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EXAMINING PUBLIC POLICY AND PROPERTY MARKETS

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David Adams¹, Craig Watkins² and Michael White³

INTRODUCTION

It is widely accepted that the performance of housing and commercial property markets has a profound impact on the social and economic well-being of our towns and cities. Property markets perform an important role as mediators of urban economic change (Gibb *et al.*, 2002). The location of property development can enhance or inhibit the competitiveness of cities and regions (Begg, 2002). In addition, through its influence on the locational pattern of homes, employment opportunities, factors of production and the urban asset base, property plays an important role in the spatial distribution of social justice (Gibb and Hoesli, 2003).

It is thus no surprise that policy makers place particular importance on seeking to influence the performance of markets. Examples of governance strategies include the regulation of markets through the planning system, direct development channelled through land policy and regeneration initiatives, and indirect influences on the behaviour of property institutions through taxation and fiscal mechanisms. Although more difficult to detect, public sector decisions on transport infrastructure, public service provision, education, and crime also influence the structure of the property markets. Household and business location decisions, and property development and investment strategies will all be shaped directly or indirectly by a myriad of policy initiatives.

There are currently numerous highly topical policy issues occupying the minds of the general public and the property community. The recent Barker Review, for instance, has focused on the role of government policy, especially planning policies, in tackling rapid price appreciation and volatility in the housing market (Barker, 2003; 2004). Interestingly, the review was the responsibility of both the Treasury and the Office of the Deputy Prime Minister (which has general responsibility for housing and planning). This reflected the fact that it was a fundamental premise of the review that the instability of property markets in the UK has important macroeconomic consequences. As expected, Barker's policy prescriptions highlight the need to reform the planning system. In addition, however, it is proposed that policy makers might consider alterations to the role of taxation mechanisms, the provision of infrastructure incentives, and reform of the construction industry. While these policy recommendations have received mixed reviews, the report ably demonstrates the difficulty associated with analysing the impact of public policies on the performance of property markets.

These are not the only property-related policy areas subject to debate at present. Elsewhere, the property market impacts of congestion charging have been contested. Others have debated the likely property market ramifications of investment in the public transport system, especially the £10 billion east-west London Crossrail initiative (RICS and ODPM, 2002). There has also been

¹ University of Glasgow - david.adams@glasgow.ac.uk

² University of Sheffield - c.a.watkins@sheffield.ac.uk

³ Now at Nottingham Trent University - michael.white@ntu.ac.uk

speculation about the likely impact of proposals to provide tax incentives for the formation of Property Investment Funds (HM Treasury, 2004). The simple message from this brief review is that, for a variety of economic and social reasons, the relationship between public policy and the structure and operation of property markets is important.

Unfortunately, however, these relationships not well understood. While some policy issues have been subject to rigorous analysis, the extent to which initiatives and interventions in property markets have been informed by evidence is fairly limited. As we argue later in the book, this is somewhat disappointing given the considerable developments, both in terms of quality and quantity, in the property research agenda.

Nevertheless, there are grounds for optimism. In recent years, it has become evident that policy-makers see a much closer relationship emerging between public policy, including the planning system, and property development, in which they are regarded less as working in opposite directions but more in synergy with each other. In this context, this book is intended to provide an introduction to 'state of the art' research on the relationship between planning, public policy and property markets. Importantly, the contributors to the volume recognise that policy makers cannot rely on either the state or market alone to deliver policy objectives. Nor are they faced with straightforward choices between resolving government failure or market failure. Rather, successful public policy requires an appreciation of the role of the state as a participant in the market (Oxley, 2004). Thus, although the book focuses on the impact of planning, housing, land, regeneration and transport policies on land and property markets, it begins to explore not just the direct impacts of policy on supply, demand and market pricing but also examines the role of market information, institutions and actors in meeting policy objectives.

THE SCOPE OF THE BOOK

This book is concerned with the relationship between planning, public policy and structure and operation of property markets and is relatively broad in scope. Our interest in property markets covers all sectors (residential, office, retail and industrial) as well as the structures, institutions and processes that characterise the market and shape market outcomes. The analysis contained in the book explores the role of policy in the determination of property values, investment returns and levels of development activity. It also considers the behaviour and interaction between a variety of actors including public agencies, planners, developers, investors and property users.

