these lessons can be the general housing policy goal which has prevailed throughout the post-war period and across all political parties, the present version being “Good and secure housing for all”.

At present the implementation of this goal is related to the principle of enabling an efficient housing market supported with social and environmental policy measures.

This general goal and the two main policy post-war policy approaches can be tested against some classical economic criteria that are operational in relation to assess design and implementation of housing policy:

- Allocation of resources to housing
- Stability in prices, investment and production of housing,
- Quality of housing,
- Social distribution of housing
- Supply of social housing.

These criteria relate to present discussions of housing policy in Norway, but appear throughout the whole post-war period as important criteria and still can work for design and testing of new policy measures. The discussion in this paper tries to follow this approach.

2. An economic - political approach to housing development and policy

The development of housing in Norway after WWII must be seen in the perspective of the overall economic and social policy. The emphasis on full employment, growth and a fair distribution has been decisive for social development in general and not least for the housing conditions. Household income growth and a fairly equal income distribution has been the foundation for a good housing development.

Within this favourable economic setting the basic point of departure for understanding the development of housing is the volume, composition, quality and social distribution of housing investments. Long-time housing investments accumulate to the housing stock which defines the housing conditions and, in the market sense, the basis for housing supply. Thus, it is important to understand how economic policy in general and housing policy in particular influence housing investment.

In Norway a politically determined and centrally planned approach to housing investment was implemented after WWII. Housing investment was given high priority in the overall reconstruction of the economy. Specific targets and 4-year programmes were formulated and a detailed macro-financial budget was decided every year. Specialized government investment banks were given priority in this national financial budget. Housing investments were to a large extent financed by the Norwegian State Housing Bank. This Housing Bank provided full mortgage financing of new housing including subsidized top loans. The loans were eligible for all people, rich or poor, but the main bulk of the loans were given to younger families and housing cooperatives. The housing projects had to fulfil fairly strict regulations regarding costs, size and lay-out. The municipalities had the task to provide new, developed land for this national housing investment programme based on cost-pricing of land. However, the project -investment initiative was left to households, housing cooperatives and private developers with the aim of owner-occupancy as the main tenure form.

In general, up to 1975-80 cost pricing of land, construction as well as trading and renting of houses was the basic principle and implemented through law and regulations. Distribution of housing was dependent on membership time, waiting lists, and social attributes. By time and inflation this cost-price system developed a gap between legal prices and ability to pay causing shadow transactions in the housing markets. In the 1980es an abolition of the principle of cost-pricing and transition to free trading of land and housing was evident, also as much as financial markets were deregulated at the same time.

A very important aspect in all the post - war years has been that taxation of housing has been very favourable to owner occupancy, creating a significant distortion in the financial, housing, land and construction markets as well as increasing social inequality. Fortunately the main bulk of housing investments was allocated through the state bank system, notably the Housing Bank.

This macro-economic approach to housing shaped the Norwegian housing conditions up to the 1980es.

It represented a mix of strict central economic governance and private initiative that provided fairly stable conditions in the construction sector, control of resource allocation and a reasonable social distribution.

From the 1980es and until today a general market approach has been the main strategy to housing production, allocation and distribution.

This implies that economic factors and especially the price of housing play a decisive role in housing production, allocation and distribution. The households can more directly choose a preferred housing situation regarding location, type, and size of housing, within their economic capacity related to income and wealth. Thus the housing conditions for the individual and for society have become even more dependent on a fair distribution of income

and wealth. This appears as the most important challenge both to general economic and social policy as well as to housing policy maintaining the goal of good and secure housing for all.

A very specific element in the development in the later years is the wide spread accumulation of significant housing capital, mainly in the form of equity in owner occupied housing. This is caused by tremendous increase in house prices since the early 1990es. This development was fuelled by low interest rates and abundant flow of capital as well as very relaxed taxation. This accumulation of housing equity has fuelled a further housing inflation as the older owner occupiers can bid for housing with substantial equity in addition to their loan capacities through recurrent income and at present, at extremely low interest rates. This is definitely not a sustainable development, especially not for the less advantaged. What can and should be done regarding economic and social policy and particularly in the housing sector?

