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## Introduction

*Tony O'Sullivan & Kenneth Gibb*

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From its very beginnings as a discipline for the study of society, economists have sought to apply economics to real world issues. While the roots of housing economics can be traced back to the work of the original classical and neoclassical pioneers of economic theory, it did not emerge as a separate and recognised area in its own right until very late in the day. After World War II economists, particularly in Europe, turned their attentions to a number of pressing issues of social policy, leading to the emergence of bodies of work on the economics of poverty, transport, education, and health. Applying the insights of welfare economics and emerging theoretical and practical developments, this work sought to address various efficiency and equity issues as they related to the everyday lives of millions of people as citizens and consumers. Not in the vanguard of this work, interest in housing as a proper area for study in the UK began to develop in a serious way from the 1970s onwards. Duncan Maclellan has from the first been prominent in contributing to and promoting this. The idea behind this book was a wish on the part of many contributors to the field to recognise his contributions.

### **Perspectives on theory**

Housing is a difficult thing to theorise about. An inherently complex commodity, with spatial fixity a defining characteristic, and asset, investment and consumption dimensions to account for, the economics of housing remains a challenge to those who seek equity and efficiency improvements for society to this day. It is a field of inquiry where, in Joan Robinson's terms, thinking in 'theory time' is a poor substitute for recognising the role of real, non-abstract, historical time. Moreover, abstracting from the spatial aspects of housing leads, to quote Maclellan, to a curious form of 'pointless economics'. Good theory necessarily involves jettisoning many of the

assumptions usually made in neoclassical economics, rendering the work more difficult and 'messy'.

Early contributions from Maclennan drew on the insights of the Austrian school, and the work of such authors as Hayeck and Von Mises. The insights produced by the Austrians concerning information, knowledge, ignorance and time are central to his work on housing search and choice (Maclennan 1982). For Maclennan, information problems are central features of the housing market, as are spatial externalities, and transactions costs associated with mobility. In such a world, neo-institutional economics (Oliver Williamson 1975, 1985), evolutionary economics and disequilibrium analysis are often the natural modes of analysis to adopt in order better to understand housing phenomena.

Demand for 'housing' in the real world necessarily embodies demand for place, for access to public and private services, and reflects the fact that housing is in part at least a 'positional good' (Hirsch 1976). Maclennan built these factors into his work from the outset, and recognised the implications for the spatial structure of housing markets. Consequently, space and place feature prominently throughout Maclennan's work, both as a key friction for understanding the complexity of housing and its impact on household and market behaviour.

Maclennan has investigated the implications of space at several different housing market scales. An enduring concern has been examining the process of neighbourhood change, within which neighbourhoods are defined as relatively open residential production and consumption spaces. Maclennan has sought throughout his career to apply useful economic models to the problem of interest. One such example at the neighbourhood scale has been his attempt to capture house price change in unimproved properties after nearby properties have received grant aid to improve their fabric, thus measuring the neighbourhood externality (Maclennan 1993b). More generally, in collaboration with American colleagues (Grigsby *et al.* 1987), he helped develop a comprehensive framework for deciphering neighbourhood change.

At the urban or metropolitan scale, Maclennan has both examined spatial aspects explicitly through the early exploration of the concept of housing sub-markets (and the associated concept of 'product groups') and used the urban level of analysis as the implicit or explicit focus for microeconomic models of tenure choice, search and housing choice (often in collaboration with Gavin Wood) (Wood & Maclennan 1982; Maclennan & Wood 1982a). In his 1982 text, Maclennan went a long way to establish a richer conception of housing choice, rooted in real time decision-making, search and bidding

behaviour, the active role of institutions and a more appropriate notion of equilibrium initially developed by Frank Hahn, where market equilibrium is based on learning of information by economic actors.

Information, time and space matter as much for supply and its appropriate conceptualisation as they do for demand. Again, Maclennan made it clear from the outset that the reductionist approach of neoclassical theory was particularly inappropriate to many of the tasks at hand. He showed that noise in the market, and uncertainty about the nature and meaning of market 'signals' result in endemic inefficiency and market failure (Maclennan 1982). These insights remain to be built upon.

Defining the product 'housing' is a basic issue in the conceptualisation of housing demand, supply, and the housing 'market'. Equally fundamental is getting an adequate handle on the concept of the 'price' of housing. Over time hedonic analysis has become the approach of choice for most economists, but it has some quite fundamental limitations. These certainly do not invalidate the use of this technique, but they do indicate the need to be careful in its application. Maclennan, who has used the technique frequently in his work, provided an early and cogent summary of these limitations (Maclennan 1977b).

