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Low-income housing policies: affordability and integration

Essi Eerola

Abstract

I review the literature on housing policies intended to improve the housing conditions of low-income households and discuss the conclusions that can be drawn from the literature. I distinguish between tenant-based programs like housing benefits and place-based programs like social housing and discuss the general characteristics of these policies in Nordic countries. Finally, I review the effects of these programs on recipient households and segregation in Finland where a large housing allowance program co-exists with a social housing sector.

Keywords: Housing policy, housing allowances, social housing, segregation.

JEL codes: H22, R21, R31.

1 Introduction

Housing policies tend to have a wide range of different objectives. For instance, in Finland the aims of housing policy include everyone's right to good and affordable housing, socially sustainable neighbourhoods, and housing supply that promotes the functioning of the labour market and supports the vitality of the regions (Ministry of the Environment 2020).

Given the broad overall scope, governments intervene in housing markets with multiple goals and multiple programs. A typical goal is the improvement of housing affordability and housing standards of low-income households. A related goal is the prevention of harmful segregation in large and growing cities. In recent years, especially after the financial crisis of 2007–2008, governments have also tried to reduce household indebtedness, for instance by limiting mortgage borrowing as part of a broader set of policies aimed at securing macroeconomic stability. At the same time, most governments have a long history in promoting homeownership, for instance through favourable tax treatment.

These types of housing policies are likely to become even more important and debated in the future. One important reason is urbanization, which creates large economic benefits but also poses significant challenges for social sustainability. For instance, agglomeration effects often increase land and housing prices in large cities. High housing prices directly reduce affordability and may also increase segregation. Together, high household indebtedness and high housing prices may also increase macroeconomic instability.

In this article, I review low-income housing policies in the Nordic countries. I will concentrate on three interconnected issues: affordability, access, and residential segregation. Although the Nordic countries are similar in many respects, their housing policy regimes have historically been based on quite different general principles. These differences concern not only the publicly subsidized housing sector, but also the relationship between rental and owner-occupied housing, regulation of the private rental market and the role of housing benefits as part of the overall welfare system.

The structure of the article is as follows. In Section 2, I discuss why and how housing consumption of low-income households is subsidized. In the discussion, I will distinguish between tenant-based programs like housing benefits and place-based programs like social housing. I will argue that although the two types of programs are based on different principles, they also have important similarities. In Section 3, I discuss the general characteristics of housing policies in the Nordic countries. In Section 4, I focus on the effects of these programs on recipient households and segregation in Finland, where a large housing allowance program co-exists with a large social housing sector. Section 5 concludes.

2 Low-income housing policy: why and how?

2.1 Why subsidize housing?

When thinking about housing policies from the point of view of low-income households, two important objectives include provision of affordable housing and reduction of residential segregation through social mixing.

Affordability is a difficult concept. It tends to aggregate into a single metric different issues ranging from income distribution and housing quality distribution to government housing market regulation and municipal decisions affecting neighbourhood quality and supply of housing. Changes in affordability over time are particularly difficult to interpret without additional information about the different components of the measure. For instance, the average rent-to-income ratio may decrease because renters experience a positive income development or because access to housing credit becomes more difficult and as a result middle-income households rent their housing more often than previously.[97]

To make matters even more complicated, affordable housing sometimes refers to a certain segment of the housing stock. In this case, affordability is defined relative to market prices. From this perspective, affordable housing becomes synonymous with social housing or rental housing sector with rents below market rents. Affordability, or lack thereof, can also refer to general level of rents or housing prices in a given urban area.

Low-income households tend to spend a large share of disposable income on housing. As housing is not easily divisible, housing consumption is costly to adjust. Therefore, when households experience transitory negative income shocks, they are more likely to first reduce spending on non-durables like food, clothing, or transportation. One concern is therefore that low-income households find it hard to afford consumption of other goods.

Another concern relates to household location choices and differences in housing costs across different labour market areas. As housing costs vary substantially across areas, moving to another labour market area might involve an increase in the cost of housing. Subsidizing housing costs aims at mitigating the negative effects of high housing costs on mobility. This issue has become more important as the housing costs in large growing cities have been increasing.

In principle, these concerns could be addressed by unconditional cash transfers instead of housing subsidies, but there may be reasons to think that subsidies tied to housing choices are more efficient. One argument follows from housing as a merit good. Housing has similar characteristics as education and health care in that households may not fully recognize the private benefits from housing consumption or housing consumption may generate positive externalities within the household. An important aspect relates to how the housing choices of adults affect children.[98]

97. For discussion on the issue, see e.g. Quigley and Raphael (2004) who decompose changes in affordability in the US over time to study the relative importance of different components.
98. See Collinson et al. (2016) for more discussion on the arguments for in-kind transfers relative to cash transfers.

In addition to these concerns relating to direct effects on low-income households in terms of affordability and access, housing programs may also have important effects beyond the direct effects on the recipient households. One important issue is related to neighbourhood effects and residential segregation. Within a labour market area, the cost of housing is directly linked to the neighbourhood characteristics. This means that local amenities are capitalized into the price of housing. Given that high-income households are willing to pay more for neighbourhood quality than low-income households, they tend to outbid low-income households for better quality neighbourhoods. This leads to residential sorting according to income. While this type of segregation is a natural phenomenon in urban areas with heterogeneous localities, it may also have negative consequences.

