

**A Tenure Choice Look at the
Portuguese Housing Market
in the eighties**

Rui Nuno Baleiras
Working Paper Nº 160

UNIVERSIDADE NOVA DE LISBOA
Faculdade de Economia
Trav. de Estevão Pinto - Campolide
1000 LISBOA
PORTUGAL

Outubro, 1990

A TENURE CHOICE LOOK
AT THE PORTUGUESE HOUSING MARKET
in the eighties

Rui Nuno Baleiras

Universidade Nova de Lisboa
Department of Economics

Lisbon - Portugal

October 1990

**A TENURE CHOICE LOOK
AT THE PORTUGUESE HOUSING MARKET
in the eighties**

**Rui Nuno Baleiras
Universidade Nova de Lisboa - Department of
Economics**

Lisbon - Portugal

An earlier version of this paper was presented at a workshop on European Housing Systems held at and promoted by the University of Bristol - School for Advanced Urban Studies. Such reference is listed as Baleiras (1990). Comments from participants are gratefully acknowledged. A special thank is owed to Dr. Will Bartlett for his definite encouragement. Remaining errors, of course, are my own.

ABSTRACT

A critical survey of the Portuguese housing market in the eighties is attempted in this paper, through the analysis of playing demand and supply tenure choice determinants. Some suitable policy recommendations are formulated; their effective implementation will not require a significant change on the degree of public intervention in the housing market, which has traditionally been low in Portugal when judged by European standards.

KEYWORDS: demand for and supply of housing, tenure choice, owner-occupancy, renting, mortgage loans, income taxation and mortgage interest, capital gains taxation, renting contracts, housing policy, Portuguese housing market.

TABLE OF CONTENTS

<u>Topic</u>	<u>Page</u>
Abstract	3
Table of Contents	4
1. Introduction	5
2. Tenure choice determinants - demand side	7
2.1. Housing tenure choice nature	7
2.2. Capital gains and their taxation	9
2.3. Implicit rental rate tax treatment	11
2.4. Mortgage loans	12
2.5. Income tax	14
3. Tenure choice determinants - supply side (brief analysis)	16
4. Overall housing policy assessment	19
5. Prospects for future governmental initiative	21
References	23
Data sources	25

1. INTRODUCTION

It is this paper's goal to use the housing tenure choice topic as a vehicle to present some of the major current features of the Portuguese housing market and policy.

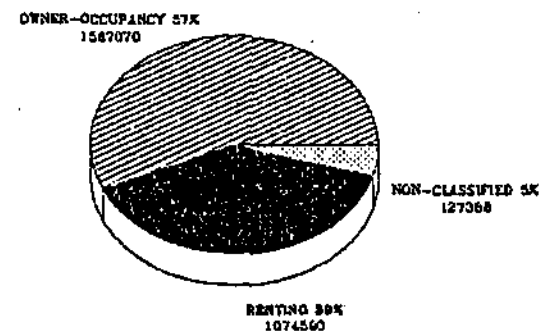
The reader may wonder why using such indirect expositional strategy rather than plainly describing the housing market. There are two reasons for adopting this strategy. First, consideration for the reader's patience and intelligence: we do not want to easily tire him (her) with an annoying, simple newspaper-style factual description of reality; therefore, an analytic, critical and selective featuring of market conditions will be attempted. Second, previous research work on tenure choice by ourselves has probably biased the exposition that follows.

The usual approach to housing tenure choice deals only with the demand side. However, the approach we try here will consider both sides of the market. Nevertheless, consumer's view will dominate the text quantitatively perhaps because we have worked on it recently. The binding time constraint will force us to focus the following discussion on the intuition lying behind several theoretical results developed elsewhere, setting aside their technical details. For a comprehensive treatment of demand considerations, please refer to Baleiras (1989), which will be recommended later on as the background paper to section 2. But, as mentioned above, we will also deal with supply-side considerations. Besides, in the Portuguese case their analysis is easier than that concerning demand; in particular, policy implications are much more clear and less ambiguous than those acting through demand channels.

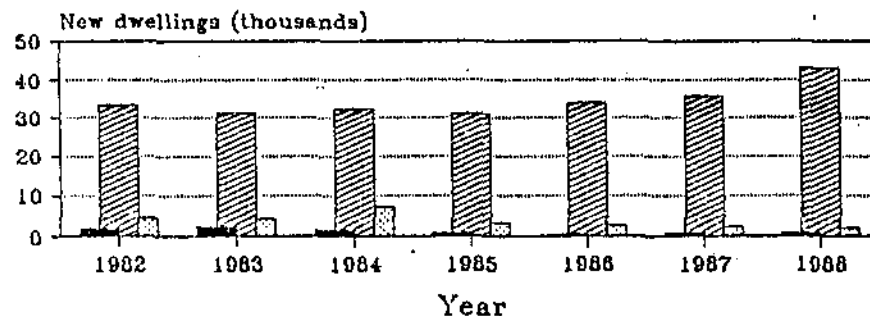
A glance over chart 1 panels will prove instructive about the general message this paper will try to transmit: the increasing size of owner-occupied dwelling stock (panels 1A and 1C) and the virtual collapse of renting-purpose housing production in the eighties (panel 1B). It will be clear from this article that "one family - one owner" has been the major policy aim since 1976 when the current mortgage loan system was launched.