A specific issue relating to the price of housing is that of housing subsidies – their definition, measurement and impacts (not to mention their rationale). Often these take the form of tax concessions. Considerable work in this area has occurred in the last 20 years, following early critique of the efficiency and equity effects of such subsidies (in the UK context see for example Robinson 1981; Maclennan & Wood 1982b; Maclennan & O'Sullivan 1987; O'Sullivan 1984, 1987). Much subsidisation of housing, however, particularly in a European context, has been tied into direct provision through public or social housing. This has raised issues not just about the welfare implications of the pricing of housing, but the comparative efficiency of public versus private provision. On pricing *per se* a considerable literature has developed, to which Maclennan has contributed (Atkinson & King 1980; Grey *et al.* 1981; Ermisch 1984; Hills 1991, 2000; Maclennan 1986b). On the question of public versus private provision, traditionally non-market providers of housing have operated through bureaucratic hierarchies, providing a rich opportunity to apply Coasian transactions costs concepts and insights from the wider work of Oliver Williamson to the specifics of organisational efficiency in public housing. Maclennan contributed to such analysis in the late 1980s in considering the comparative efficiency of different housing providers in the UK (Centre for Housing Research 1989).

While the microeconomics of housing has developed apace over the last two decades, attention has also been given to modelling at the regional and macro scale. At the national scale of analysis, housing in the UK (as elsewhere) was transformed in the 1980s by a process of financial deregulation. Collaborative work by Maclennan with Geoff Meen, John Muellbauer, Mark Stephens and others identified many of the connections between housing and the macro-economy and helped forge a bridge between housing specialists and those macroeconomists coming to the housing sector for the first time. This also helped policy makers who needed to understand the micro-foundations of mortgage market change, housing equity withdrawal, house price volatility and their transmission mechanisms into consumption, indebtedness and the labour market (Maclennan *et al.* 1997).

## **Policy and practice**

Much of the interest in housing economics that has developed over the last two decades has emerged on the back of considerable intervention in housing by central and municipal government. Policy makers of all political hues, especially but not exclusively in Europe, have seen it as desirable if not essential to intervene in, regulate, suspend, replace or compete with various aspects of the housing market. Maclennan has been particularly active in seeking to influence policy, especially, but not exclusively, in a UK context. In doing this, being based at the University of Glasgow for most of his professional working life is not the only link between Maclennan and the classical economists. In his conception of policy there is much to link Maclennan's approach to the classical school.

From the first, any failure to distinguish technical from ideological positions in policy analysis has been rejected as at best sloppy intellectualism and at worst sharp practice. This does not imply however that he has promoted a narrow 'technical' interpretation of the economist's role in policy formulation; on the contrary he has been a constant advocate of a broader 'political economy' interpretation of the role. Moreover, the use of assumptions regarding the operation of housing (and wider economic) systems to progress an argument, where the basis should be the results of applied research, has usually been given short shrift. In this regard, Maclennan has been very aware of the relatively poor base provided for applied research by official statistics and has indeed been a stern critic of government.

In 2001 Maclennan was involved in redesigning the Right to Buy (RTB) in Scotland as an element of what was to become the Housing Act (Scotland)

2001. Starting from an examination of the available evidence he commented:

'The RTB has been a source of enduring controversy over the two decades since its introduction. Views on policy proposals can diverge for at least three different reasons. First, individuals or organisations may have different ethical or political views about an issue and facts or evidence may have little relevance in resolving such differences. Secondly, many policy decisions involve changes with complex, long-term effects on the economy and society. Individuals with the same values may reach different conclusions because their model or analysis of impacts differs from each other. Again this requires judgement in choices, but it also requires the participants in a debate to be clear and consistent in their analyses. Finally, even with the same ethical values and analytical approaches, individuals may reach different conclusions if they have different facts or evidence at hand.'

(Maclennan *et al.* 2000, p. 1)

These views echo those expressed in his 1982 text (which, coincidentally, used the then very new RTB issue to illustrate the point).

Maclennan has consistently rebuked both economists and critics from other disciplines who have sought to interpret or represent the role of the economist in policy discourse as being focused on competitive housing markets, the use of deductive partial or general equilibrium models, or to be unthinkingly centred on Pareto-based social welfare functions. For him,

'... it is not enough to restrict the role of the political economist to accurately describing market behaviour for policy makers - although such action may be an improvement on proffering advice largely based on deductive reasoning and assumption. Instead, applied economic analysis of policy (or political economy) requires the analysis of a more detailed set of questions. For instance the analyst must enquire as to what are the objectives of government, what role housing policy plays in attaining such objectives, who actually makes housing policy, what economic and political constraints restrict action, what advice and information exists and what model of the housing system is used by policy makers? These questions are not to be viewed as minor concerns for applied economists. Economists may deduce conditions for optimality or second best conditions for the design of housing policies *ad infinitum* but unless they understand how economic analysis and research is absorbed and transformed by the policy

process they run the risk of having their work, at best, ignored or, at worst, misused.'