Of course, policymakers may care about neighbourhood segregation for its own sake. However, living in a deprived neighbourhood may affect, for instance, children's school outcomes and their future labour market outcomes. In the presence of such neighbourhood effects, housing programs may improve overall welfare if they affect the neighbourhood quality of low-income households. Two issues make understanding and tackling this problem quite difficult. First, income is an important determinant of household location choices. This makes it difficult to identify the direction of causality when studying the relationship between residential segregation and income. Second, identifying neighbourhood effects does not in itself give sufficient guidance for choosing appropriate policies to tackle the issue.

To date, there exists credible evidence on the causal effects of neighbourhoods, especially on children's long-term outcomes (see e.g., Chetty et al. 2016 and Chyn 2018). However, this evidence is mainly from the US, and it is unclear to what degree these results on neighbourhood effects can be generalized to the Nordic context because of differences in the overall welfare systems and in the quality distribution of publicly provided services. It is therefore important to obtain evidence on the magnitude of these effects also in settings were the socio-economic differences between the neighbourhoods are relatively modest.

In general, it seems fair to say that the mechanisms behind neighbourhood effects are not well understood. One potential mechanism is residential instability. Involuntary moves could have damaging effects not only on those moving by breaking up social networks and forcing children to change schools, but also on those who remain. However, the social life of individuals and families in large urban areas may be segregated for many different reasons. Clearly, these questions are important not only for housing policy, but also for the supply of local services, especially schools, public transportation, and accessibility more generally as well as for political representation.[99]

It is also important to note that measuring changes in the degree of segregation over time is not straightforward, especially if one is interested in segregation based on income. It is also not clear what the relevant geographic scope of the neighbourhood effects is. This is partly explained by data availability. Often researchers are forced to resort to data with location information based on administrative borders. Fortunately, this is rapidly changing. Increased availability of

99. For instance, Harjunen et al. (2021) show that in Finland, residential sorting leads to geographic inequality in political representation that affects school closures. The changes in the school network in turn further reinforce residential segregation.

exact location information of households for research purposes will allow a more flexible analysis of the geographic scope of the neighbourhood externalities.

2.2 How to subsidize housing - social housing and housing benefits

Social housing is a general term for quite different models and programs applied in different countries under different names. I define social housing as rental housing with three main characteristics: i) rents are regulated, ii) housing units are allocated according to specific rules, often targeting low-income households or specific groups like the elderly, students or the disabled, and iii) housing units are owned and managed by municipalities, non-profit organizations or other actors with a public benefit purpose and are subsidized by central and local governments.[100]

In the social housing sector, rules regulating rent setting vary a great deal. OCED (2020) distinguishes four main types. *Market-based* rents are determined relative to market rents of similar properties. *Cost-based* rents are determined by maintenance and capital costs of the property. *Income-based* rents depend at least partly on the income of the tenant. *Characteristic-based* rents are based on dwelling characteristics. Clearly, these different rent-setting models will create different incentives for the tenants and owners of the buildings. They will also result in different distributions of benefits for the tenants as measured by rent savings relative to market rents.

Rules on tenant selection are typically based on individual tenants (for instance, household income and composition, nationality, housing need). Some rules relate to the building so that a certain fraction of units must be allocated to households with incomes below a threshold (OECD 2020). In most countries, the right to occupy a particular unit is granted indefinitely (Scanlon et al. 2015).

Finally, the ownership structures and financing of social housing take different forms. In some cases, governments and municipalities directly provide social housing. In addition, governments may provide grants, tax credits, loans or loan guarantees to social housing providers. Local governments also subsidize social housing by supplying land at discounted prices (Scanlon et al. 2015).

Typically, social housing programs co-exist with some type of direct subsidy program. Important examples of the latter include housing allowances, which are means-tested benefits and depend on household size and composition and on housing costs. In addition to the household characteristics, the benefit may depend on location or other characteristics of the building. These programs may be broad or more targeted to certain groups of households, such as families with children or pensioners. The benefits are entitlements in that all eligible households receive the allowance if they apply for it. As a result, the overall amount of outlays typically varies over the business cycle.[101]

100. In the Nordic context, social housing defined in this manner does not cover all non-profit housing segments. For instance, in Sweden the aim has traditionally been to make municipal housing available for all citizens. I will return to this issue in the next section when discussing the Nordic regimes.
101. The organization of, say, the US housing choice voucher system is quite different. A household is eligible for a voucher if its income is low enough relative to the local income level. Given a fixed budget, only a fraction of eligible households receives a voucher. After having received a voucher, the recipient needs to find a dwelling that satisfies the requirements of the program.

The differences between social housing programs and housing allowances are often highlighted in the public discussion. However, social housing and housing allowance programs are also similar in three important ways. First, to the extent that social housing rents are below market rents, both constitute a transfer to recipient households. In the case of housing allowances, the transfer is a cash subsidy. In the case of social housing, the transfer comes in the form of rent savings relative to market rents.

