

REGULATIONS ARE THE MAIN CAUSE OF INADEQUATE HOUSING SUPPLY AND RISING RENTS IN TEXAS

KEVIN ERDMANN

Senior Affiliated Scholar, Mercatus Center at George Mason University

Texas Senate Committee on Local Government

September 13, 2022

Chair Bettencourt and members of the Senate Committee on Local Government, thank you for the opportunity to speak with you today. I am Kevin Erdmann, a senior affiliated scholar at the Mercatus Center at George Mason University. My research focuses on the effects of land use restrictions, and my work on the topic includes the 2019 book *Shut Out* and the recent book *Building from the Ground Up*.¹

In today's testimony I offer these main takeaways:

1. All paths to create new housing face obstructions—some new, some long-standing.
2. Some of these barriers to expanding the housing stock arise from federal policy and cannot be affected by state policymakers.
3. At all levels of government, permissiveness in housing regulation is vital. Permissiveness in housing regulation ensures that houses are available for everyone. It is the only way to stop the relentless rise in rents, and it will preempt an increase in homelessness.

HOW NEW HOUSING IS CREATED

New housing can be created through several avenues:

- *Developers can build large apartment complexes.* These complexes are an important element for cities transitioning into exciting urban hubs capable of expanding useful mass transit systems and bustling central residential areas. Many cities have created years' worth of regulatory hoops for such projects to

1. Kevin Erdmann, *Shut Out: How a Housing Shortage Caused the Great Recession and Crippled Our Economy* (Lanham, MD: Rowman and Littlefield, 2019); Kevin Erdmann, *Building from the Ground Up: Reclaiming the American Housing Boom* (New York: PostHill Press, 2022).

jump through and frequently are able to stop projects outright at the discretion of individual policymakers.²

- Families or small-scale landlords can build structures such as duplexes or backyard units (also referred to as accessory dwelling units).³ This housing can fill niche needs within individual neighborhoods. The extra rental income they generate can help working-class homeowners make their mortgage payments. They can give elderly parents or young adults semiprivate living options. These types of housing fill countless needs, but they are simply illegal in most neighborhoods because of zoning regulations that are common across the country.
- *Families can buy single-family homes.* This is the housing type most favored by zoning regulations. But since 2007, new lending standards regulated by the Consumer Financial Protection Bureau and by underwriters at the federal mortgage agencies (the Federal Housing Administration, Fannie Mae, and Freddie Mac) have prevented millions of families from buying new homes.⁴ Homeownership rates peaked in 2004, and because of these new lending standards, homeownership rates for all working-age age groups are still lower than they had ever been before 2004 going back to 1982, when the Census Bureau began annually tracking homeownership.⁵
- *Developers can build single-family homes to rent to families.* This housing type was unusual in the past, but it is becoming more common because, owing to the difficulty families have today qualifying for mortgages under the new tight lending standards, many families who want to live in single-family neighborhoods can do so only by renting. This type of housing has only recently started to grow, but because of fears about both the corporate owners and their renter tenants, municipalities in some places have started to limit or ban it.⁶

HOW OBSTRUCTIONS ON BUILDING NEW HOUSING AFFECT HOUSING COSTS IN TEXAS

These obstructions have increased housing costs the across country, including in Texas. According to Zillow, the median rent in the United States has risen by more than 5 percent annually since 2014, and this has been true in many Texas cities too. Even worse, the lack of new supply creates a bidding war for the homes that exist. That 5 percent average increase is not evenly distributed. In Texas’s largest metro areas, rents have risen annually by about 4.5 percent in neighborhoods where the average annual income is \$100,000, but they have risen more than 6.0 percent in neighborhoods where the average annual income is \$35,000.⁷ That adds up to a 20 percent cumulative additional increase in rents since 2014 in the neighborhoods that can least afford it. This is not a coincidence; it is the predictable result of an inadequate supply of new housing.⁸

2. Leah Waters and Francesca D’Annunzio, “Mesquite Has Rejected Affordable Housing for Nine Years. This Week, the City Said No Again,” *Dallas Morning News*, June 28, 2022; Sandra Sadek, “Update: Grapevine City Council Denies Proposed 475-Unit Multifamily Development Near Mall,” *Community Impact*, May 18, 2021.

3. Emily Hamilton and Salim Furth, “Allowing Missing Middle Development Would Contribute to Housing Affordability in Nebraska” (Testimony before the Nebraska Legislature Urban Affairs Committee, Mercatus Center at George Mason University, Arlington, VA, February 4, 2020).

4. Antonio Weiss and Karen Dynan, “Housing Finance Reform: Access and Affordability in Focus,” *Treasury Department* (blog), *Medium*, October 26, 2016.

5. Census Bureau, “Table 12. Annual Estimates of the Housing Inventory by Age of Householder 1982 Present” (dataset), accessed September 9, 2022, <https://www.census.gov/housing/hvs/data/histtabs.html>.

6. Heather Middleton, “No Renters: Clayton County Board of Commissioners Eliminates Builders’ Ability to Rent, Lease New Homes,” *Clayton News Daily*, April 12, 2021.