(Maclennan 1982, p. 142)

Policy influence, then, must start from an understanding of the institutional, administrative and legal contexts from which policies emerge. Ethical positions on policy issues are acceptable (indeed unavoidable) but should be explicit and honest. Value judgement should not be dressed up as technical issue, and ignorance on empirical matters of importance must be acknowledged and must constitute the soil to be tilled by the applied researcher. This view of the policy role is demanding above all else of honesty, and for this reason is brutally demanding in application.

While Maclennan has been clear from the start of his career that governments can quite legitimately hold to non-Paretian objectives, he has also been steadfast that these objectives must be capable of clear operational interpretation. This in Maclennan's eyes is perhaps the key part of the bargain policy makers have to deliver, for the policy-making process to have any hope of working to the benefit of the citizen – the impact on whom always remains the focus of Maclennan's work. In his writings but even more so in direct dealings with senior government administrators, ministers and politicians, he has delivered this message in an uncompromising way. Given this, other issues can be largely worked around – recognising there is plenty to be so worked.

For a start, the structure of government and the distribution of policy responsibility across different tiers and geographies of government make the achievement of coherent policy intrinsically difficult. Joined-up government is a popular current slogan, but also a desideratum recommended by Maclennan over 20 years ago – with due recognition of the inertia built into the existing system, and the consequent need for an institutional economics perspective on the problem. Writing in the UK policy context he noted:

{The} complex organisational model for housing policy in Britain would not necessarily be inadequate if some centrally determined operational principles for policy existed such as market pricing or income/wealth related subsidy systems. But where policy, as in Britain, lacks a central organising principle then the distribution of subsidy reflects neither house type nor household characteristics but is an outcome of chance, history and in particular of tenure selected. Thus, whilst it has been argued that housing market intervention may be rational and required, it is difficult to believe that the present system could not be improved or it may even

be that the imperfect market system that the policy is designed to circumvent would perform more effectively as an agent of allocation and redistribution. However it is probably not possible to answer this question in the UK because, as in most fields of policy in the country, there is often more concern with the level than the quality of public expenditure.'

(Maclennan 1982, p. 167)

In his 1982 text, he categorised housing policy into a number of different types of successively greater generality. These were:

- Removing specific market failures through taxation, subsidisation, or regulatory action
- Replacing fundamentally unfixable market with administered allocation mechanisms
- Using housing as primary vehicle for achieving non-allocational ends, such as income redistribution, or regional growth.

His subsequent work has demonstrated that simple or pat conclusions on the relative attractiveness of state versus market-based policy solutions, while endemic in policy debate, invariably miss the point. In local markets, for example, it is not clear that public monopoly provision would be in any way superior to a private sector version. In a sense the policy question of interest to Maclennan has always been not whether housing (and regional economic) outcomes can be optimised by state intervention or forbearance, but whether, working in a real world context, market failure or state failure constitute the least bad means to achieve clearly articulated ends. To answer this question, he made an early plea for what has come to be widely referred to as 'evidence based policy'.

Starting in his 1982 text, Maclennan made a point that has continually recurred in his work: that there is a need for a co-ordinated provision of market and non-market information to drive market allocation decisions, and to inform public action. The absence of this information base resourced (if not necessarily discharged) as a function of government has, he has argued, led to poor investment planning in the private as well as the public sector. In a public policy context, the consequences are as follows:

'In this context for policy formulation, there are two alternatives at least for formulating strategies. First, ministers ... will listen to the arguments of pressure groups and interested parties. Power, in this case, not to the

people, but to the groups with organisation and capital to present the most convincing (not the best) case. Alternatively, ministers with an inner circle of policy advisors may form a view as to what is appropriate policy. These views may be based either simply on ideologies or on a limited or even partially researched view of the housing system.'

[Maclennan 1982, pp. 168-9]

Part of the problem as he saw it was the absence of appropriate training for those engaged in policy making and implementation, from the strategic to matters of detailed operation. He certainly demonstrated the personal courage of this conviction, in one instance telling an audience of around 500 not-for-profit housing practitioners that in his opinion they couldn't strategically plan their way out of a paper bag! More constructively, his view has been expressed as follows:

'It must be of some concern within central government that many officials responsible for policy have no initial familiarity with housing and that, within the British Civil Service, transfer often follows mature acquisition of insight. Similar comments ... apply within local authorities and the lack of formal training within public housing management is now the cause of some concern ...'

[Maclennan 1982, p. 168]

This in part has led to the establishment of major programmes of housing training at Glasgow University from the early 1980s onwards, integrating theory, policy and practice. These covered both the needs of housing management and development practitioners through to the tutelage of civil servants and local authority officials at a postgraduate level.