Second, both programs also impose costs to taxpayers. For housing allowances, these costs are direct budgetary costs. For social housing, they consist of direct subsidies and foregone income. If the amount of foregone income is not estimated on a regular basis, a transparent comparison of program costs is not possible.

Finally, both may subsidize housing in a manner that increases the aggregate demand for housing. This can happen in two different ways. First, housing allowances or rent savings in social housing increase disposable income of recipient households and reduce disposable income of households who finance the system (income effect). This may increase overall housing demand if the income effect is larger for recipient households. Second, both allowances and rent savings may also reduce the cost of housing relative to other consumption for recipients (substitution effect). If the programs reduce the cost of the marginal housing unit relative to other consumption, they may increase demand for housing. Depending on the supply conditions, this may lead to higher rents in the private rental market.

Given these important similarities, why favour one over the other? Housing allowance programs are often more transparent than social housing programs. Social housing units need to be rationed when rents are set below market rents. Therefore, the details of the allocation mechanism determine the distribution of benefits. Equal treatment of similar households cannot be guaranteed with a fixed number of housing units. Housing allowance programs are also more flexible when the need for support is growing. At the level of the economy as a whole, housing allowance programs act as automatic stabilizers by complementing other segments of social security systems.

There are, nevertheless, at least two reasons to think that social housing programs could dominate housing allowance programs in helping low-income households. The first relates to location. Social housing tenants are required to reside in specific buildings. This means that in principle it is possible to design a social housing program so that it helps to reduce residential segregation. Second, housing is different from many other consumption goods in that it is possible to be excluded from the private rental market for various reasons. It is hard to claim that direct transfers could ever solve this problem. However, as the discussion in the following sections shows, it is not always obvious that the actual social housing programs are able to realize these advantages.

3 On the Nordic housing policy models

In all Nordic countries, a majority of households own their home. For the most part, the rest live in rental housing. The organization and size of the private rental market varies between the Nordic countries. In Finland, the private rental market is unregulated and quite flexible while in Denmark, Norway and Sweden different types of rent regulations are in place (Kettunen & Ruonavaara 2020). In addition, the non-profit rental market can take different forms, including social housing discussed above.

Table 1 shows the share of households living in owner-occupied housing (including so called co-operative or tenant-owned housing) in the Nordic countries and the share of non-profit rental housing stock.

Table 1 Owner-occupied housing and non-profit rental housing in Nordic countries

	Share of home owner households, percent		Non-profit dwellings, as percent of owerall housing stock	
	2010/2011	Latest	2010/2011	Latest
Denmark	57	53	22	21
Finland	68	65	13	11
Sweden	56	63	23	16
Norway	77	73	5	4
Iceland	75	73	9	11

Note: For Sweden, the first two columns contain the share of dwellings, not households.

Sources: For Sweden, Grander (2020, Table 6). For other countries, OECD Affordable Housing Database.

Apart from Sweden, the share of the households living in owner-occupied housing has declined slightly in recent years. There is some indication that especially among young households the share of owner-occupiers is declining. For instance, in Finland the share of owner-occupiers among the 30–34-year-old adults was less than 50 percent in 2018 compared to 58 percent a decade earlier (Statistics Finland 2019). A similar trend has been previously documented for Sweden and Denmark (see e.g., Enström Öst 2012 and Nielsen & Jensen 2011).[102]

The second general trend is that the share of non-profit rental housing is slightly falling. Provision of non-profit housing has not kept pace with overall construction and part of the stock has been privatized, freed from regulation, or demolished.[103] Together these two trends mean that a well-functioning private rental market is highly important when aiming to guarantee affordable housing for

102. Several potential explanations have been put forward to explain the phenomenon (see Eerola et al. 2021).
103. The same trend is true in many other European countries (Scanlon et al. 2015) and the US. In the US, after the Second World War, government-managed public housing was the only major form of federal low-income housing assistance. During the past twenty years, the public housing stock has shrunk, but this reduction has been more than offset by new recipient households in tenant-based programs (Collinson et al. 2016).

low-income households.

Housing policy regimes in the Nordic countries differ quite substantially, both in their general aims and principles as well as in implementation. Bengtsson et al. (2014) discuss the differences in a comparative study taking a historical perspective starting in the early 1900s. The authors classify the Nordic systems along two dimensions. The first dimension relates to whether the regime explicitly favours owner-occupied housing relative to rental housing. The second dimension relates to whether the housing policy can be characterized as universal or selective. A universal housing regime aims at ensuring good quality housing for all citizens. A selective regime aims at targeting certain groups of individuals or households based on different criteria. The latter regime can also be more closely connected to the social security system. Bengtsson et al. (2014) classify the Danish and the Swedish regimes as universal, and the Finnish and the Icelandic regime as selective.

In Denmark, non-profit housing is defined as general housing (*almen bolig*) and is provided at cost-based rents through a variety of public interest housing associations. The housing associations receive government subsidies of capital costs (Svarer et al. 2005).

The Swedish system has traditionally included a broad model of non-profit housing managed by municipal housing companies for the 'benefit of everyone' (*allmännytta*). The Swedish regime also contains a small selective *secondary housing market* for households excluded from the rental market. Within this program, the municipalities' social services rent housing units from private and public housing companies and sublet the units to their clients. Initially this program was designed to provide housing for those incapable of obtaining housing on their own, for example due to substance abuse or other social problems (Grander 2017).