Our use of the term planning in the title is reflective of the relatively high profile of current controversies associated with the relationship between planning and property markets. In the context of this text, 'planning' is thought of in much broader terms than its statutory functions. Indeed, following Adams *et al.* (2003), the conception of planning relates to the intentional interventions in market processes, usually (but not exclusively) by local government, in the pursuit of societal objectives. In this sense, the scope of the book is broader than that of many economic analyses where the focus has tended to be on land use regulation (see Evans, 2003). This broad definition of 'planning' is indicative of an interest in public policy more generally and thus includes all land, land use planning, housing, transport and regeneration policies that are likely to have clear impacts on the use, investment and development of land and property. It is also consistent with the government view of the function of planning which highlights the role of the planning system in maintaining economic growth and in providing investment and jobs as well as homes and buildings.

Clearly, given the breadth of the subject matter, it is difficult comprehensively to cover all relevant current and recent research on the topic. Instead, the treatment of policy debates and market

sectors is necessarily selective. We do not attempt to tackle all policy issues, nor do we not seek to explore all sectors of the property market in equal depth. There are thus some obvious gaps in coverage. For instance, none of our chapters is concerned with the private rented housing market, even though buy-to-let policies and proposals for Real Estate Investment Trust (REIT) style vehicles are having important impacts on market performance. Nor do we focus explicitly on prominent housing policy issues such as Right to Buy. Instead our intention is to provide a flavour of contemporary issues in property research rather than an exhaustive treatment of all important topics.

This is reflected in a much more pronounced concern with methodological debates and research methods that are relevant to the ways in which policy impacts on property. Analyses of particular policy initiatives and programmes are thus intended to be illustrative and are used to exemplify particular methodological and analytical approaches. Nevertheless, this approach enables the book to provide an overview of the available research evidence on a number of important policy questions.

PROPERTY RESEARCH AND PUBLIC POLICY

One of the main aims of the book is to demonstrate that property research can make important contributions to understanding public policy and its influence on urban dynamics. We argue that the maturing property research community now produces high quality research based on sound theoretical foundations, useable models and diverse research methods. This reflects the evolution of an increasingly coherent research agenda that has been enhanced by improved communication across disciplines and specialisms.

Although the pioneers of classical and neo-classical economics often investigated land and housing market issues, it is only since the 1970s that a distinct property research community has emerged in the UK (O'Sullivan and Gibb, 2003). This research drew initially on the traditional property-related disciplines of economics, law, human geography, urban planning, construction and valuation. More recently, research output has begun to mirror trends in the US by encompassing advancements in business studies and finance.

The diverse backgrounds of property researchers and practitioners has inevitably led to a fragmented research agenda characterised by a range of quasi-independent specialisms in areas such as urban economics, housing economics, property investment and finance, property valuation, property and the macroeconomy, property and business economics, and planning and property development. Indeed, until relatively recently, there has been only limited cross-fertilisation between housing economics and commercial property market analysis and between economic analysis and planning research.

Within each of the relatively narrow specialisms that emerged, the focus of research has varied from individual actors, through groups of actors to the market in aggregate; from the local to the national to the global dimension; from the demand side to the supply side; from the public sector to the private sector; and across the residential, retail, office and industrial sectors. Furthermore, theoretical and empirical studies of property market phenomena have also varied in terms of the methodological and epistemological approaches adopted (Adair *et al.*, 2003).

Encouragingly, however, there have been several initiatives, which have helped facilitate greater communication between property sub-specialisms. For instance, between 1998 and 2000, the ESRC funded a Property Economics and Finance Seminar Group. This group held four meetings on diverse themes including housing economics, urban regeneration, property investment and

corporate real estate. Although the group helped establish links between housing and commercial property researchers, much of its activities focused on the role of property as a financial and corporate asset rather than as a mediator of urban economic and social change.