Maclennan was heavily critical of policy reflected in key pieces of housing legislation in the late 1970s and early 1980s [Maclennan 1982]. He saw it as a professional responsibility on him and fellow economists to present government with usable models, methods and material that can improve the quality of public policy. His subsequent career has been geared to the dispensation of this responsibility at the national and international level. His success in this regard is perhaps best reflected in the pivotal design role he played in the development of the Housing Scotland Act 2001, which gave him the opportunity, albeit in a purely Scottish context, to influence the structure of the Right to Buy, of which he was so critical in 1982.

## Contributions to this book

The contributors to this volume have all had the opportunity and pleasure of working with Duncan MacLennan at some time in their careers. Each of the chapters picks up on an area of interest to him over the last 20 years. Collectively, these chapters cover much of the landscape of housing economics and housing policy.

### *Urban housing models*

The chapter by Kenneth Gibb assesses the different types of urban housing models that have been developed. Gibb considers the role the 'standard' access-space approach has played as the starting point for analysis of urban housing in much of the literature. The chapter makes a case for more extensive use of filtering research in the future investigation of urban housing systems. It also looks at the latest generation of urban simulation models, in particular those associated with Anas and Arnott, and presents a simplified metropolitan model of Greater Glasgow developed by Gibb, Meen & Mackay (2000).

More fundamentally however, Gibb argues that the evolution of these different types of model has failed to address many of the concerns voiced by MacLennan (and subsequently reiterated e.g. MacLennan & Gibb 1994). It is not that these models fail to give useful insights, but that by and large their strengths and weaknesses remain as profiled two decades ago. While filtering models perhaps as noted have a greater potential for providing insights than they have so far delivered, the whole field would benefit from new thinking. The future development of spatial models of the housing market will need to incorporate adjustment and disequilibrium on both sides of the market, information imperfections, reflect the importance of real time and process in market evolution, and capture the key role of housing market institutions in a way that can be sensibly operationalised. This is a formidable challenge.

### *Segmentation, adjustment and disequilibrium*

Urban housing markets are generally thought of as segmented in one or more dimensions. This can be in product group terms, or in terms of quality hierarchies, where the key distinction is made in order to classify the market into sub-markets involving dwellings that are more or less substitutable as far as consumers are concerned. In her chapter, Yong Tu provides an analysis of the causes and consequences of housing market segmentation. Using the well-

known conceptualisation of housing as a composite commodity, she defines sub-markets in terms of underlying attribute prices. A given attribute has a constant hedonic price within a sub-market but across sub-markets it will vary. One important implication of the analysis of segmentation Yong Tu provides is that disequilibrium is likely to be the norm. She examines the properties of such disequilibrium in the housing market.

Turning to the thorny problem of identifying housing sub-markets in practice, Yong Tu evaluates the main alternative methods and concludes that there is nothing that intrinsically distinguishes one as superior to another. Of more significance, her analysis suggests that urban house price indices should be constructed at sub-market level, and is again strongly persuasive that disequilibrium should be explicitly factored into analysis of urban housing. Yong Tu also argues that a disaggregated framework is the proper basis for analysing the local neighbourhood impacts of urban and housing policies.

### *Transactions costs*

John Quigley's chapter deals with the question of transactions costs and their significance for the housing market. Apart from the costs of search, consumers must deal with legal negotiations and bargain with other parties. In addition, because choice is infrequent and information or knowledge of the housing market decays, costs linked to uncertainty and expectations are important (if inherently difficult to measure). His chapter sets out a taxonomy of these costs and reviews the empirical literature on their individual magnitudes. He reports, for example, that the average costs of negotiating and legal transactions in the US housing market vary from 6% to 12 % of house value. However, these costs may be relatively small in comparison to moving and psychic (adjustment) costs. Quigley presents a simple model based on consumers making move/stay decisions by comparing the discounted utility gains forgone by not moving with the discounted transactions costs that a move will incur. This, he suggests, gives an alternative basis for measuring the magnitude of transaction costs facing households to deriving this information through survey work.

Quigley also considers whether transactions costs in the housing market involve significant costs for the wider economy, and whether policies can be developed to lessen any such costs. Although Quigley acknowledges some limited theoretical support for Oswald's contention that reduced owner-occupier mobility is the source of higher associated unemployment among

homeowners in different OECD countries (Oswald 1997b, 1999) (where debt constraints, such as negative equity, effectively act as arbitrarily high transactions costs inhibiting mobility), he finds no credible empirical evidence that home ownership causes high unemployment. Quigley argues that government should act to reduce transactions costs in the housing market, however, facilitating flows of information, and in the development of standards that can make transactions simpler.