The Finnish system is based on government-subsidized public and private non-profit organizations providing rental housing that is allocated based on need and income.

Of course, the actual degree of universality or selectivity will ultimately depend on the details of implementation. In addition to tenant selection rules, an important factor is position of the non-profit housing units in the quality distribution of the overall housing stock. The location and other characteristics of the non-profit housing units will determine who will apply for the units.

In all Nordic countries, the non-profit housing sector co-exists with a housing allowance program. Table 2 compares the housing allowance programs in the Nordic countries. There are clear differences between countries both in the distribution of recipient households across income groups and in the size of the programs.

Table 2: Housing allowance (HA) in Nordic countries

	Share of households receiving HA by income quintile					HA spending as percent of GDP
	Bottom	2nd	3rd	4th	Top	
Finland	57.3	21.3	8.5	4.4	2.9	0.9
Denmark	40.8	39.4	10.1	2.9	1.5	0.7
Sweden	38.3	9.1	3.7	1.4	0.7	0.3
Iceland	39.4	35.8	29.2	24	9.3	0.2
Norway	14	2.1	0.3	0.3	0.1	0.1

Note: Share of households receiving housing allowance in 2017.

Source: OECD Affordable Housing Database.

In Finland, the program consists of two distinct schemes (general housing allowance and pensioners' housing allowance) with no restrictions on eligibility except income. The Finnish housing allowance system covers a large share of the population and has been extended in recent years. Since the beginning of 2000s, the number of recipient households living in rental housing has more than doubled.

In Sweden, in contrast, the number of households receiving housing allowance has decreased since the early 2000s. The system is targeted to families with children and young adults under 29 years of age. Housing allowance is paid primarily to single parents (Swedish Social Insurance Agency 2019). In addition, there exists a separate system based on income and wealth for pensioners older than 65 in full retirement pension. Some 30–35 percent of the pensioner population are likely to be eligible, but only 15 percent of the population receive the housing supplement (Engström et al. 2019).

3.1 Finland vs. Sweden

Given the quite different premises for the housing policy regimes, it is interesting to compare the distribution of households with respect to tenure in Sweden and Finland. In Finland, the well-off are almost always owners. Most households in the lowest income decile are renters, while 90 percent of households in the highest income decile are owner-occupiers. Social housing tenancy is more common in the lowest income deciles, but even in the highest income decile, a fifth of renters live in social housing (Hirvonen et al. 2014). Also in Sweden, tenure is strongly driven by income. Renters have on average lower incomes than owners do, and tenants in municipal rental housing have lower incomes than tenants in the private rental market. In addition, the share of immigrants from non-EU countries is higher in municipal housing than in private rental housing (Grander 2020). In general, although the overall level of ethnic segregation is lower in Helsinki, immigrants seem

to be more concentrated in social housing in Helsinki than in Stockholm (Andersen et al. 2016).

Concentration of low-income households in non-profit housing in large cities cannot be considered good or bad without further information. On the one hand, the cost of housing is high in large cities and non-profit housing may offer low-income households the only possibility to live in these cities. On the other hand, the concentration may be problematic if the non-profit housing is geographically very concentrated.

The Swedish municipal housing regime has changed in important ways in the 2000s because of privatizations and the need to adapt to EU legislation. The latter has resulted in a change in the law regulating municipal housing companies. Now, municipal housing companies should act in a 'businesslike way' but also have a 'public purpose' (Elsinga & Lind 2013).

Currently, the Swedish municipal housing companies impose financial requirements for households to be eligible to rent. The requirements might include, for instance, permanent employment or an income threshold.[104] At the same time, households in municipal housing in Sweden have become poorer in relative terms (Grander 2017). One possible reason is the expansion of the secondary housing market. Because of income thresholds in municipal housing, low-income individuals may be forced to rent in the secondary housing market.

Another potential reason is the conversion of municipal rental housing into private cooperatives. For instance, the city of Stockholm allowed municipal housing tenants to buy their dwellings if at least half of the tenants were in favour of buying.[105] Andersson and Magnusson Turner (2014) study the tenant composition in the municipal housing buildings before and after the conversions. Two things happened to the population mix. First, because most conversions took place in inner city neighbourhoods already dominated by cooperative housing, municipal rental housing became increasingly concentrated to the periphery. Second, households moving out from converted municipal housing had lower earnings and a lower rate of employment, and were less likely to have university education than those replacing them.

The overall social housing program has changed importantly in the 2000s also in Finland, but for different reasons. A large share of the social housing units has been freed from regulation, overall demand for housing has shifted from small municipalities to large cities with increasing rent levels, and the tenant selection legislation has been modified. I will discuss the recent developments in the next section.

104. See e.g. Elsinga and Lind (2013) and Grander (2017).
105. In Stockholm, three municipal housing companies used to own about 110 000 housing units or 30 percent of the housing stock. They privatized 12 200 units between 1999 and 2004 (Sodini et al. 2016).