Chart 1: PORTUGUESE HOUSING - TENURE BREAKDOWN

Panel 1A: 1981 DWELLING STOCK Composition

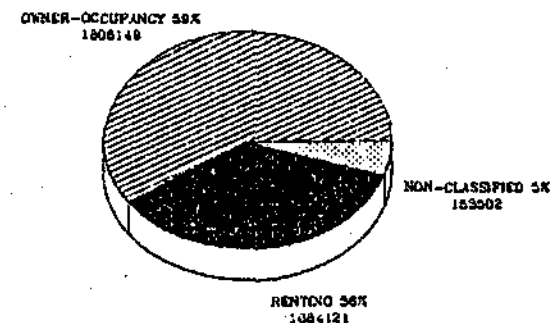


Panel 1B: HOUSING SUPPLY Yearly Flows



Legend
 Renting Owner-occupancy Non-classified

Panel 1C: 1988 DWELLING STOCK Composition



Estimated composition
 Demolition data is not available

Chart 1

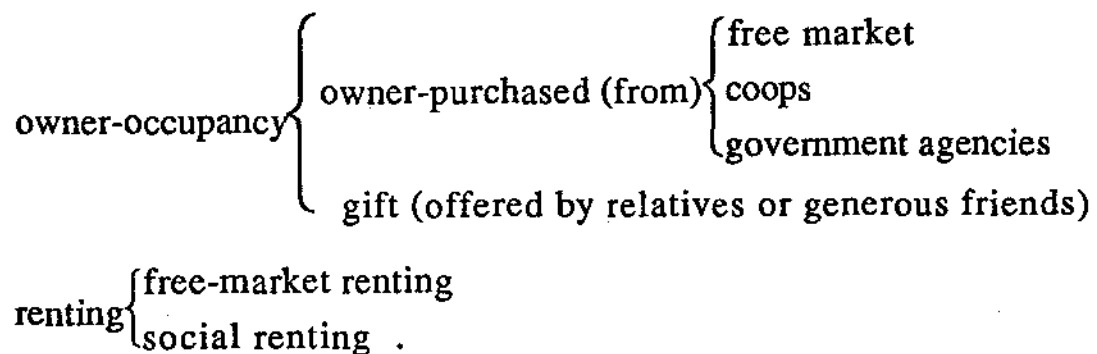
Basic data: INE (1 and 2).
 Author's own tenure classification.

This text is organized as follows. Section 2 looks at consumers' motives for choosing one tenure rather than the other. As explained before, we will not attempt at showing rigorously the playing mechanisms determining that choice [the interested reader is urged to see Baleiras (1989) or any reference mentioned therein]; rather we will try to give a clear intuition about their flavour. The determinants to be considered (refer to the table of contents) will not exhaust the list of elements potentially affecting tenure choice. An account of important supply-side forces will be presented on section 3. The treatment will be necessarily brief due to space lackness but this by no means intends at recognizing proeminency to the demand role. Many market reactions to be examined so far are stimulated by government initiative; therefore, section 4 will try to summarize and assess housing policy. To close the paper, section 5 will present policy vectors arising from previous discussion as desirable goals and will try to sketch likely future government action.

2. TENURE CHOICE DETERMINANTS - DEMAND SIDE¹

2.1. HOUSING TENURE CHOICE NATURE

1. Housing services can be consumed out of two tenures: owner-occupancy and renting: These tenures can be partitioned into several other categories. The following breakdown is an instructive example.



Our discussion in this section will evolve around the relative size of both tenures in Portugal and some disperse references to their partition will be made occasionally.

2. In this section, we analyse the user of housing services (consumer)'s perspective, that is, the demand side. When a household decides whether or not to enter the market he (or she) must choose the tenure under which he (she) is going to consume such services.

Owner-occupancy or renting: which tenure should he (she) choose?

The answer economists give is simple: the household should choose the housing tenure that pleases him the most, given the constraints facing such choice. Basically, these constraints are budgetary, one for each lifetime period. But, of course, other limitations restrain feasible choices, like institutional features of the market (legal nature of renting contracts, for instance, may be very important and, in fact, this is actually the case in

¹ All arguments whose intuition is sketched in this section are rigorously elaborated in the background paper we referred to above: Baleiras (1989).

Portugal). Deutsch and Schöpp (1990) is a remarkable example of how careful one should be about modelling choice constraints.

3. On what follows, let us look into the owner-occupancy tenure through the owner-purchasing (or building) gateway: this is empirically the most relevant one.

Therefore, there is a price associated to the owner-occupancy regime and a rental rate (rent, for short) associated to the renting tenure:

Price (P)_____ owner-occupancy

Rent (R)_____ renting .

A price is paid by the owner-occupant at the beginning of his economic lifetime and a (eventually different) price is received by him at the end of such lifetime when he sells his dwelling. A rent is paid every period to the landlord.

These two nominal variables are linked, however, by an arbitrage process performed by landlords competition.

Landlords are required if one wants to consider the renting tenure. They play an intermediation role between constructors/real estate promoters and potential tenants. Basically, they buy homes at price P, rent them for several periods at R and eventually sell off somewhere in the future. Profit-maximizing behaviour is expected to bound these activities.

If a large number of landlords exists, market competition will tend to drive discounted profits of all active landlords to zero. If this happens (and there are solid grounds in economic theory to expect so), a communication, a bridge between owner-occupancy and renting is established: P and R are linked together by the arbitrage condition (an increase in P will lead to a rise in R and vice-versa). The two tenures are nothing else than two segments of the same market, housing.

Let us now discuss the influence of several disturbances on housing tenure choice, bearing in mind these preliminary considerations.

2.2. CAPITAL GAINS AND THEIR TAXATION

Housing is a consumable asset; as such, it offers two kinds of return to its owner: appreciation and rental rate. Let us first explore the effects of the former.

1. Like any financial asset, housing capital gains can be either positive or negative and are uncertain at the purchasing moment. So, there is a risk associated to home holding; the selling (future) value of this asset may be higher or lower than the buying (current) price.

If the typical household is risk-averter, then random capital gains will divert him away from ownership; *ceteris paribus*, he (she) will be better-off as tenant.² Hence, if housing is a risky asset (that is, if the standard deviation of its future price is non-zero) a rational household will prefer to rent rather than to buy.