And what can and should be done by the technocrats being bureaucrats or experts or housing researchers to help the politicians?

The ambition to trace factors influencing housing development, and particularly to identify the influences of housing policy systems and instruments is difficult to achieve. Different methods may to be applied in order to reach practical conclusions. The statistical – econometric approach has been a main method in Norway not least because of the influence of the late professors Ragnar Frisch, Tryggve Haavelmo and Leif Johansen at the Department of Economics at the University of Oslo, and the practical implementation of macroeconomic models at Statistics Norway.

This tradition was followed up in the 1980es by a housing market model developed by Asbjørn Rødseth, now professor at the University of Oslo, in cooperation with housing researcher Rolf Barlindhaug at the then Norwegian Building Research Institute. Quite a number of simulations and projections were carried out by applying this model in relation to the annual national budgeting carried out in cooperation between the Ministry of Finance, the Housing and Building Department in the Ministry of Local Government and the Norwegian Building Research Institute. In the later years quite some economic and social housing research have been carried out, especially focussing on social, environmental and administrative topics, but with less emphasis on macroeconomic aspects

But just as important may be the experiences of long-time housing bureaucrats formulating housing policy measures and implementation on behalf of the politicians. A kind of housing programming approach based on the classical stock-flow models of housing need assessments was the back-bone. This programming was related to the national economic policy to consolidate financial programmes for housing investment. The policy was presented for political approval in Government white papers and the annual budgets and 4 year programmes. In 1999 a government committee was appointed to review all main aspects of housing policy. It came out in 2002 with a solid report, applying housing research as well as current experiences and presenting some policy proposals. However, the report got little political backing and hardly touched critical macro-economic issues, even if there was a good chapter on housing taxation. In 2004 a follow-up Government white paper was praising the mechanism of well functioning housing markets, and avoiding inherent problems in this difficult market. The priority was given to homelessness, but with little financial support. In the later years the Government has emphasized poverty issues as an important aspect of housing policy and has decided to expand the financing of the housing allowance system. The current financial crisis has also caused some expansion in the government budget for

social housing investment grants. But quite some housing challenges remain to be answered by the government, especially as the Auditor General has raised quite some critical questions and the housing organisations and the public in general appears confused. The present financial and general economic crisis has also left some critical questions to be answered in relation to housing. May be a new white paper should be presented by the Government, based among other sources on recent housing research?

3 A tale of two systems – from direct regulations to support of a free housing market

Systems and periods - of path dependence

The end of WWII marked in Norway as in many other countries the introduction of a new era in policies in general and not least in the field of housing policy. Long lasting institutions and instruments were introduced and firmly established. A development of path dependence was started. Still today many of the post-war institutions are alive and functioning, some quite reformed, and a few new ones have emerged. This development can be interpreted in different ways; slow and hesitant adaption to new challenges or durability and efficient management to meet new challenges. Or as one senior bureaucrat once said: No changes without a real crisis, or as a version of Newton`s second (?) law; an external power is necessary to change public institutions???. Thus the time may have come for reforms in housing policy, at least the leaders of important countries and institutions have emphasized the need for regulatory reform both internationally and on national levels.

The experiences of Norwegian housing policies can be summarised in the following power-point graph: The crisis in the 1930es caused a new way of thinking with Keynes as the most famous proponent. Also in Norway we became Keynesians and to some extent still are. The ideas was developing during the time of WWII and in 1945 a new approach to housing policy was presented by the majority based Labour Government. New institutions were created, the most important being the Norwegian State Housing Bank and the Government`s Housing Directorate as a kind of a department in a Ministry. Further on an office for building research was established, later turned into the Norwegian Building Research Institute. These institutions together formed an effective troika for supporting good housing for ordinary people, and they succeeded.

By 1965 it was obvious that Norway had to face the housing needs of the large post-war baby-boom and new programmes for massive construction of houses were obvious to all parties. On base of the Swedish approach to municipal housing programmes, such programmes were introduced in a simplified form to Norwegian municipalities. It became an important instrument in implementing an ambitious housing program, it could in Swedish terms be called the ½ million program. During the 1970es more than 400 000 new dwellings were built and by 1980 the housing stock was in reasonable balance with the housing needs. This was fortunate as the financial imbalances created during the 1970es the situation was ripe for the deregulations of the housing market that was carried out by the conservative-liberal government that came into power in 1981.