4 Evidence from Finland

4.1 Institutional context

In Finland, owner-occupied housing enjoys a tax-advantaged position relative to rental housing and investment in financial assets. Housing is also the single most important form of wealth for Finnish households. In 2016, according to the Statistics Finland Wealth Survey, roughly 50 percent of household net wealth was in the form of owner-occupied housing as principal residence, 6 percent in secondary residences and 10 percent in other real estate.

Households either own their housing directly or own shares of a housing cooperative. Housing cooperatives own the building and often the lot. Owning shares gives the right to occupy, renovate and rent out a particular unit.

The most common alternative to owner-occupied housing is rental housing. The rental market can be divided into an unregulated, private rental market and a social housing sector. Landlords in the private rental market are private corporations and foundations, large institutional owners such as banks and insurance companies, and private individuals. Units owned by private individuals constitute roughly two thirds of the private rental market. In the social housing sector, municipalities own more than 60 percent of the dwellings. The rest are owned and managed by non-profit corporations and associations.

Tenant selection in the private rental market is not regulated. Landlords are entitled to use their own criteria when selecting tenants and have the right to check the credit history of potential tenants. Rent setting is free but was controlled in different ways until the early 1990s. Starting in the late 1960s, rents were allowed to be freely set only when the unit was rented for the first time, but rent increases were not allowed thereafter. In the 1970s, rent control was extended to new units. The regulation then applied to all rental units, and the maximum acceptable rent increases were determined annually by the government based on proposals made by tenant and landlord representatives. Rent control was gradually abolished in the early 1990s.[106]

Despite a long tradition of social mixing policies and low-income inequality in the society as a whole, there are some indications of increased segregation in Finnish urban areas. Saikkonen et al. (2018) study the recent development of income inequality and segregation in the Helsinki, Turku and Tampere regions. They conclude that the regions are different in terms of segregation. Ethnic segregation is strongest in the Turku region while the Helsinki region, and especially the city of Helsinki, is characterized by stronger segregation in terms of household income.

4.2 Two large overlapping programs

The details as well as the stated objectives of the social housing program in Finland have varied over time. Currently, the main objective is to provide affordable housing for low-income households and to create socially balanced neighbourhoods and buildings that are diversified in terms of household composition. Part of the subsidized housing stock is explicitly directed towards special groups such as the

106. Kettunen and Ruonavaara (2020) discuss the history of the rent control in Finland.

disabled, students and the elderly.

The aim of the housing allowance program is to reduce the cost of housing to the recipient households. There is substantial overlap between the two programs. In 2018, roughly 40 percent of general housing allowance recipients were social housing tenants.

4.2.1 Housing allowance in Finland

Initially, in the 1940s, housing allowance was paid to families with many children. In the early 1960s, all low-income families with children living in rented flats became eligible. By the 1980s, housing allowance had been gradually expanded to apply to all kinds of households and tenure.

The program has been further reformed and extended during the 2010s. First, in 2015, the housing allowance was made more generous as part of a large reform which radically simplified the way in which the allowance depends on household income and the characteristics of the housing unit. In 2017, a separate system for students was abolished and students were included in the general housing allowance program. This reform led to more generous allowances for students not living with a working partner.

The housing allowance is a means-tested benefit covering up to 80 percent of the rent up to a rent ceiling. The rent ceiling varies based on local affordability, and the allowance depends on household size as well as household income. The same rules apply to tenants in social housing and in private rental housing. Eligibility does not depend on tenure, but 95 percent of the housing allowance recipients live in rental housing.

Housing costs of low-income households are also covered through the social assistance system. Social assistance is provided to individuals and families whose income and assets do not cover their essential daily expenses. Unlike the general housing allowance program, social assistance can reimburse reasonable housing costs in full. The limit for what is considered reasonable varies by municipality. If the housing costs are judged unreasonably high, the beneficiary should search for more affordable housing.

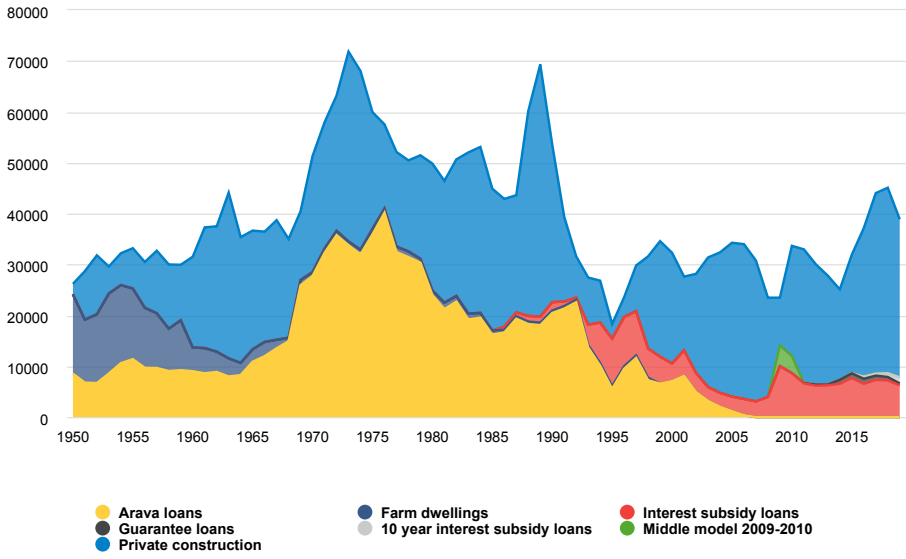
4.2.2 Social housing in Finland

The Finnish social housing program dates from the mid-1940s. Initially the program consisted of various subsidy schemes for construction and renovation of rental housing and owner-occupied housing. In the 2000s the main focus has been on rental housing in growing urban areas. More than 90 percent of construction of subsidized dwellings was located in growing cities in 2019. The program is implemented by the Housing Finance and Development Centre of Finland (ARA), an off-budget governmental agency operating under the supervision of the Ministry of Environment. The same program covers housing owned by municipalities and by non-profit corporations and associations.

