

LOCAL REGULATIONS AND THE PRICE OF HOUSING

A new Bank of Canada study provides insights into why housing prices remain stubbornly high.

Economists explain that when consumers increase their demand for goods, they bid against one another for a limited supply and so push up the price of those goods. Producers see price increases as an opportunity for profit and so increase the quantity they offer for sale. The larger this response from producers, the smaller will be the increase in price because what consumers want to buy will no longer be in such short supply.

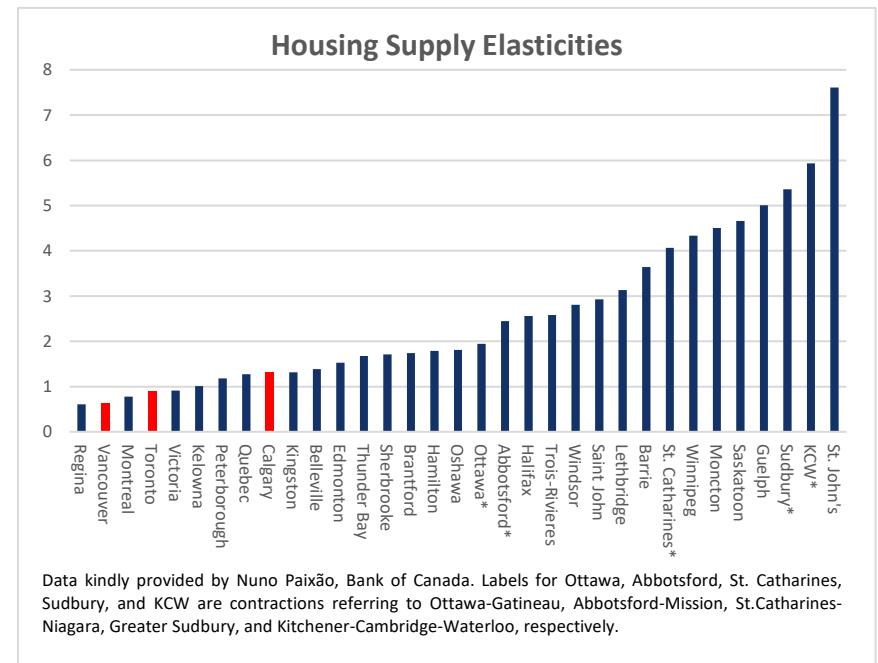
So, what's with housing prices and the price of rental units? Plenty of signals have been provided to house builders and providers of rental accommodation that profit opportunities are available. But they have not responded by increasing the quantity supplied of housing and rental accommodations sufficiently to keep prices from continuing to increase. Why aren't prices moderating?

All levels of government have a role to play in housing markets, maybe local governments in particular.

The story economists tell about how builders and landlords respond to higher prices is predicated on the assumption that their effort to increase supply is not unduly inhibited. But that may not always be the case.

We live together in communities and so our housing choices impact one another, both positively and negatively. Local governments impose zoning laws and regulations to make sure our choices appropriately balance the advantages and disadvantages of living close to one another. These laws and regulations restrict developers in what types of homes they build, how many they build, and where they build them.

Recent evidence from the [Bank of Canada](#) is consistent with previous [research](#) at the School in suggesting local regulations determine, in part, how responsive the supply of



housing is to increase in price. The Bank's report shows considerable variation across communities in the responsiveness of supply to increases in housing prices. In cities like Vancouver, Toronto, and Calgary the response of housing supply is low. In cities like St. John's, Winnipeg and Guelph the response is much larger. The report shows these estimates are correlated with house prices in ways one would expect: In cities where the supply response is low, housing prices have increased by much more than in cities where the supply response is high.

Differences across cities, especially those in the same province, indicate the reasons for them are to be found locally, perhaps in the form of differences in local government regulations. This suggests the need for leadership from local governments to take steps to increase the responsiveness of housing supply to rising prices.