These deregulations were coming along with deregulations of the financial markets. The timing and administration of these reforms were a new experience for Norwegian politicians and authorities and quite some mistakes were done. An illuminating example was that the loan to value ratio on the housing stock was quite low and created the potential for heavy credit expansion, at low interest rates. The expansion was inevitable and the government counteracted with high interest rates. A crisis developed in both the housing and the financial

market. Banks had to be rescued by the government and payment problems appeared in the housing sector. Municipalities experienced substantial losses on investments in infrastructure. The Housing Bank rescued the building industry by providing reasonable loans for new housing.

Since the middle of the 1990s the development has been more stable until the recent boom started in 2004 fuelled by exceptional low interest rates. This year is characterised so far by a substantial fall in new housing starts, and an increase in unemployment towards a doubling of recent levels. What will be the effect on housing demand remains to see.

In short the experiences of the 1980s appear forgotten and governments are panicking to save financial institutions and keep cheap money flowing to save jobs. As indicated by quite some economists the problem may be more long term and structural. Immense financial imbalances has been developing internationally, most visible is the imbalances between China and the western world. Cheap products from China are substituting domestic production in a wide range of countries. The production costs notably labour wages in China are so low that even at low prices China is accumulating huge quantities of international capital for further expansion abroad. Maybe a substantial wage increase in China would be the best way to improve international price balances as well as increasing the living standards in China.

Tenure forms

Both the housing and the building sectors have all the time been traditionally privately organised and owned. However, after WWII the establishment of the housing cooperative movement introduced a viable alternative to traditional private commercial rental housing as well as traditional municipal housing. As housing developers the housing cooperatives were given priority both by the local and the central authorities with access to reasonable land, mortgage loans as well as subsidies through the Housing Bank. In this way a full housing investment package was made available to local initiatives forming cooperatives in most cities and neighbouring municipalities. Thus new urban housing after WWII was dominated by this new tenure form accessible for everyone to become member. The members had to provide some housing equity to access a house or flat, in the size of 15- 25 pct of total investment cost or around the size of an ordinary annual income. The establishment of condominium type of housing was prohibited by law until the 1980-es. From the 1980es and onwards the trading of houses and flats including cooperative housing have been open to free bidding on price. This is mainly trading between owner-occupiers that occupy almost 80 pct. of all housing.

The rental sector, some 20 pct of housing stock, has become a temporary form of housing especially for young people, students and temporary workers. A substantial part of rental housing is letting of additional small flats in low-rise housing occupied by owner-occupiers. A more profitable tenure form is developing within condominiums where investors buy flats for letting earning both high rents and increase in value.

Municipal social housing which constitute some 4 pct of all housing, appears to develop into more segregated housing earmarked for vulnerable groups. This according to the philosophy that ordinary household manages without occupying public housing.

The cost pricing - an important principle in housing policy that by the end of the 1970-es had to be abolished.

An important part of the post-war policies to achieve affordability was that the households should only pay the initial investment costs and recurrent costs. The owners of a house or a dwelling should not earn a large profit on the house whether it was land lease, rental housing