Is this theoretical result supported by Portuguese recent data? At a first thought, NO! Just remember the huge superiority of owner-occupancy weight "vis-à-vis" that of renting during the eighties... But let us assess reality in a deeper way. Thus, consider chart 2.

There are no data at all on housing capital gains since successive transactions of a particular dwelling are not observed. Therefore, we looked for a proxy variable and found that the price trend of new, first-hand houses can perform an indicative role. As an example, we picked up available information on T3 dwellings located in the metropolitan regions of Lisbon and Oporto.³ Personal feeling based on actual home-search performed recently (but hardly proofable, unfortunately) leads us to evaluate reported bars and lines as undervaluing true appreciation, particularly in recent years [a 30%-35% nominal appreciation "per annum"]

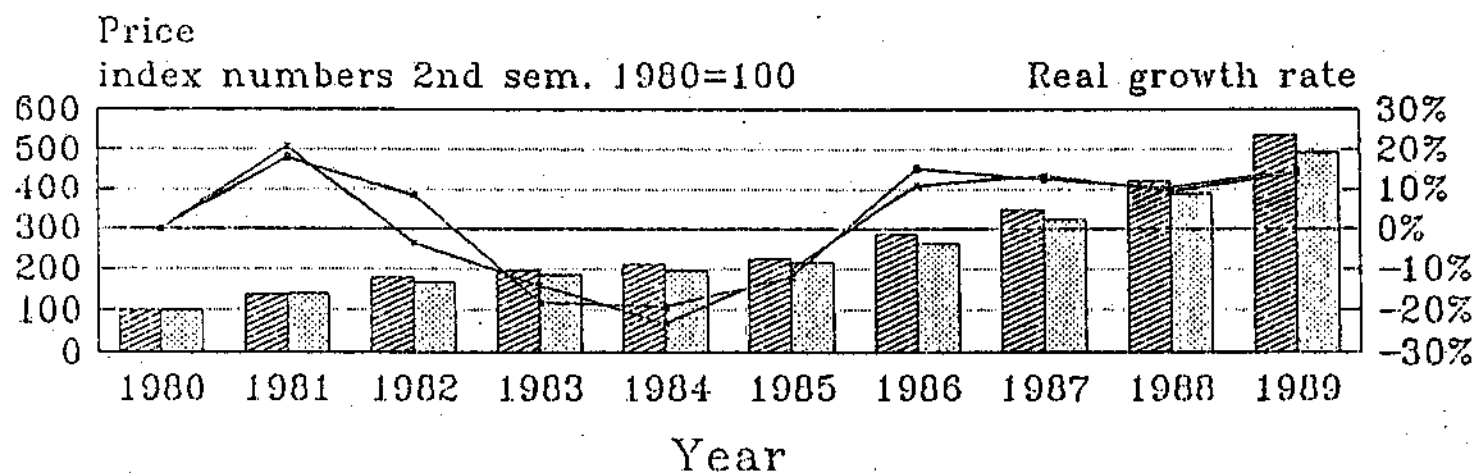
² Choice analysis in an uncertain environment is discussed in many background references. The derivation of the above result draws significantly on insurance contracts as presented by the well known Varian (1984, pp. 161-2) and Laffont's (1985, p. 106) graduate textbooks.

³ T3: three bedroom + one larger room housing unit. Information on other regions of Portugal is gratefully acknowledged. Chart 2 background data were constructed by MOPTC (2) from newspaper advertisements.

Chart 2: NEW HOME PRICE TRENDS

Example of T3 dwellings

in Lisbon and Oporto metropolitan areas



Legend

Lis cur. price index Opo cur. price index
 Lis real growth rate Opo real growth rate

Price deflators: CPI without housing expenditure, respective city.
 Basic data: INE (3) and MOPTC (2).

has been quite common on in-(Lisbon) city first-hand housing investments for the last three years].⁴

Despite the arguable quality of presented data, evidence seems strong enough to suggest that recent Portuguese housing capital gains are reasonably well predictable, consistently reporting positive real appreciation year after year. Deterministic modelling of such variable thus seems more appropriate. Doing so, we find no clear-cut preference for any tenure.

Everything else the same, the consumer is indifferent between both tenures.⁵ Therefore, if we want to explain the definite preference for owner-occupancy in the eighties, we have to look for a different reason.

2. Can capital gains taxation provide a preference for owner-occupancy?

Typically, existing taxes are linear because they are a first-order proportion of capital gains. The relevant shock variable for families is now the net or after-tax capital gain. A tax like this reduces expected appreciation but also the risk inherent to this asset's price (in fact, fluctuation of capital gain around its mean value is softened by the fiscal instrument. The tax provides an insurance against price fluctuation whose coverage is higher the higher is the tax rate; interpreted this way, the tax leads to risk-sharing between household and government.⁶

Therefore, when a proportional tax is levied (or its rate is raised) ownership becomes relatively more attractive if the capital gain is stochastic but does not destroy tenure indifference if it is a deterministic variable.

⁴ As a by-product of our data collection we found that housing prices have increased faster than construction costs (opportunity cost of capital not accounted for) during the last decade - see chart 3. Is this a signal of demand-pull housing inflation or declining productivity?