### *Hedonic pricing models*

Stephen Malpezzi reviews research on one of the most important tools in housing economics: hedonic price models. There is a voluminous literature concerned with house price index construction and a smaller field of work examining the underlying demand for individual attributes. In his chapter, Malpezzi provides a clear exposition of the fundamental conceptual and empirical issues often ignored when undertaking applied work in this area. In particular, he considers the functional form problem (there is no obvious *a priori* functional form to adopt and the one chosen is usually on the basis of convenience alone). Malpezzi reviews the econometric issues associated with identification, mis-specification, non-robustness of co-efficients, non-linearity and disequilibrium tendencies.

Malpezzi provides an overview of the main applications of hedonic analysis in housing and identifies areas that would repay further study. He draws on Maclennan's (1977b) work to suggest, given the continuing dependence of housing economics on this class of model, that hedonic models should *de minimis* possess three features: their use in any specific application should have a firm theoretical basis; their specification should be complete and if not the practical consequences should be fully explored; and, perhaps most critically, the design of a pricing model should be fit for its intended purpose. These recommendations are pertinent to a literature that is too often consumed by a sterile battle between protagonists of different index schools, the performance of which are not always strictly comparable.

### *Housing in the macroeconomy*

In his chapter, Geoff Meen surveys the relationship between housing markets and the macro-economy. Meen organises his review around five themes: the relationship between house prices and consumer expenditure; the effect of housing on the labour market nationally and regionally; national differences in housing markets and their consequences for EMU; the contribution

of housing to economic cycles; and possible links between housing and the spatial concentration of business start-ups.

He calls into question the feasibility of house price prediction, house price being the key variable linking housing to the macroeconomy, and moves on to investigate the implications of unpredictability and to suggest a different basis for housing market analysis starting from the bottom up, recognising that local markets cannot be treated as if they are all effectively the same. Meen examines the scope for using complexity theory as a basis for simulating local housing markets, characterised by heterogeneous agents, non-linear outcomes (such as 'tipping') and multiple equilibria (including prolonged disequilibria). Meen argues that tipping and thresholds are important processes underpinning neighbourhood housing market change from decline through normalcy to gentrification. While arguing that the reductionist neo-classical models may well be inappropriate for many aspects of housing economics research, however, he does point out that they continue to have relevance under specific circumstances and that 'a slavish attitude to any approach is rarely likely to be optimal'.

### *Taxation, subsidies and housing markets*

Gavin Wood examines taxation as one of a set of frictions that impact on the efficiency of housing market outcomes, as well as having important distributional consequences. His chapter demonstrates the regressive and often counter-intuitive effects of housing taxation. He then uses tax arbitrage models to analyse tenure choice. His literature review and subsequent analysis of the distributional incidence of taxation on housing shows that, while the user cost effects of housing taxation may be well known, the systematic variations in landlord user costs associated with differential tax treatment are less well known or studied despite their importance for rental investment. In the discussion of tax-induced efficiency distortions, Wood makes a case for rental housing supply segmentation arising from 'clientèle effects'. Furthermore, there are 'lock-in' effects associated with this segmentation because capital gains taxation is rarely levied on an accruals basis.

Wood goes on to review the literature on the size of the welfare loss associated with taxation expenditures for home ownership, assessing the proposition that tax-induced housing investment (often in second-hand housing) may have crowded out industrial or 'productive' capital. He finds the evidence to be conflicting, suggesting that housing investment generates both positive and negative externalities in the wider economy.

### *The economics of social housing*

In her chapter, Christine Whitehead applies economic principles to another question of considerable policy importance: what is the rationale for social housing? Whitehead concentrates on three issues: the efficiency rationale for government intervention, the role of housing as a method of redistribution, and the insights that economic theory can provide into appropriate governance structures for housing provision and management.

Whitehead shows that housing is subject to a significant number of market failures, and that their impact is, on the balance of evidence available, probably large enough to matter; but that it is far less obvious that social investment in housing will necessarily solve the problems these failures create. The political case for the provision of social housing has usually been made in terms of the efficacy of housing as a direct means of redistribution. Whitehead shows that the relative merits of income versus supply subsidies for achieving distributional objectives are less obvious in the case of housing than many assume, and that the most appropriate way to achieve distributional objectives comes down to empirical answers to questions regarding the relative importance of market failures in the context of specific economies and housing markets.

Moreover, the possibility of state failure must also be factored into any analysis of the appropriate response to market failure, or assessment of the form of intervention needed to achieve an agreed distributional objective. What is required in a housing context is a proper evaluation of governance issues. As Whitehead notes, in reality, any governance system is imperfect. It is therefore a matter of analysing the different attributes of market, regulatory and administrative systems in particular social, political and market contexts to determine the least-cost approach. Whitehead concludes in the UK context at least that in the future there should be less emphasis on social housing *per se* and more on managing markets, ensuring adequate investment and enabling different types of providers (public, non-profit and private) to compete on cost and quality.