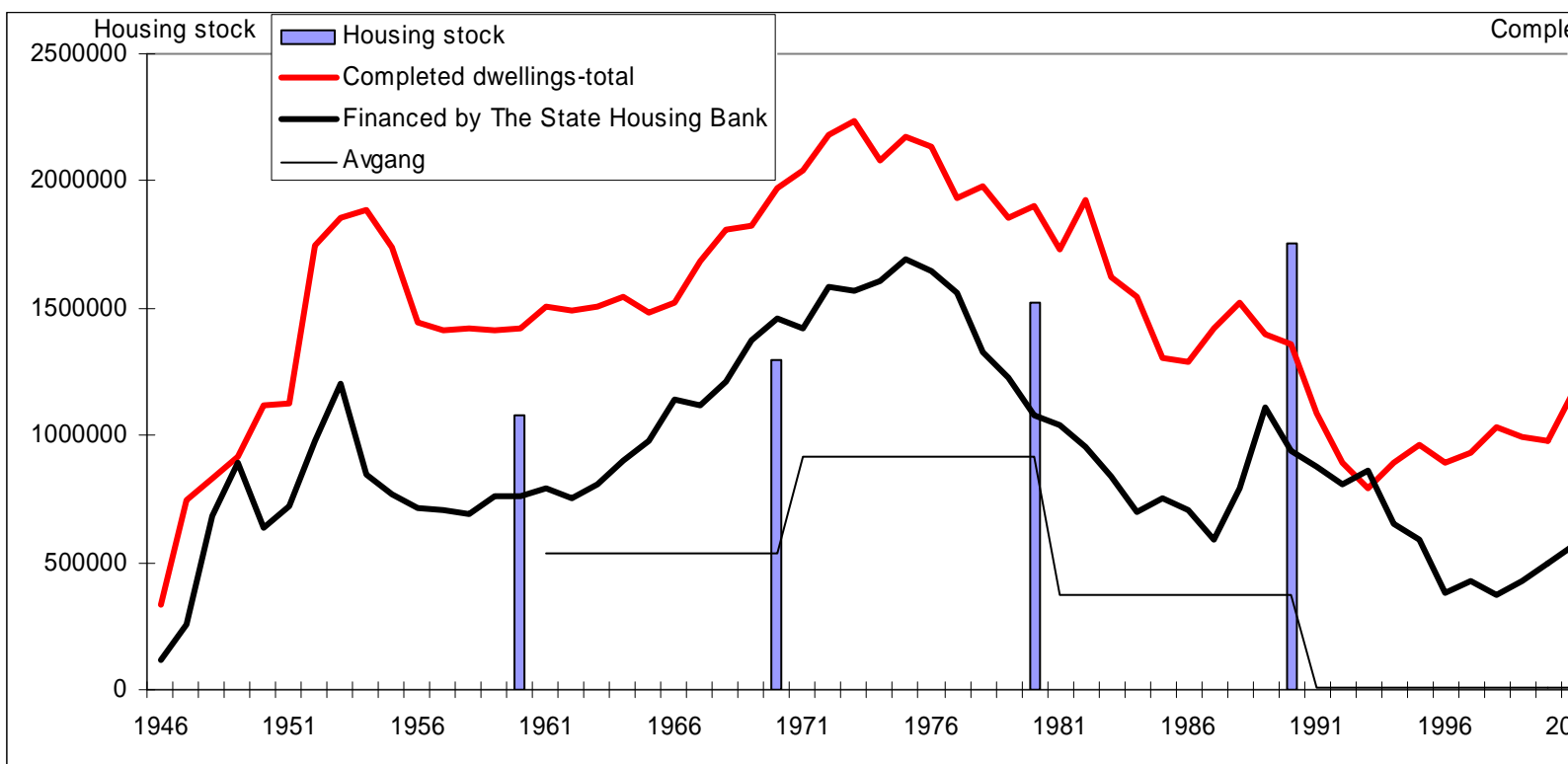
or sales price. With increasing building and land costs this was by time difficult to achieve and shadow transactions omitting price regulations were increasing. And most price regulations were abolished during the 1980es.

However, the last reminiscence of direct price regulation, rent regulation in older parts of the bigger cities will be abolished by 2010.

The main achievements of housing policy in terms of quantities ia appearing in the graph 1 sowing the volume of housing stock, volume of new housing as well as the volume of new housing financed by the Housing Bank

The withdrawal of housing units from the stock is also calculated, most of it substandard or with remote location.