Figure 1 shows annual residential construction in Finland from 1950 to 2019 divided into private construction and different ARA programs. As the figure shows, subsidized construction constituted a large share of all construction, especially in the 1970s and 1980s, but its share was gradually shrinking after the 1990s recession until the financial crisis. During the last ten years or so, different new programs have been established, some of which have been temporary. The figure also shows that private construction is quite sensitive to the business cycle, with remarkable reductions in

construction during the severe recession in the early 1990s and the financial crisis in 2008–2010. During the early decades of the ARA programs, most dwellings were built with AVARA loans granted by ARA, while in the 2000s the main forms of construction subsidies have been interest subsidies and loan guarantees.[107]

Figure 1 Residential construction in Finland, 1950–2019



Notes: For units in category '10 year interest subsidy loans' rent setting and tenant selection restrictions are in place for 10 years. For units in category 'Model 2009–2010' there were no rent setting and tenant selection restrictions.

Source: Own calculations from Statistics Finland building and dwelling construction data and ARA construction data.

The subsidized rental properties are subject to different types of regulation regarding the use and transfer of properties. A typical restriction period is 40 years. After the restriction period, the owner can freely set rents, select tenants and sell the units at market prices.

Over one million dwellings have been constructed within the social housing program and currently more than 400 000 units are still subject to the tenant selection and rent setting restrictions. Although the absolute number of social housing units subject to restrictions has remained quite stable in the 2000s, their share of the overall housing stock has decreased since the early 2000s. The share of social units is highest in large cities. For instance, there are some 76 000 social housing units in the city of Helsinki, which amounts to roughly 20 percent of the overall housing stock in the city (Housing Finance and Development Centre of Finland 2019).

Rent setting is cost-based. The average rent depends on the capital and

107. Bengtsson et al. (2014) discuss in more detail the evolution of the system.

maintenance costs of the building, but rents of specific units may vary depending on unit characteristics. The general idea is that the owner receives subsidies that reduce capital and maintenance costs. Through the rent setting regulation, the subsidies lower the rents paid by the tenants. This means that the rents in social housing units relative to market rents vary across municipalities and neighbourhoods.

Tenant selection is based on legislation. Previously, tenant selection legislation included formal income limits. The limits were relatively high in European comparison and were abolished in 2008 (Andersson et al. 2010). Income limits were re-introduced in the Helsinki Metropolitan Area in 2017. The limits were again relatively high. Only 18 percent of all households and 25 percent of owner-occupiers in Helsinki had income levels exceeding the limits. The limits were abolished in 2018. At the same time, the government abandoned plans to introduce periodic income inspections for tenants in social housing units (Vuori & Raunionmaa 2018).

Currently, the selection criteria include the applicant's urgency of housing need, wealth, and income. Details of the selection process depend on the owner. Typically, however, there is no explicit ranking of the applicants or a formal queuing system. In the case of the city of Helsinki, the applicants cannot apply for a specific flat, but instead express preference for a neighbourhood. Once a household has obtained a social housing unit, it has the right to occupy the unit indefinitely, regardless of changes in its income or wealth.

The buildings are owned by municipal rental housing companies and by non-profit organizations.[108] Municipalities are important decision makers within the program. However, especially in large cities, the decisions are also directly affected by the ARA regulations. For instance, one prerequisite for ARA construction is a reasonable lot price. ARA approves the lot prices and the approval is regulated by regionally determined maximum lot prices. This restricts the municipalities' freedom in terms of locating new social housing units in certain neighbourhoods.

Regarding financing, the government subsidizes social housing through the different programs managed by ARA. In addition, municipalities subsidize the municipal housing companies in particular by not including capital costs in the cost-based rents, by providing loan guarantees, and by subsidizing lot rents and selling prices (Kaleva et al. 2013).

The overall costs of the social housing program to the taxpayers consist of direct subsidizes and guarantees administrated by ARA and various subsidies and discounts granted by the municipalities. There exist no systematic data on these costs.

4.3 On the effects of the programs

4.3.1 Direct effects on recipient households

The effects of the housing allowance program are constantly under scrutiny in Finnish public discussion. This is probably explained by the high degree of transparency of the program costs combined with increasing overall outlays during the last decade. The main concerns relate to the potential effects of the program on

108. ARA grants non-profit status. In 2020, some 550 organizations had non-profit status.

rents paid by recipient households and on the overall rent level. These are important issues because large rent effects would substantially undermine the efficiency of the program. However, both are difficult research questions because of reverse causation. That is, housing allowances may affect rents but rents may also affect the amount of housing allowance received.