### *Neighbourhood dynamics*

In his chapter, George Galster considers the notion of 'neighbourhood' from an economic perspective. Defining neighbourhoods as bundles of spatially-based attributes (including such things as class profile, tax/public service levels, demographic profile and the political activity characteristics of residents as well as property-based characteristics), Galster shows that

neighbourhoods have a number of important features. These are that attributes vary in their durability and ability to be priced, that they are valued in a relativistic (cross-neighbourhood) way by consumers and that the spatially-based attributes comprising neighbourhood can change by the very act of consuming them. Galster shows the implication of these features to be that the costs and benefits associated with consuming a neighbourhood largely originate externally to the consumer in question.

Galster presents neighbourhoods as dynamic and subject to constant change, and at the same time highly risky for potential consumers and investors. He conceives urban neighbourhoods as being situated within a broader segmented housing market, with change at the neighbourhood level driven fundamentally by external shocks transmitted across the market. Once initiated by such a shock, within-neighbourhood micro processes that can be represented through complexity models embodying non-linear threshold effects ensue. Galster argues the intrinsic nature of neighbourhoods is such that they are not likely to produce socially efficient outcomes. Moreover, because neighbourhoods are valued in a relativistic way, poorly conceived policy might have zero sum effects. On the other hand he points out careful targeting can be highly effective in assisting neighbourhoods on the cusp of catastrophic decline.

### *Home ownership and constraints to tenure choice*

Joc Gyourko looks at the determinants of access to owner occupation in the US. Until quite recently, permanent income and the relative cost of owning versus renting were thought to be the dominant factors. Gyourko reviews recent theoretical and empirical work that shows it is net worth and asset price that drives the transition from renting to owning. This view of the world implies that attempts to improve access to owner occupation through policies aimed at reducing payment to income ratios are misconceived. Leaving aside the question of whether such an objective is in fact appropriate, Gyourko shows that reducing the required down-payment on purchase should be considered the more effective policy instrument.

Gyourko goes on to consider the implications of this new view for explaining racial differences in US home ownership rates, and finds that these can be eliminated once household wealth is properly controlled for. Properly controlling for wealth in this context means allowing for racial differences in intergenerational wealth transfers between parents and children, as well as accounting for a household's own net worth. Because of these differences in wealth, black households are far less likely than their white counterparts

to apply for a mortgage, and Gyourko reports evidence that shows this is far more significant than discrimination in the mortgage market in explaining ownership differentials.

Gyourko also considers trends in the affordability of ownership in the US since the 1970s. Rather positive conclusions on this can be derived from a prominent national interest rate-based index measuring housing costs to the median income household purchasing the median home. In contrast, he presents evidence showing that affordability conditions have varied across the income distribution, with low-income households having fared badly. This finding reinforces the significance of Gyourko's conclusions regarding the relevant budget constraint facing households who are seeking to become owner-occupiers.

### *Planning regulation and housing supply*

In his chapter, Glen Bramley discusses housing supply. While supply is clearly of central importance to housing economics and the operation of housing markets (as well as more generally), Bramley points out that it typically receives much less attention than demand, and suggests this might derive from the difficulty of applying deductive modelling to this subject.

Bramley reviews past economic research on new housing supply, and discusses the operation of land use regulation in Britain, which he contrasts with systems in other countries. While land use regulation is likely to affect the supply of land for new housing development, land and house prices and housing densities, the scale of these effects and their welfare interpretation is not certain. Bramley concentrates on the measurement issues and employs a panel model to analyse the impact of the amount and type of available land on new housing supply and house prices in England. The data are organised spatially on the basis of 90 'zones' constructed as simple aggregations of local authority districts and Bramley builds a straightforward supply and demand system, on the basis of which he concludes the price elasticity of new build supply is low in Britain, and may be getting lower.

Bramley also finds low land price elasticities and draws a number of conclusions of policy significance from his model. These include that land availability through planning is a strong driver of development, that greater land supply reduces house prices to a modest extent only, and that emphasis through the planning system on residential development on urban and recycled land carries a significant output penalty.

### *Housing planning*

In his chapter, Tony O'Sullivan looks at local housing planning in the UK. There has long been a presumption in the UK that such planning is necessary (and the chapter by Galster supports this conclusion), and that municipal government is the appropriate agency to carry it out. Having considered the case for such planning, O'Sullivan looks at what it is expected to achieve, and compares this with what it has actually delivered. Housing planning and the related land use planning that occur in the UK are shown to be almost entirely devoid of economic content.