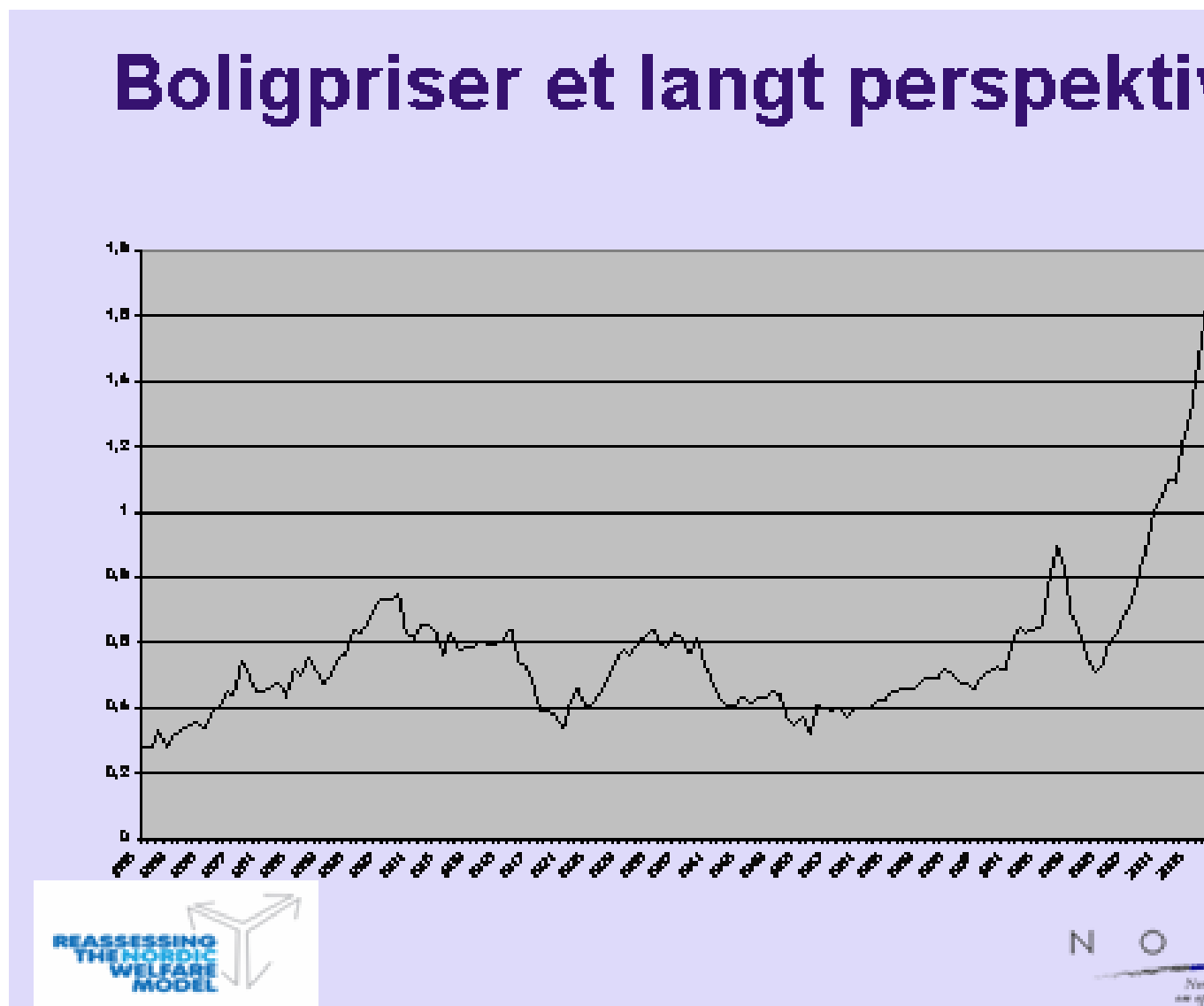
The figure also reveals the decline of the importance of the Housing Bank in the later years.



With free pricing in the housing markets the public interest has been focussing on house price development and less on quantities. Every month price statistics are published and

every increase has been welcomed as positive by the public and the industry, as price decreases has been seen as sign of a recession.

Figure 2 Housing price development



The figure reveals the large housing prices in the later years and thus the accumulation of housing equity by the owner occupiers as well as those landlords letting rental housing.

Many factors have contributed to this unique housing price development, notably income increases, but clearly interest development and lack of proper taxation.