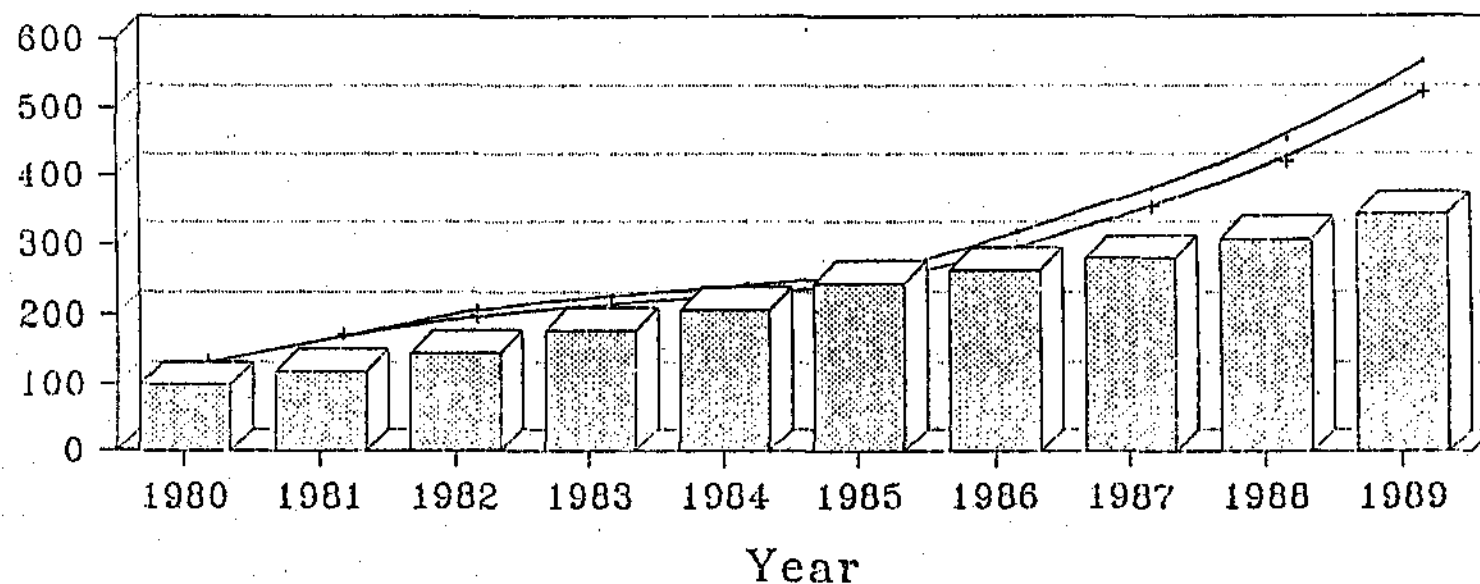
⁵ Why? A certain capital gain affects all home owners, and landlords in particular. A known, positive appreciation allows the typical landlord to reduce the rent and still make the same profit. So, through landlords competition, a sure appreciation affects both home owners and tenants the same way.

⁶ A somewhat analogous result can be found in Finance literature concerning demand of financial assets and taxation of their appreciation. Using Tobin's general equilibrium asset model, this is shown in Baleiras (1988).

Chart 3: SELLING PRICE AND CONSTRUCTION COST (T3 Dwellings)

Lisbon and Oporto metropolitan areas

Index number
2nd sem. 1980=100



Legend

— Lisbon price

- - - Oporto price

■ Construction cost

Basic data: MOPTC (1 and 2).

What can Portuguese experience tell us about this?⁷

Until the end of 1988, there were no taxes on assets appreciation. The 1989 Income Tax Reform introduced this instrument. Hence, during the absence of this tax tool and given the pro-deterministic nature of capital gains, the government had been neutral "vis-à-vis" tenure choice. Given the low risk profile revealed by housing investment in recent years, the 1989 Income Tax Reform maintained a neutral effect on tenure choice but its distortionary nature is likely to have reduced families (both owners and tenants)'s welfare.

A final remark: the capital gain neutrality result draws heavily on the assumption of landlord competition. As the number of such players is relatively small, this hypothesis seems awkward in the Portuguese case. If landlords have and exercise their market power, a rise in capital gains (or net capital gains) is not likely to reduce rents low enough so as to keep profits near zero. Thus, such rise on (net) capital gains is expected to clearly favour ownership tenure. Similarly, a tax rate increase may cause an overmatching rise in rents, hence shifting home searchers away from the renting tenure.

2.3. IMPLICIT RENTAL RATE TAX TREATMENT

As a consumable asset, housing provides services to its user and the price of such services is the rental rate. This rental rate (also known simply as rent) is explicit for tenants but implicit for owner-occupants. In this latter case, it should be interpreted as the opportunity cost of consuming rather than selling housing services produced by its owned dwelling.

Explicit rents are taxed in Portugal (their legal incidence lies upon landlords), although renting contracts with price ceilings (the so-called

⁷ Capital gain taxation on owner-occupied housing is still little known in practice at the international level. Even in countries where this instrument is more experienced, like Israel, the tax rate is below that applying to landlording appreciations, as reported in Weiss (1978, p. 51). There is no such tax in the UK, according to King (1980, p. 145), and, in the USA, housing resale gains are "almost" tax-free [explained in Manchester (1987, p. 108, note 6)]

"conditioned" rental contracts) may benefit from certain tax privileges.⁸ Implicit rents, however, are tax exempted. This asymmetry clearly invites ("ceteris paribus") a home searcher to become a home owner.

This conclusion, self-evident and stressed several times in the literature,⁹ seems compatible with the actual Portuguese trend of the eighties: a sharp preference for owner-occupancy.

2.4. MORTGAGE LOANS

1. Many actual credit markets exclude solvent customers because they do not recognize future income as a credible collateral. This exclusion distorts intertemporal choices consumers make and, as such, is a financial market imperfection.

The imperfection we are dealing with forces people to save (a non-negative amount of money) in the beginning of their economic lifetime (substantial inheritances not considered) and to postpone part of their current consumption wishes. This constraint is more active the shorter are funding availabilities in the market and, in general, hurts youth and low-income families relatively more.

This financial imperfection is certainly not the only one hampering house searchers but seems particularly relevant in countries where funding supply is scarce, like Portugal - where credit has been rationed for years. How does it affect consumers?

