Bringing home the housing market

Should homes be just for making money from, asks **Susanne Velke**

The traditional idea of buying property with the foremost thought of making it a home, has changed.

The housing market should be a natural social institution which allows citizens to accommodate their lives according to their needs, means and preferences. It should be the principal economic mechanism ordering the transfer of homes between those who want them and those who have them. But in recent years it has increasingly become something else as well as this.

Home making has been invaded by the ethics of commerce, and the economics of profit making. Speculative behaviour has made house prices soar. It is creating an unstable market. Houses are now far too expensive.

Politicians and economists alike are seeking remedies to the problem. They want to make housing affordable again. But to do this they really need to start at the root of the problem, the functioning of the market itself. They seem to be choosing not to do this.

The housing market more and more resembles the stock market, an institution whose very purpose is commerce. People are buying and selling houses just to make money.

This speculation tends to lead to booms, bubbles and a final burst of the bubble. In the past, the speculative behaviour of stock market agents has had devastating effects on the overall economy. Stock market crashes are highly economically visible events. Housing market crashes are not so dramatic, yet their effects are probably more devastating in terms of the depths and extent of their consequences.

More people own homes than own shares. And people are more likely to go into debt to buy a house than to buy shares. 'Negative equity' is the word to keep in mind: people with a high mortgage debt will face serious difficulties in paying back their mortgage in the case that the value of their house caves in. They are much more vulnerable to any loss of income, be it through unemployment, divorce or death of a partner. The Labour Party reminded us in its recent election campaign that 'repossession' is not a too-distant memory. Ultimately, one of the worst economic consequences of a housing crash is a national recession, Harrison argues, turning conventional thinking on its head.

Speculation in an asset with such social significance as housing - that is, our homes - drives prices up and forces particularly first-time buyers out of the market. It is an important aspect in the discussion on affordable housing. Solutions need to address it if they are to be effective in the long-term.

To ensure long term stability in the housing market, it is not sufficient to deal only with lack of supply. It is necessary to make sure that the nature of demand is not perverting the housing market. We must change the nature of demand by removing the drive of speculation.

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The housing market is an 'imperfect' market. As *The Economist* put it, houses "are illiquid, trading is infrequent, assets are heterogeneous (both by location and by type), transaction costs are high, and information is imperfect because there is no central exchange." This 'imperfection' and perverse demand make it difficult for the average person looking for a home to act with decision and rationality in the market. In times of intense market competition and an imbalanced situation of supply and demand, these factors come to their full significance. First-time buyers are forced out of the market and the commercial ethic takes over.

The Bank of England tries to tackle these problems indirectly by raising interest rates to check borrowing. Politicians are attempting to procure 'affordable housing' by subsidising first-time buyers - to help them get on the 'property ladder'.

Although subsidies might be widely appreciated among young people, the proposal would only treat the social difficulties that arise from high property prices. And it will be just another financial burden on the national treasury. It will not cure the problem of affordability in the longer term, because such measures do not lead to lower house prices. A policy of subsidy only introduces more people into bidding wars, and increases demand even more. The measures currently being put forward by the government neither lower the prices of houses nor increase the supply of them. It is clear that dealing with the symptoms is not enough.

The 'property ladder' is a false metaphor. The term is a metaphor for a perverted market. Every new rise in prices sets the first step a bit higher. The ladder cannot reach endlessly into the sky. So what's at the top, that the 'ladder' lets us reach? All we know is that there is more money and less people at the bottom of this ladder.

We need measures that cure the market from within. We need measures which do not encourage the commercial ethic in the housing market, and which therefore change the character of demand.

If the assumption of speculative profit is allowed to remain as a principal driver of demand in the housing market, the market will increasingly produce perverse outcomes and fail in its social function as the proper socio-economic mechanism for distributing homes according to needs, means and preferences. **L&L**

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