4. Some comparative conclusions.

Stability in housing prices, investments and production

The structure of the building and housing sectors with a long-term- immobile object – the house – makes the sector very vulnerable to waves, bubbles and even crash. Stability based on

regulation. This because the total supply- availability- of housing is at any time the present stock of housing which can be utilized in different ways, thus coping for the actual demand. Thus the price of housing is very vulnerable to the fact that the total demand being less or more than the stock. Low demand creates low housing prices and low investment activity. The demand is dependent upon a wide range of factors, but demographic factors including urbanization, business cycles and employment, interest rates. The basic political issue is stabilization of the macro economy in general through financial and fiscal policies as well as more or less regulations. With a regulated national economy and a regulated housing and building sector it was obviously possible to carry out stabilization policies. With the deregulation of trade and finance the small and specialised economy of Norway became more vulnerable to international business cycles and globalization. With the national free financial and housing markets, the danger of waves and bubbles has increased, as was experienced both in the 1980es and in the last years.

The liberalization contributed to drastic increase and decrease in building volumes both construction of new buildings and modernization of the stock, , Employment has been characterised by recruiting temporary labour from abroad, which has now turned unemployed,

A clear decrease in productivity at the same time wage increases causing tremendous cost increases.

House price variations and differentiation according to location and special features

Less stability, more variation in size and standards,

Pricing according to business cycles and location. Intense densification, less size and more costly

The new low-interest policy with few restrictions adds to consumer spending, but not so much to rational housing investment Prices are not stable enough for long-term investment.

Social distribution

In the longer perspective housing in a free market will be distributed according to income and wealth. This is clear evidence from history and across nations.

Not least will accumulated housing and property equity stimulate further inequality in housing conditions.

More segregation seems to appear stimulated by concentration of municipal housing for the few and needy

Taxation subsidies of housing, a strong stimulus to inequality as well as waste, underutilization of land and housing and lack of infrastructure and environmental investments

The market tends to resist Quality problems, size, design, energy saving access-universal design

Owner occupancy based on accumulation of housing/property accumulation of equity. Distribution of housing has become more dependent on income and wealth and less on legitimate needs.

Change of attitudes – from decent pricing to land grabbing.

During the first 20-30 years after WWII there was a general attitude among the both the professionals and the public that housing should be reasonably priced according to costs, only adding for general inflation as measured by the consumer price index- CPI . With the heavy inflation in the 1970es the gap between original cost pricing and present values was becoming so large that more and more people were omitting the price regulations in different ways and principles of pricing of land was changed from value in use to alternative value.

With the deregulation policies in the beginning of the 1980es maximization of land and house prices were becoming legitimate and during the housing boom in the later years maximization of prices by bidding freely on prices was a fully accepted method. With the strong price increases on good locations fortunate land acquisition was the key to good profits, not to say fortunes. This was happening with hardly any comments from the professionals, the public and the politicians. When it was suggested that developers could finance some social infrastructure in connection with larger development projects, this was prohibited by a legal decision of the parliament. And general taxation of this location rent has been kept low all the time.

5. The present and the future – some challenges and proposals

Norwegian housing policy is based on the assumption of well functioning housing markets, as well as land markets, construction markets and finance markets. Social aspects of housing shall be solved by housing policy.

Norway has gained some long-term experiences in long term housing development, most of them can be termed quite successful and some less. This development is due to many factors of historical character. Many of these can be classified as good luck but combined with conscious and determined policies not least in the economic and social fields. A basic value of equality in rights and living conditions may have important in this connection. The housing conditions have been central in the development of these general living conditions. The present housing situation is created on long term accumulation A target of housing capital stimulated by a conscious economic and social policy This development has been supported by a conscious and target oriented policy combined housing economic policy and housing policy and development.

The stability challenge: Presently the world and to some extent also Norway is experiencing a business cycle slump with quite serious impacts on the housing, construction and finance sectors as well as general employment and income. A challenge mainly towards the general economic policy and in particular the financial- credit market policies.. With an extremely open and specialized economy economic stability in Norway can be almost impossible to achieve. International coordination and cooperation is required to stabilize international trade and finance. . Unfortunately great structural international imbalances have developed over many years. The great fluctuations in supply and interest rates influence directly the housing and construction markets and create great instability in house prices and employment in the construction sector.