It requires a positive (or, more rigorously, a non-negative) saving in the present whichever tenure the typical household chooses. Since housing purchase in cash demands a greater initial disbursement than renting, we should expect at least youth and low income-families not to embrace ownership; in fact, it could formally be shown that renting will make them at least as well-off as ownership - see section 3 of Baleiras (1989).

⁸ See Law No. 46/85, of September 21 - in particular, art. 35. Conditioned rental contracts are also regulated by "Decreto-Lei" No. 13/86, of January 23.

⁹ Informal views can be found, for instance, in Henderson and Ioannides (1983, p. 109), Rosen et al. (1984, p. 405) and Arnott (1987, p. 984).

2. Although future income (and customers' honesty even less) is not, in general, recognized as collateral by the credit market, valuable physical goods usually do work as that. In fact, bank loans for housing purchase in most countries are granted on the basis of ownership transfer to creditor in case of debtor's default: mortgage loan. What effect does this financial instrument cause upon tenure choice?

The prospective tenant has no access to credit in order to finance his (her) consumption of housing services as long as the financial market does not acknowledge his (her) future income as a guarantee of solvency.

With no loan, the buyer would have to pay his home by cash at once and at the beginning of housing services consumption. The mortgage enables him to postpone, to defer payment into the future. Therefore, he may increase his present consumption and still make a positive saving. In fact, considering a certain dwelling that may be rented or bought, we could show with a bit of algebra that the initial (or what we call here "present") housing expenditure would be higher in the renting case - see section 4, in particular pages 26 to 28, of Baleiras (1989).

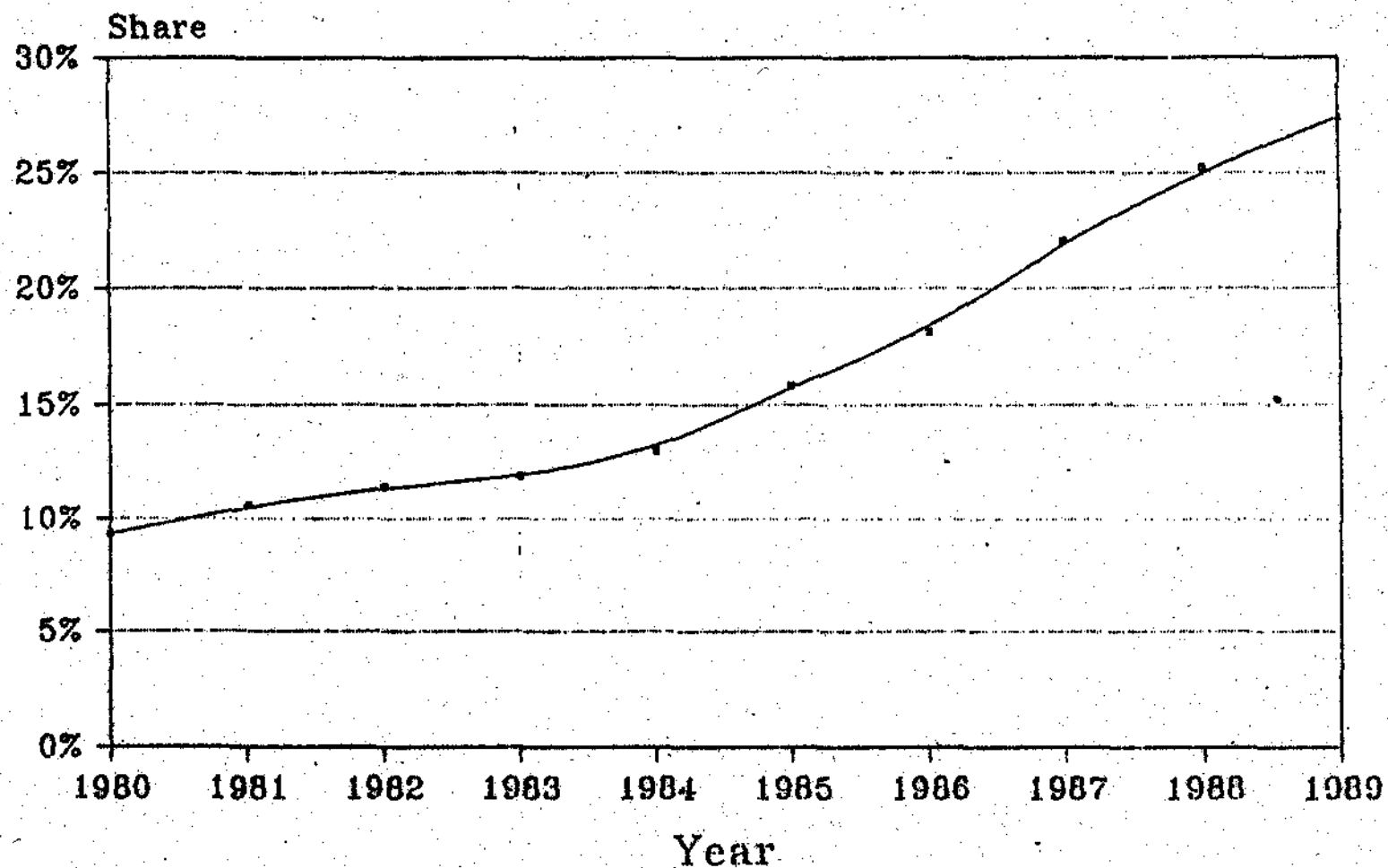
From this discussion we may now conclude that the mortgage loan favours ownership because it makes credit available to consumers, thus counteracting, in a sense, the saving boundary imposed by the financial market imperfection described above. Hence, home purchasing through borrowing offers individuals constrained by that imperfection the chance to increase their current consumption of non-housing goods, leaving unchanged their future consumption possibilities.