Eerola and Lyytikäinen (2021) use two different strategies to isolate the rent effects of housing allowances from other factors affecting rents. First, they exploit the discontinuities in the Finnish housing allowance scheme that was in place until 2015. The system featured discontinuities caused by rent ceilings, which varied as a function of the characteristics of the dwelling. The discontinuities are used to assess whether differences in the housing allowance generosity affect rents paid by the recipients. The second research design is based on a housing allowance reform implemented in 2002. The reform changed in different ways the rent ceiling in different types of housing units. The resulting exogenous variation in housing allowances can be used to identify the rent effects.

Both analyses suggest that the rent effects of housing allowances are small. That is, differences in the housing allowance generosity do not translate into differences in rents of the recipient households.[109] One possible reason for these relatively small rent effects is related to the nature of housing consumption. Housing consumption can only be adjusted by moving, which is always costly. It is conceivable that the differences in the housing allowance generosity are too small to induce mobility. However, as housing units with similar characteristics are close substitutes, conditional on moving, a recipient household should find a unit with more generous housing allowance more appealing. The evidence from a UK reform that reduced housing benefits for social housing tenants deemed to have a spare bedroom supports this hypothesis. The aim was to promote mobility and reallocation of the social housing stock. Although the policy was not successful in encouraging mobility, it did incentivize those who moved to downsize (Gibbons et al. 2020). If the Finnish program had similar effects, they were not large enough to be detected in the analysis.

The incentives generated by the housing allowance program also depend on the expected length of the housing allowance spell. If the expected housing allowance spell is short, changes in disposable income do not result in housing consumption adjustments, but instead affect non-housing consumption. In this respect, different types of recipients are likely to be in quite difference situations. Students constitute a particularly interesting group. The length of the expected housing allowance spell should be more predictable for students than, for instance, the unemployed.

Despite the large scale of the Finnish housing allowance program, its effects on labour supply or housing consumption choices have received much less attention in research. Although the negative incentive effects on labour supply as well as the incentives related to location choices are much discussed, there is no clear evidence on the magnitude of the effects.

Because social housing rents in Finland are cost-based, they can be expected to be lower than market rents, especially in large cities. To understand the distributional impact of the program one must first determine the rent savings generated by the

109. Kangasharju (2010) found substantially larger rent effects of the 2002 housing allowance reform.

program.

Eerola and Saarimaa (2013, 2018) assess the rent savings accruing to social housing tenants in the city of Helsinki, where the city owns a large stock of subsidized rental units. Rent savings are defined as the difference between the market rent of a social housing unit and its actual regulated rent. Of course, the market rents of the social housing units are not observed and are likely to vary substantially depending on location and physical attributes of the unit. To overcome this problem, the study uses detailed micro data on the attributes, rents and the location of private and social rental housing units in Helsinki.

Implicit prices for housing attributes within the unregulated rental market are recovered using hedonic regression methods with spatial fixed effects. These implicit prices along with estimates of spatial fixed effects are then used to predict market rents and to calculate rent savings for individual social housing units. This can be done without information about the tenants, as social housing rents do not depend on tenant characteristics.

Eerola and Saarimaa (2013) analyse rent savings in dwellings owned by the city and non-profit organizations respectively and examine how the rent subsidy varies according to the characteristics of the dwelling. The rent savings are substantial in dwellings owned by the city but vary considerably depending on the size and location of the dwelling. The rent savings decrease with distance to the city center and are highest in expensive neighbourhoods. In contrast, rent savings in dwellings owned by non-profit organizations are on average significantly smaller.

Eerola and Saarimaa (2018) match unit level rent savings with household register data for social housing dwellings owned by the city. The aim is to study the distribution of rent savings as well as to compare the distribution of the rent savings with the distribution of housing allowances.

The total rent savings to social housing tenants are considerable and comparable to the total amount of housing allowance. Housing allowances are much more concentrated to low-income households than rent savings. The households in the lowest income quintile receive 66 percent of the total amount of housing allowances, but only 34 percent of the total rent savings. Moreover, 22 percent of the rent savings in social housing accrue to households with income above median income.

4.3.2 Effects on segregation

In theory, both programs may be important for residential segregation. In an unregulated housing market, local amenities are capitalized into housing prices and increase the cost of housing. Therefore, housing allowances that enable families to move to dwellings that are more expensive also enable them to move to more advantaged neighbourhoods and thereby reduce segregation. In the social housing sector, the neighbourhood choice of the program participants is determined by the location of the subsidized buildings. Therefore, at least in principle, locating social housing to sought-after neighbourhoods and avoiding large concentrations in specific areas may serve to reduce segregation. Reliably detecting these effects is notoriously difficult as the location choices of households are affected by a host of factors typically unobservable to the researcher.

To shed light on this issue, Eerola and Saarimaa (2018) compare the socio-economic

mix and quality of the neighbourhoods of social housing tenants and similar households in private rental housing in Helsinki. One potential strategy for reducing the spatial concentration of poor households is to allocate part of the social housing subsidy to middle- and high-income households. This can be done by actual tenant selection or by giving the right to occupy the subsidized dwelling indefinitely. Analysing the neighbourhoods that social housing tenants occupy, however, suggests that this strategy does not work as intended.