More recently, an ESRC funded Planning and Development seminar group has been established. This group has a more explicit interest in public policy issues and has sought to foster interaction between property, housing and planning researchers. The first meeting of the group, hosted in September 2003 by the Department of Land Economy at the University of Aberdeen, focused on the relationship between planning, public policy and property markets. The meeting built on growing interest in this topic and provided the impetus for this book.

In an interesting precursor to the establishment of the ESRC Planning and Development seminar series, Guy and Henneberry (2002a) edited a collection of papers on property development. The collection had been inspired by multi-disciplinary discussions of the development process at the annual Royal Institution of Chartered Surveyors (RICS) conferences in 1994 and 1998 and sought to demonstrate the heterogeneous nature of research on property development. The resulting book included contributions from a variety of disciplines and the editors explicitly considered the ways in which different methodological perspectives on property have framed analyses of the development process. They suggest that the 'interpretative flexibility' relating to the built environment gives rise to the use of diverse theories (and associated research methods) when formal, analytical attempts are made to explain development. This diversity has generated considerable debate about the competing merits of alternative methodological approaches. It has also encouraged ongoing debate about the value of particular research methods.

Superficially, it may appear that this debate has been won by the mainstream. Recent analyses of leading property economics journals show that journal publications have been dominated by the quantitative model building (Newell *et al.*, 2001; Ong *et al.*, 2001). This is particularly evident in the major US academic journals, where housing and commercial property are primarily analysed within an asset market framework (Levy and Henry, 2003). However, this masks some underlying concerns with mainstream economics. Schiller (2001, p. 4), for instance, notes that "economic man may still exist, minimising cost and maximising utility, but he gives only part of the picture".

In the UK, the broader social science perspective adopted by several leading journals has allowed academics to continue to debate the merits of alternative approaches (see Guy and Henneberry, 2000; Ball, 2002, for instance). Furthermore, the case for considering alternative perspectives less as competitors and more as complements has received considerable support (Adams *et al.*, 2003; Monk and Whitehead, 1999; Lizieri, 1995).

As Guy and Henneberry (2002b, p299) state "instead of trying to shoe-horn property research into competing disciplinary models or prioritising methodological approaches, we might begin to take a more heterogeneous route (or routes) in the future. While this would not mean abandoning critical debate between analytical approaches, it would mean adopting a more catholic community of property researchers with some parity of esteem. The effect of this would be to open property studies to a much wider world of analytical innovation."

It is hoped that this book will make a further contribution to this progressive view of property research. Although the book is dominated by the work of property economists it is no less supportive of the need for pluralist approaches to property research. Indeed, methodological diversity is seen as an essential ingredient in the improved analysis of the influence of public policy on commercial and residential property markets.

STRUCTURE OF THE BOOK

As we note above, the book focuses on theory and methods rather than policy themes or disciplines. This is reflected in the structure of the book. There are a further three sections to the text.

Section 2 introduces some of the contemporary debates in conceptualising the relationship between the state and the market. In three chapters, this section explores the range of theoretical approaches that inform property and planning researchers' studies of the relationship between public policies and property markets. In chapter two, David Adams, Neil Dunse and Michael White examine the methodological scope of mainstream economic analyses, which encompasses neo-classical and welfare economics. Although the authors highlight the limitations of the approach, especially in terms of its restrictive and unrealistic behavioural assumptions, they balance this by pointing to important developments in modelling approaches, especially with respect to modelling adjustment processes, choice and spatial phenomena, as well as advancements in information and search theory.

In chapter three, the same authors explore role for various forms of institutional economic analysis, including new institutional economics and more radical 'political economy of institutionalism' perspectives. Although it is established that, in overcoming the restrictions of mainstream approaches, institutional analyses has the potential to provide a fruitful basis for land and property market studies, the authors also acknowledge that empirical studies can tend towards description or 'story telling' Ultimately, Adams *et al.* conclude that what is required is greater methodological pluralism. This is a sentiment that is given strong support by the quality of insights derived from the diverse approaches employed in the empirical studies contained within this text.