3. Portuguese experience in the eighties

As stated in the introduction, "one family - one owner" has been a primary goal of housing policy since mid-seventies. Mortgage loans have always been the prominent instrument to achieve this end, although not necessarily the most effective one [I may describe the key features of the current Portuguese mortgage loan system upon participants' request - an interesting account of the British-related mortgage system with insightful econometric remarks can be found in Atkinson et al. (1988)].

Chart 4 highlights the increasing size of mortgage loans to households during the last decade: in ten years the share has tripled!

Chart 4: MORTGAGE LOANS (HOUSEHOLDS)
Share on Total Domestic Credit



Basic data: MOPTC (1).

Simple statistical analysis confirms a close correlation between owner-occupancy dwelling purchases and loan market size: the partial correlation coefficient between house transactions value and the amount of loan contracts is 92.82%.

The next chart aims at pointing out what the credit market direction had been in the eighties. Despite its title, it is not an accurate indicator of excess demand for two reasons:

- i) requested loans and contracted credit should be expressed in monetary units rather than in number;
- ii) implicitly assumes that contracts signed on year t relate exclusively to requests submitted on the same period and this is not true (such unavoidable error was minimized by grouping data in two-year periods).

Despite these drawbacks, chart 5 gives a reasonable picture of what trends have the Portuguese mortgage loan market passed through.

The eighties are characterized by permanent excess demand and reasons for this pressure may already be found on our previous subsection discussions. Note the current convergence between demanders and suppliers intentions: high level of interest rates, long queuing (due to credit ceilings and bureaucracy in major banks) and almost unbearable high housing prices for low and middle class budgets have discouraged loan requests a lot!

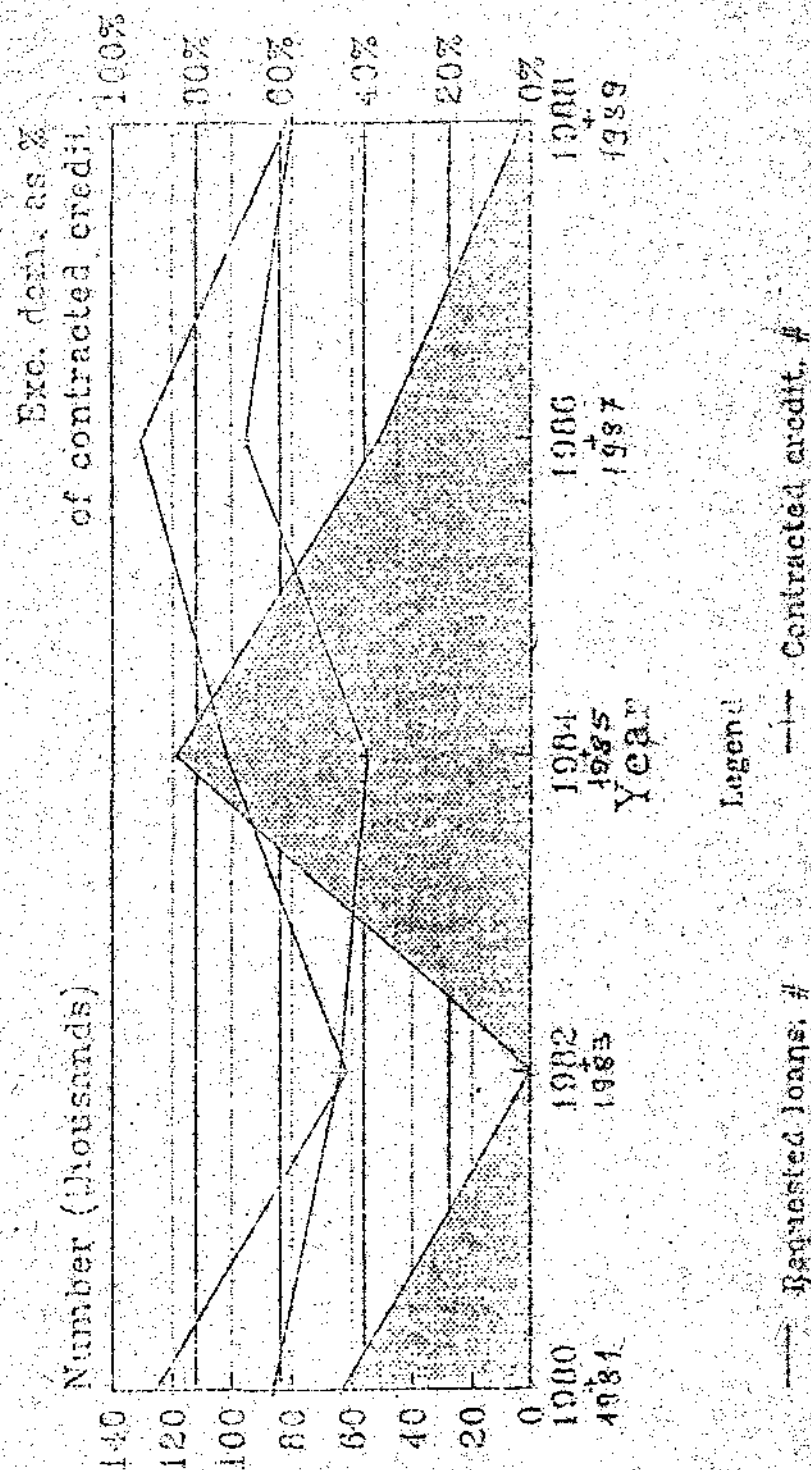
2.5. INCOME TAX

1. Many income tax systems allow for mortgage interest deduction. As common sense predicts and some theoretical literature¹⁰ has already proven, this tax feature incentives a home searcher to join the "owners club".