7. Zillow, “ZORI (Smoothed): All Homes Plus Multifamily Time Series (\$)” (dataset), accessed September 9, 2022, <https://www.zillow.com/research/data/>; “SOI Tax Stats—Individual Income Tax Statistics—ZIP Code Data (SOI),” Internal Revenue Service, last updated September 7, 2022, <https://www.irs.gov/statistics/soi-tax-stats-individual-income-tax-statistics-zip-code-data-soi>.

8. Kevin Erdmann, “Rising Home Prices Are Mostly from Rising Rents” (Mercatus Special Study, Mercatus Center at George Mason University, Arlington, VA, August 2022); Kevin Erdmann, “Build More Houses: How an Incorrect Perception of Housing

The decade-long depression in construction has caused rents to rise the most for low-income individuals, who can least afford it because they naturally have the fewest alternatives. When *everyone* has more choices, people with more income do not have to poach the housing choices of those who have less. The rising tide truly lifts all (house)boats.

It might be hard to imagine how building more homes in middle-income and affluent neighborhoods can help make homes in poorer neighborhoods more affordable. Maybe it is easier to think about it from the other direction. When there are not enough new homes in middle-income and affluent neighborhoods, the homes that were formerly occupied by less affluent families become costlier. The millions of families (usually with lower incomes) moving out of housing-deprived places such as coastal California because of rising rents for many years were victims of this problem. The past decade, during which housing production has been low across the country, has provided researchers with an unfortunate national experiment to confirm the problem.⁹

HOW TO FIX THIS

Some significant obstructions are not within the power of Texas policymakers to change. Much of the decline in entry-level single-family home building since 2008 is likely due to federal mortgage regulations. And the significant increase in the demand for housing in Texas is likely due to residents of states like California being driven out of their native states and pulled into Texas in search of affordable housing.

Where Texas policymakers can control these obstructions, permissiveness will yield better results for Texas residents. Cities need to be able to accommodate changing needs. Both large-scale and small-scale apartment developments and accessory dwelling units are a part of that solution. And where the final stopgap source of new housing is now growing, which might finally settle these rising rents—new large-scale single-family home developments for rent—I strongly urge you to refrain from adding obstructions and to prevent localities from adding them as well.¹⁰ Families that the federal government considers unqualified for a mortgage need homes, and if all types of new construction that can provide those homes face some sort of legal injunction, then the government is effectively legislating homelessness, even if it is dressed up as an imposition on corporations and developers.

The problems of cost and access have many solutions that do not involve public spending and frequently simply require government getting out of the way.

Where the cost of new homes is high, consider the many unnecessary contributors to that cost that can easily be removed (Houston has been an exemplar in this way):¹¹

Supply Fueled the Great Recession and Slowed Recovery” (Mercatus Research, Mercatus Center at George Mason University, Arlington, VA, April 2021).

9. Some research into the local processes that facilitate or block affordability include the following: Quentin Brummet and Davin Reed, “The Effects of Gentrification on the Well-Being and Opportunity of Original Resident Adults and Children” (FRB of Philadelphia Working Paper No. 19-30, Federal Reserve Bank of Philadelphia, Philadelphia, PA, July 2019); Evan Mast, “JUE Insight: The Effect of New Market-Rate Housing Construction on the Low-Income Housing Market,” *Journal of Urban Economics* (forthcoming): 103383; Liyu Liu, Douglas A. McManus, and Elias Yannopoulos, “Geographic and Temporal Variation in Housing Filtering Rates,” *Regional Science and Urban Economics* 93 (2022): 103758; David Card, Jesse Rothstein, and Moises Yi, “Location, Location, Location” (CES Working Paper No. CES 21-32, Census Bureau, Washington, DC, October 2021), 41.

10. Salim Furth, “Build-to-Rent Housing Bans: A Case of Zoning Overreach” (Mercatus Policy Brief, Mercatus Center at George Mason University, Arlington, VA, August 2022).

11. Salim Furth and Emily Hamilton, “Cities and States to Watch in 2019,” *The Bridge*, January 11, 2019.

- Are there parking mandates?
- Are there rules about minimum lot sizes?
- Are there delays in permits and inspections?
- Are there height limits, unit size minimums, or arbitrary aesthetic requirements?

Where rents are rising, consider why renters lack alternatives:

- What percentage of urban land outright bans apartments, backyard units, and other housing types?
- Are there bans on manufactured homes?
- Are there ordinances against living arrangements like unrelated roommates?

If some new types of owners or property uses seem a nuisance, consider why they are being chosen over the alternatives:

- If municipalities are bothered by the growth of short-term rentals such as AirBnB, then they should remove the barriers to new hotels.
- If municipalities are bothered by corporate-owned build-to-rent neighborhoods, then they should remove the barriers to more apartments, more duplexes and triplexes, and more homeowners.
- If existing residents of poor neighborhoods are being priced out by gentrification, then policymakers should remove the barriers to building new neighborhoods or new dense luxury high-rise apartments.

After years of accumulation, individual rules meant to obstruct home building on the margins have added up to obstruction on the whole. They say when you're in a hole, the first thing to do is to stop digging. To get home builders to pick up their literal shovels once again, rule makers first need to put their proverbial shovels down.