The fourth chapter seeks to link the conceptual and empirical issues. Steven Tiesdell and Philip Allmendinger develop a typology of 'planning' tools based on their relationship to the operation of land and property markets. The taxonomy proposes four types of planning tool – those intended to shape markets, those intended to regulate markets, those intended to stimulate markets and those directed at developing the capacity of market participants. The typology draws out the main relationships between public policy and property markets identified in mainstream and institutional economic analyses.

Section 3 is the largest part of the book. It provides examples of empirical work consistent with the main theoretical traditions. Much of the work included in this part of the book has been undertaken with the support of research councils, government departments or charitable trusts and has been produced with the specific aim of contributing evidence to contemporary policy debates. In line with current policy concerns, the contributions provide further evidence of the level of interest in themes such as the effect of policies on property *market outcomes* and, in particular, property values; and the extent to which policies can alter *market processes* and help correct market failure through, for instance, assisting in the delivery of non-market homes, in facilitating the redevelopment of inner city areas and in shaping the nature and form of development in suburban growth areas.

Although these studies do not reflect the totality of work on public policy and property markets, they demonstrate the diversity of research methods used in applied research. As such the section is further sub-divided to highlight the approaches to developing economic models of the relationships between policy change and markets, to measuring and monitoring market performance and to using surveys, qualitative methods and detailed case studies to analyse market behaviour.

Chapters five and six provide examples of attempts to model the relationship between land use planning and property values. Both studies exemplify current advancements in the development of quantitative economic models in the mainstream tradition. Glen Bramley and Chris Leishman focus on modelling outcomes in the residential property market. Although housing economists have long been concerned with the theoretical impacts of planning and other public interventions on the market, it is only in the last fifteen years that these impacts have been empirically estimated. This chapter builds on a substantial body of previous work on the topic (including Bramley, 1993a; Bramley, 1999). It uses a panel data set to develop a system of equations, within a long run equilibrium framework, to estimate the impact of different packages of public policies on a range of outcomes including the price and quantity of housing in 'high' and 'low' demand housing markets. The model also allows the authors to simulate the effects of policy changes, such as an increase in the level of building, over a seven-year period from the end of 1997. The results suggest that a combination of supply-side and demand-side (through the local economy and labour market) policies could achieve substantial impacts on the price of housing and quantity of new development.

John Henneberry, Fotis Mouzakis and Tony McGough model the commercial and industrial property markets. Although a significant literature on the effects of land use regulation on housing markets has emerged in recent years, there has been very little attention paid to the regulatory impacts on commercial markets. This chapter reports on what is to date the most systematic attempt to address this issue. The authors develop models of rental values and development output based on a system of equations covering the industrial, retail and office sectors of the property market over the 1998-2000 period. In the model, a proxy variable is constructed to represent the planning regime. The variable measures the proportion of planning decisions that are approvals. The behaviour of the variable implies that as planning regimes become tighter the percentage of approvals decreases and so does the local property supply. These lower levels of supply are in turn associated with higher rents and lower levels of local economic activity.

The next two chapters move from model building to the indirect measurement of the impact of policies on property values. Neil Dunse and Colin Jones illustrate the use of hedonic methods in computing the 'shadow' or implicit price of public sector infrastructural improvements. The chapter has its intellectual roots in a voluminous mainstream urban economics literature that has long been concerned with the way that transport systems, land use, and residential and business location are inter-twined (Evans, 2003). The empirical work in the chapter derives from the approach used by researchers seeking to unpick the effects of public policy decisions, including the location of new airports and light rail systems on property values. The study's novelty is associated with the focus on the industrial property market rather than the housing market. The application of this mode of analysis to commercial and industrial property markets has largely been precluded by the paucity of good quality local market data (Dunse *et al.*, 1998). The chapter shows that, in the contemporary industrial property market context, access to transport links is likely to have a more pronounced effect on rental structures than access to the market place. Thus, importantly for economic development policies, access to motorway networks dominates the locational choices of manufacturers.