¹⁰ An insightful and very interesting comprehensive treatment of housing-related income taxation can be found in Nakagami and Pereira (1989b). In an earlier paper, these authors discuss the relevance of appreciation for housing trade-ups - (1989a)

Chart 5: MORTGAGE LOANS (HOUSEHOLDS)

"Excess Demand" Indicator



Base data: MOPIC (1)

Why is this so? In the last subsection we found that initial housing expenditure is (potentially) larger in the renting tenure. Consider a certain non-housing consumption level common to both tenures: household's current saving is higher if he decides to become a owner. The superiority of ownership we discovered in the last subsection lies precisely on this higher current saving.

Take now an income tax system allowing for interest deductivity: this feature reduces taxable future income, an advantage only achievable by owners.

2. Portuguese experience

Until the 1989 Income Tax Reform, mortgage interests were fully deductible¹¹. This buying-oriented policy has been drastically eliminated by that Reform.¹²

¹¹ For the sake of truth, Law No. 2/88, of January 26, limited this deduction to £4,000 (1,000 contos) "per annum".

¹² The Reform imposed an overall deduction ceiling of only £360 "per" year for single tax-payers. This overall ceiling applies to all deduction categories allowed by Law: health, education, housing, etc.. The previous ceiling of £4,000 mentioned before applied to housing mortgage interests alone.

3. TENURE CHOICE DETERMINANTS - SUPPLY SIDE (BRIEF ANALYSIS)

Table 1 extends panel 1A data back to the seventies. Two facts are worth notice:

- total production fall from 1974 onwards (the 1974 level is regained only fourteen years later, in 1988!);
- renting-purpose production continuous decline from 1974 onwards and current virtual disappearance.

Let us try to stress potential supply-side explanations for the renting tenure collapse.

3.1. RENT FREEZING

Rents have been frozen in Lisbon and Oporto cities since 1948 until 1985 (37 years!). Freezing was generalized to the whole country in September 1974. Rental rates were stuck in nominal value, current prices!

From 1985 onwards (Law No. 46/85, of September 20, arts. 6 and 11 to 15) rental rates have been insulated some "heat" every year - however, liberalization was not complete, that would be socially unbearable. A partial adjustment scheme was designed by the government, featuring three key elements:

- yearly relative increase (from 1985 onwards) is higher the older is the contracting date (arts. 11 to 14 of Law No. 46/85);
- a rent subsidy is granted to less favoured families, as a function of tax reported incomes, to ease the burden imposed by the above adjustment (arts. 22 to 27 of Law No. 46/85);
- for recent rental contracts (established after the 1st January, 1980) the proportional increase is a fraction of the Consumer

Table 1: PORTUGUESE HOUSING SUPPLY - 1970-1989

Year	New dwelling production	For renting (1)	For owner- occupancy (1)
1970	27193	49.9	50.1
1971	35309	54.9	45.1
1972	39530	54.6	45.4
1973	41316	50.8	49.2
1974	42580	53.6	46.4
1975	31172	24.4	75.6
1976	29290	15.7	84.3
1977	33848	8.5	91.5
1978	33082	6	94
1979	36430	4.8	95.2
1980	38231	3.7	96.3
1981	38597	3.9	96.1
1982	39791	5.5	94.4
1983	33127	4.8	95.2
1984	41250	4.3	95.7
1985	35475	2.9	97.1
1986	37274	2	98
1987	38833	2.3	97.7
1988	45974	1.8	98.2
1989	(2) 45000	(3)	(3)

(1) Denominator used to compute this share is "total production less non-classified production". Value in percentage form.

(2) Estimate.

(3) Not available yet.

Sources: 1970 to 1978 - AECOPS (1988, p. XII);
1979 to 1988 - INE (2);
1989 - MOPTC (3, p. 5).

Price Index (CPI) of the previous year. That fraction lies between 3/4 and 100% of the CPI and is determined by the government in October after consultation of the Social Partners Council (art. 6 of Law No. 46/85).

At most, landlords now keep constant in real terms rental rates received from new renting contracts.

3.2. UNLIMITED TIME HORIZON OF RENTING CONTRACTS

Although formally contracts last only six months or one year, they are automatically renewed for equal periods until

- the tenant resigns
- or
- the tenant dies, leaving no eligible transmitant.

Only in very limited circumstances has the landlord the right to cease the contract (for example, unauthorized sub-renting and emigrant status).

3.3. CONTRACT TRANSMISSIBILITY

Rental contract regulations still allow for transmissibility in a wide number of cases. In fact, by death of the original tenant, the contracts is automatically transmitted to any relative living with the current tenant for at least one year (art. 1111 of the Civil Law Code).

This makes renting contracts virtually durable "ad infinitum", with no positive real return expectancy to the landlord!

3.4. FAST REAL APPRECIATION OF OWNER-OCCUPIED DWELLINGS

Landlords watch to an incredibly fast real appreciation of owner-occupied homes, while their own dwelling investments pay them a zero (if not negative) real return.

Under all these circumstances, what incentive does a potential investor have to become landlord? NONE!

4. OVERALL HOUSING POLICY ASSESSMENT

1. From the discussion of sections 2 and 3, we may discover what the government's view about the best housing tenure choice for its citizens is. Apart from the recent (1989) tax penalty on mortgage interest and despite frequent party suessions in Cabinet, all policy instruments analysed point out for a clear owner-occupancy preference.

In fact, and as far as demand-side instruments are concerned, we noted how the:

- implicit rental rate tax exemption during the whole decade did favour owner-occupancy;
- mortgage credit system has been used since 1976 as the primary policy tool to promote explicitly and deliberately dwelling buying by home users;
- personal income tax rules allowed for mortgage interest full deductivity all along until 1988;
- 1989 capital gains tax introduction, in the light of reduced competition within the landlording industry, is expected in the near future to contribute even further for owner-occupancy relative attractiveness.