O'Sullivan details the areas where it is reasonable to expect economics to play a role in housing planning as conceived in the UK and contrasts this with the economic tools actually available. However, he points out that even with better tools a major gap between requirements and reality might be expected to remain unless incentives structures between and within levels of government are adjusted. He concludes that housing planning *per se* is needed, and that the American apathy towards such planning is not a better approach. However, the emphasis should be on the process of planning, and plans produced should be seen as contingent on unknown and currently unknowable future events.

### *The Right to Buy*

The final three chapters in this book look explicitly at different aspects of the relationship between research and academics on the one hand, and government and policy development on the other. The chapter by Williams looks at the Right to Buy in the UK, a policy under which local authorities have been required to sell rental stock at a substantial discount to market value. Right to Buy has been the most significant and contentious housing policy in the UK in the last 20 years. Williams shows that between the introduction of the Right to Buy in 1980 and the end of the century there was little connection between research and policy development. It was introduced to increase owner occupation, pure and simple, not to address any specific equity or efficiency issues in the UK housing system. Key restrictions on sale under Right to Buy were adopted at the outset on the basis of skilful political lobbying, not hard evidence of a problem to be addressed. Meanwhile, subsequent evidence on the negative and unintended effects of Right to Buy was largely ignored.

Academic (and housing professional) reaction to Right to Buy was largely hostile, and Williams argues this too was at least in part ideological rather than evidence-based. While much research has now been done, key research into the local effects of Right to Buy, called for as early as 1981, still remains to be undertaken. Williams considers recent developments in Scotland where the establishment of the Scottish Parliament in 1999, with housing as a devolved function, have provided an opportunity for more rational arrangements for the Right to Buy to be established. In 2001 a Housing Act was passed that significantly amended the terms under which Right to Buy can be exercised in Scotland. He shows how these amendments were based for the first time on serious examination of the available research evidence. Whether or not the revisions to Right to Buy lead to better efficiency and equity outcomes in the Scottish context remains to be seen. The more general light Williams' chapter throws on the relationship between academics and policy makers also raises many interesting questions.

### *The political economy of housing research*

Donnison and Stephens address some of these questions in their chapter. They consider the scale and scope of housing research undertaken over time, in the context of changes in the political and academic environments for such research. In doing this, they are able to identify some of the main factors responsible for shaping the evolution of housing research in Britain. They situate housing research clearly in the time-specific cultural, political and economic circumstances of the countries in which it takes place, but argue that over time academics have faced increasing competition as a source of knowledge for policy makers, and greater difficulty in disseminating their findings to the wider public. Reminding academic colleagues 'who think of themselves as analysts of housing problems and policies, that they are applied social scientists for whom their own profession is also a proper subject for study', Donnison and Stephens argue 'the comparative advantages remaining to academics are their opportunities – and obligations – to gain a broad understanding of the workings of their society, and to speak uncensored truth to power and to the public at large'.

### *Policy and academia*

The final chapter comes at the relationship between academics and policy makers from a completely different direction. For Best, the issue is one of how to maximise the relevance and impact of research findings on policy development. He acknowledges the tensions that exist between academics

and policy makers, but sees them as in something of a symbiotic relationship. Sometimes academics take a direct and active part in the development of policy, even to the extent of taking up active political roles. Best outlines the pros and cons of these situations, and considers some of the personal qualities needed to make this transition successfully. He goes on to discuss how research undertaken by those who do not wish to take an active political role feeds into policy development and sees this as being determined by four factors: who pays for the research (and what their motive is); how it is presented; the timing of research findings; and the persistence with which they are presented to policy makers. Best makes the case that the skills needed to bring research to bear on policy making are not the same as those necessary to do the research in the first place, and raises the question of strategic alliances with intermediate agencies that specialise in driving research into policy development. As such agencies are thin on the ground, he suggests an alternative might be to promote the development of specialist units within universities to carry out the task.

## **Recurrent themes and key issues for the future**

The contributions to this book cover a very broad range of issues in theory, policy and practice. In terms of the contributions MacLennan has made to housing and urban economics, one can identify a number of common themes that recur across chapters.

One relates to the fitness-for-purpose that models of housing markets exhibit. Malpezzi points out that fitness-for-purpose is a fundamental criterion in deciding which method to use in the construction of a house price index. Simple frictionless neoclassical models are neither right nor wrong, and to try and categorise them as such would be to miss the point. For some purposes, as Gibb, Galster, and Quigley show, they are extremely valuable. But for much housing market analysis there is a need to accept that many of the assumptions made in the development of such models actually dispense with the real problems of interest. The chapters by Yong Tu and Quigley, Galster, Meen and Bramley, in different ways, testify to this.