In chapter eight, Alastair Adair, Jim Berry, Kenneth Gibb, Norman Hutchison, Stanley McGreal and Craig Watkins seek to measure the impact of urban regeneration policies on the performance of commercial and industrial property markets. The authors construct indices that measure property rents, returns and yield movements in areas of the property market that have been subject to urban regeneration interventions. The indices are constructed using a 'bottom up' method based on detailed field visits during which regeneration areas were delineated and individual property

offering identified. These properties acted as a sampling frame for the collation of market data from a variety of sources including a survey of valuers and property industry datasets. Ultimately, the performance of the regeneration indices is compared with that of the industry standard benchmarks typically consulted by the property investors. The research found that, contrary to the common perception that regeneration areas are characterised by high risk and low returns (Adair *et al.*, 1999), regeneration areas have outperformed prime markets since the early 1990s.

The next three chapters (which make up section 4) are less reliant on quantitative methods. In chapter nine, Chris Leishman and Fran Warren undertake a detailed exploration of the influences on demand for new housing. It is clear that, if the levels of new housing required are to be met, then significant numbers of new homes will need to be built. The development of these homes will need to be consistent with sustainable urban forms. However, little is understood about the levels of consumer satisfaction with new housing development. The chapter introduces research methods that are borrowed, in part, from psychology in that it experiments with use of visual images as part of a survey of consumers. It combines the survey results with the use of more conventional statistical techniques and concludes that housebuilders need to address numerous sources of dissatisfaction in order to establish strategies for the delivery of sustainable housing developments. Unless this happens, there will be an increasingly difficult mismatch between the requirements of house buyers and the dwellings offered – a challenge that may require the intervention of policy makers.

Chapter ten, by Sarah Monk, Christina Short and Christine Whitehead, explores the role of the planning system in the delivery of affordable housing. They note that, in a marked departure from past approaches, the planning system locates social rented housing on the same development sites as new homes built for owner occupation. Thus the policy makes an explicit link between land use planning and both the financing of affordable homes and the desire to establish mixed tenure developments. The chapter considers the effectiveness of the system on the basis of evidence collated from a survey of local authority planning departments, face-to-face interviews with planning and housing officers and detailed examination of housing development sites. The research shows that the volume of housing provided is low relative to levels of need and that the majority of housing provision is not adding to the level of supply. Although there is a suggestion that the policy is now becoming widely accepted, the research also stresses difficulties associated with the negotiation process, and inconsistencies in the behaviour of public and private sector actors. The authors conclude by highlighting the extent to which the efficacy of the policy is linked to the level of market provision. They note that the system will not provide affordable homes in the numbers required if the current low levels of development activity prevail.

In chapter eleven, Gwyndaf Williams and Stuart Batho examine the capacity of a city to respond to urban property market challenges using a range of urban redevelopment delivery mechanisms. The analysis is based on a detailed case study of the renewal of Manchester city centre in the wake of the IRA bombing in June 1996. The study explores local capacities for enhancing city competitiveness in a five-year period of intense renewal and development activity. In the context of this volume, the chapter provides a uniquely detailed examination of the processes through which governance and urban economic change shape the built environment, influencing the direction and flow of investment and nature and rate of development activity. The authors highlight the opportunistic, pragmatic and entrepreneurial behaviour of key actors, notably those in the public sector. The analysis invites us to consider the extent to which the lessons from Manchester's renewal are transferable to other urban policy challenges.

In the fifth and final section of the book, the editors provide some comments on contemporary challenges faced by planning and property researchers and on the future direction of research into

the relations between the state and the (land and property) market. There are several messages. First, it is clear that we do not face simple choices between state and market solutions – or even between state failure and market failure. Rather the studies reported in this book provide clear evidence that the state must participate in the market. Second, the book highlights the progress being made in property research. We call for increased methodological pluralism and point to the diverse insights that can be derived and drawn together from the vast array of social science research methods and improved data that the property research community now has at its disposal. Finally, we would hope that the book demonstrates that the theories, models and empirical evidence collated by property researchers have an important role to play in improving the quality of public policy. There is clearly considerable attention being paid to developing useable models and to locating the analysis of policy impacts within its institutional context.

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