Not surprisingly, there is clear residential sorting according to income in the private rental market. High-income tenants tend to live in neighbourhoods with higher median income, less poverty, higher education level and higher market rents. Interestingly, a similar pattern can be observed across income quintiles in the social housing buildings owned by the city. Tenants higher up in the income distribution live in better-quality neighbourhoods than the ones in the lowest income quintile. More importantly, social housing tenants in the lowest income quintile live in poorer, less educated, and lower quality neighbourhoods than households in the same income quintile in the private rental market.

Low-income social housing tenants are therefore exposed to poorer, less educated, and lower quality neighbourhoods (measured either at the level of post code area or building) than similar low-income households in the private rental market. This finding suggests that social housing programs may lead to more segregation than tenant-based alternatives, even when neighbourhood mixing is an explicit aim of the program.

There may be several reasons for this observation. One potential issue relates to the difficulty of attracting middle-income households to social housing dwellings in neighbourhoods where social housing sector is large relative to overall housing stock. Another issue is the tax advantages of owner-occupied housing. These advantages generate a strong incentive for middle-income households to become owners. As most of the social housing buildings are reserved for tenants who qualify for social housing, those wanting to become owners need to move, which limits the potential for social mixing.

4.3.3 General equilibrium effects

As discussed in Section 2.2, in addition to all other effects, both social housing and housing allowances may influence the overall rent level. In the social housing sector, the logic is as follows: When part of the overall housing stock is allocated with regulated, below market rents, some households choose to apply for a bigger or a more centrally located dwelling than in the absence of the regulated rents. As a result, given the size of the overall housing stock, the effective supply left for households that do not have access to subsidized housing is smaller. This leads to higher rents in the unregulated rental market.[110]

The same mechanism works for housing allowances. However, almost all studies on the incidence of housing allowances use variation generated within the housing allowance program to assess the effects on rents paid by recipient households. Identifying the effects of housing allowances on the overall rent level requires a different research design. If the rental housing market is competitive, a change in

110. Kaas et al. (2021) offer a model analysis on the German social housing stock taking these rent effects from the social housing segment to the private rental market into account.

housing allowances will affect the rents of all tenants regardless of their recipient status. Therefore, comparing the rent development of different household groups (treated and untreated) will underestimate the effect of housing allowances on rents.[111] To date, there are no reliable assessments on the effects of the social housing and housing allowance programs on the overall rent level in the Finnish context.

The above discussion assumed a fixed housing stock. However, social housing construction may directly influence the overall housing supply. It is likely, however, that in densely populated urban areas, subsidies to social housing construction lead to substantial crowding-out of private construction. On the other hand, by increasing housing demand, both housing allowances and social housing may affect municipal decisions on land use. These indirect effects on housing supply are difficult to identify and further complicate the assessment of the subsidies on the overall rental level.

5 Conclusions

I have discussed housing policies, especially housing allowances and non-profit (or social) housing, their rationale from the point of view of low-income households, and their design in the Nordic countries. In discussing the effects of the programs, I focused on evidence from Finland. Four general conclusions can be made.

First, housing costs can be reduced either by housing benefits or vouchers, or by supplying housing with below market rents. Both alternatives will improve the living standards of the recipient households. Other things equal, they leave the recipients with more disposable income for non-durable consumption. However, both also incur costs for the taxpayer, direct budgetary costs in the case of housing benefits and foregone revenue in the case of social housing.

Second, the overall effects of the programs do not directly follow from the stated objectives. The effects are typically complicated and difficult to establish reliably. The details of implementation will determine whether programs based on quite distinct principles lead to different distributions of benefits. It seems, for instance, that the distribution of tenant characteristics in Swedish municipal housing and Finnish social housing are more similar than the principles and stated objectives of the programs might suggest.

Third, a difficult tension is built into the social housing programs. On the one hand, there is a clear justification for directing public support to low-income and vulnerable households. On the other hand, one may want to avoid creating neighbourhoods with a high concentration of disadvantaged households. Changes over time in the program rules and location of non-profit housing reflect changes in the awareness of this tension.

As housing costs in sought-after neighbourhoods in growing cities continue to increase, this tension will become more difficult in the future. True and sustainable

111. For instance, Gibbons and Manning (2006) use differences in the share of recipient households in different regions to assess the general equilibrium effects of housing allowance in the UK.

affordability is more likely to come in the form of increased overall housing supply than subsidized demand, be it through below market rents or housing allowances. All housing construction is useful in this respect and will benefit the low-income households due to the filtering effect, since increased supply will serve to lower the cost of housing generally. Insufficient construction in growing housing market areas is a distinct problem from providing housing subsidies for low-income households. These two issues call for different types of solutions.

Finally, most research on low-income housing programs focuses on the program participants. However, programs that seek to change the supply side of the housing market or the distribution of low-income families across neighbourhoods presumably affect also non-participants through channels other than the tax burden associated with financing the programs. These effects operate through demand and supply responses in the housing market, affect housing prices, rents, and residential sorting. Research on the indirect and sometimes potentially unintended consequences of these programs would be highly useful for the design of the programs in the future.

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