A second relates to the issue of state versus market failure, and choice of the 'least worst' policy option in any given context. The chapter by Whitehead deals explicitly with this issue, but in essence, this is an issue underlying the chapters by O'Sullivan, Galster and Meen. If neighbourhoods are socially inefficient and there is a concern with the local equity effects of housing consumption and production, what should be done about it? Is there a case for state-led planning, or will the outcome be no better, or even worse than

that which the market will deliver? In practice of course there is no definitive answer to this and the issue must be considered on a case-by-case basis – another instance of being aware of fitness-for-purpose.

A third relates to the issue of evidence-based policy. The chapters by Wood, Gyourko and Williams show that in the absence of sound evidence policy positions can be irrelevant to the problem they are attempting to address, or generate unintended and unwanted distributional and/or efficiency effects. Developing evidence-based policy is often no simple matter, however, as the chapter by Bramley shows.

A fourth concerns the more general issues that the chapters by Williams, Donnison and Stephens, and Best throw up in terms of the appropriate relationship between academia and policy makers. There is a constant tension between the world of politics and the world of the academy. Should research be the handmaiden of policy, or the guardian of the public interest? Can it be both? In practice, there must be times when academia speaks truth to power, and times when power returns the compliment. Again, the relationship between policy-making and research must in any specific situation be one that is fit for the given purpose – but we must all be aware of the rules of the game being played.

The individual chapters in this book also show how housing economics has developed over the last two decades. An important complementary question to ask is how it might develop in the years to come. Our crystal ball is as clear or as foggy as the next person's with an interest in the field, but we offer the following thoughts and hopes on the matter.

As with any applied area, data and access to it is of fundamental importance to housing economics. In the last 20 years there have been remarkable leaps in computing power and ease of use for even the most demanding econometric and mathematical software. With some important exceptions, this has not always been accompanied by improvements in the quality of housing market data sets. This is partly the result of commercial confidentiality but it is also a consequence of data providers failing to recognise the policy and practical relevance of better information. In Britain, the pursuit of evidence-based policy is becoming reflected in more open access to public data, in recognition of the greater need for good empirical information at local levels and in an increasing amount of longitudinal data collection. However, even in 2001, the Census was carried out without any question on household incomes or resources. Our hope for the future is that technological developments in statistical and GIS software will marry with increased access to improved data in the UK – but this is unlikely to happen evenly or smoothly.

We suspect that space will become more rather than less important in both theory and policy terms. While an increasing amount of research in theoretical housing economics is attempting to allow for space in a meaningful way at different levels of aggregation, it is also becoming increasingly clear that housing analysis has to cohere *across* levels of aggregation (Meen 2001). An integrated framework of analysis from the level of urban neighbourhoods, through sub-markets and segmented housing markets to an adequate representation of regional and ultimately national housing markets is a long way off, but a prize for which more people are reaching. Galster sketches elements of it in his chapter, and Meen is actively working on aspects of this agenda, but as we say, it will be the work of many years and many hands to achieve.

One reason why it is likely to come is an increasing awareness, certainly in the UK context, that policies developed to operate at different spatial levels can inadvertently work against, even neutralise one another, or alternatively greatly enhance each other's chances of succeeding. MacLennan points out that '[ignoring] geography has a long tradition in British policy making' and that '[for] most of the period since 1980, until the last few years, economic policy was constructed as if the economy existed on the head of a pin' (MacLennan 2002, p. 1). But Britain, in common with a number of other advanced European economies, is beginning to accept the idea of 'territorial management' as a legitimate, indeed inescapable policy objective. Community regeneration policies (for reasons Galster and Meen elucidate) cannot work without an explicit spatial dimension:

'There are also major gains to be had from setting community level initiatives in a better-understood geography of wider systems, for instance in a city-regional framework. More often than not a failure to do this means that policies concentrate on local physical actions and facilities rather than convincingly connecting regeneration activities to wider labour markets, transport systems and the environment; but if they are to succeed long term [these are] precisely the wider system connections that have to be made.'

(MacLennan 2002, p. 7)

And of course both local and city level policy has to connect in some meaningful way with national and international developments.

'We need a new framework of policy thinking and development which marries the impact of top down external forces and events with the creative and recursive effects which clearly push from the bottom up.'

(MacLennan 2002, p. 6)

With a continued growth in understanding by policy makers of the significance of space, not at one, but at many levels simultaneously, there will be increasing demands for models and theory to provide an evidence-base for policy work.

And this last requirement is the final big pointer towards the future. While academic independence must never be taken lightly, the trend to evidence-based policy will gather steam, and hopefully create a positive dynamic between the academic and policy-making worlds. As new benchmarks are set in the evidence-base of specific policies, greater demands will be placed on research to furnish the needed information. More sophisticated policy positions will increase the demand for more sophisticated and realistic representations of housing markets. The meaning of 'fitness for purpose' is shifting in policy terms, and with it the goalposts for what is acceptable as a representation of housing markets will shift also.