The distribution challenge: The social challenge: Good and safe housing conditions for all in a good and sustainable environment.

Housing conditions are vulnerable to inequalities in personal abilities and resources, income and wealth.

A reasonable equality in income and wealth is a basic requirement to achieve good housing conditions.. The free market may in the long run not fulfill this requirement. Thus economic and social policy is necessary supplemented by a good housing policy. This is our experience and what about the future?

. However the structural long-term challenges are and will continue to be greater. The general income and distribution problems may increase as well as environmental non-sustainability.

The housing supply challenge.

The housing market will not automatically provide sufficient relevant housing. Even if the market works well it will have to supply housing according to effective demand i.e. the relevant housing has to be specified and paid for. For quite substantial groups this will be difficult to achieve. The most obvious example is to provide good housing for low-income elderly and handicapped people with little housing capital. The support of this type of housing has been a tradition in Norwegian housing policy. With an increasing number of elderly people and other groups the challenge will remain. Quite a lot of elderly people have however accumulated a substantial housing equity that can be channeled into relevant housing- if so wanted. Many elderly people are hesitant to take such action and even relatives may be hesitant. An important point here is a mix of financial incentives- including taxation reforms and tempting subsidies. See point on affordability and financing below

But a main point is that the appropriate even attractive housing alternatives must appear on the ground and with the preferred location and at reasonable prices.

This is a clear challenge both to the central government, the Housing Bank, the municipalities, the housing cooperative movement and the building industry.

The quality and cost challenge

The quality and cost issues have with the boom in the housing and building markets, appeared frequently in the media as well as the journals. Particularly has the lack of control of quality in planning and building processes been an issue. This relates to the follow –up of the intentions and regulations in the current Planning and Building Act. IThe law was based on internal systems of quality control in planning and building companies. During the boom the capacity and competence to execute control was variable and quite a

Professional institutions and companies.

To cope both with general market preferences as well as special social requirements

Professional housing industry-with professional developers and a professional building and real estate industry.The supply of good and reasonable housing for all groups of society- the homeless, elderly and handicapped people. The young generations with no or little housing capital. Low-income groups in general, one –parent families, singles.

In particular the provision of good social housing avoiding segregation and concentration of vulnerable groups. The integration of vulnerable people in the ordinary housing stock. The

legislation on housing cooperatives and condominiums provides legal access for the municipalities and related organizations to buy

Good rental housing provided by professional landlords.

The affordability and finance challenge

Prices and costs have increased tremendously during the later years, driven by finance expansion at reasonable interests and increasing incomes in combination with low productivity development.

Price increases have especially been triggered by location preferences especially prices of new houses with very central location. In some case the total costs of land, infrastructure and construction has gone beyond the market even at highly attractive locations (Fornebu close to Oslo).

The central government and the building industry have been concerned and have supported a 5-year R & D program on construction productivity and costs. During a boom situation it has not been easy to trace effects of the program on the actual development in the market. Further industrialization of Norwegian construction appears difficult to achieve. And according to industry representatives productivity on site has decreased and costs have escalated. How can this challenge be met?

With an apparent recession in pipeline, construction volumes have gone down, for example housing starts have decreased some 30 pct.

Stabilization of investment activities through the public licensing of oil investments

Licensing of building starts. This was a central part of housing and building policy up to the 1980es. There is still a law that authorises the government to take measures if the problems in the construction sector becomes to

Substituting private disinvestment with public investments Portfolios of public investments that can be put into work at short notice.

Improved taxation of real property - a green location tax.

A reform is highly needed in the taxation of housing and other property in Norway. The present system is not a system but inherited from historical circumstances and short-sighted political considerations. Reforms have been recommended by government committees up through the years, but in vain,

Some municipalities are struggling to introduce and improve property taxation, but with little support from central authorities. The need for infrastructure investments has caused more interest property taxation as a source of finance.

Improved information and competence in the building and property sector

Prohibiting short-term speculative housing projects by introducing new regulations.

Better land use planning and building control by new legislation and guidelines.