Supply-side instruments reinforce this preference. All four instruments described in section 3 orient investment out of the renting tenure. Their manipulation contribute for non-positive real return expectation on this tenure and a clearly positive expected real return on (alternative) ownership investment. Partial adjustment defreezing of 1985 relieved the picture but has not been enough to restore supplier's confidence on renting-purpose investment.

2. But has this policy orientation been able to solve (or, at least, to improve) the housing situation in Portugal?

We all know governments never determine economic facts alone, even in decrepit centralized economies. We have always to account for spontaneous, automatic adjustment forces generated by a multitude of anonymous agents). Therefore, authorities cannot be made fully responsible for all market outcomes, negative or positive.

However, the figures about the Portuguese housing market situation cruelly dispute any optimistic policy assessment of the past. The following table (table 2) is quite impressive!

Actual accumulated supply in this period (1982 to 1988) is 276,724 new dwellings. Total satisfaction of housing needs in Portugal would require an instantaneous provision of just 854,800 additional homes! The study we are referring to [AECOPS (1989)] estimate an yearly increase in new needs of 50,000 to 60,000 dwellings. Hence, ten years ahead, total new dwelling requirements will amount to 1,354,800 - 1,454,800. Therefore, total needs full clearance will require an annual production average of 135,500 to 145,500 dwellings in the next ten years. Compare this last figure with actual average production in the previous seven years: 39,532!

Given the past performance evaluated by charts and tables shown in this paper, the reader may judge by him(her)self the colossal effort Portugal needs to make in the years to come.

Table 2: HOUSING POTENTIAL EXCESS DEMAND (END 1988)

New dwelling total requirements	851300
For elimination of "bidonvilles" and similar unworthy housing in 1981 (1)	377300
For co-housing living families in 1981 (1)	111500
For new needs not pleased between 1981 and 1988 (1),(2)	365500

Sources: AECOPS (1988 and 1989).

(1) See methodological notes on table 1, p. VII, of AECOPS (1988).

(2) Explained on page IX of AECOPS (1989).

5. PROSPECTS FOR FUTURE GOVERNMENTAL INITIATIVE

How does the government intend to react to the impressive deficit we mentioned in the last section? Let us first focus on what vectors should housing policy be based on and then anticipate what actual initiatives are being prepared.

A - Desirable policy vectors

- financial and fiscal incentives designed to increase production scale significantly
- promotion of renting - oriented housing production and demand (labour mobility, also discussed at this SAUS's workshop, definitely requires a dynamic renting tenure)
- complete re-designing and promotion of social housing schemes

B - Likely future government actions

The probable initiatives we list below are certainly not new in the European context but will represent an innovation for Portugal.

- mortgage bond market launching

virtually no detail at all about this operation has been released so far.

- housing leasing

From what we heard in the backdoor this instrument seems tailored for commercial customers rather than individuals in light of some main features already disclosed:

- "short"-run nature (ten year maximum repayment period);

- interest rate (2.5% "per" month) above mortgage loan's;
- fast depreciation / higher tax saving;
- no downpayment.

- rental contracts liberalization

Limited durability and restrained transmissibility scope are expected to dominate future legislation. However, huge popularity costs (the electorate is made of many tenants and few landlords) are likely to delay one or two years further this liberalization (there will be general elections in 1991).

Final Note

This text was written between May and September 1990. Meanwhile, the government proposed two measures for parliamentary discussion in line with what has been recommended above and these proposals have been approved:

- five-year minimum time horizon for future rental contracts (landlords may unilaterally cease contracts after five years; no limits for the first year rent - to be freely negotiated between parties; yearly rent increases administered according to what has been explained in point 3.1. above).
- tax deductivity of rental payments (future rental contracts will enable tenants to deduct payed rents from taxable income up to the same overall ceiling already established for home buyers).

Both decisions are in force since October 15th, 1990.

REFERENCES

- AECOPS -Associação de Empresas de Construção e Obras Públicas do Sul - (1988), Para um Modelo Novo de Política Habitacional, *Colecção Documentos (Separata da revista "Indústria da Construção")*, No. 12, January, Lisbon.
- _____ (1989), As Vicissitudes e as Contradições da Política Habitacional Portuguesa, *Colecção Documentos (Separata da revista "Indústria da Construção")*, No. 14, May, Lisbon.
- ARNOTT, Richard (1987), "Economic Theory and Housing", ch. 24 of E. S. Mills (ed.), *Handbook of Regional and Urban Economics*, Vol. 2 (Urban Economics), Amsterdam: North-Holland.
- ATKINSON, Anthony B., GOMULKA, J. and SMITH, J.M. (1988), "Treatment of Mortgage Interest in the FES", ch. 9 of A. B. Atkinson and H. Sutherland (eds.), *Tax-Benefit Models*, London: Suntory-Toyota International Centre for Economics and Related Disciplines and London School of Economics and Political Science.
- BALEIRAS, Rui N. (1988), "Tributação de Mais-Valias: porque espera o Governo?", *Euroexpansão*, Year VI, No. 44, April/May, pp. 46-52 (reprinted in No. 45, pp. 56-59, due to typing errors in the first published version).
- _____ (1989), Determinantes da Escolha do Regime de Habitação, Universidade Nova de Lisboa, Department of Economics, *Working Paper* No. 117, April.
- _____ (1990), "Housing Tenure Choice: recent trends in the Portuguese market", in W. Bartlett (ed.) *European Housing Systems: lessons for the U.K.*, forthcoming book.
- CIVIL LAW CODE - "Código Civil" - (1985), Coimbra: Livraria Almedina.
- "DECRETO-LEI" No. 13/86 of 23 January 1986, *Diário da República*, I Série, No. 19, pp. 240-243.
- DEUTSCH, Edwin and SCHÖPP, Wolfgang (1990), Housing Choice and Income Distribution, paper proposed to workshop A of the *CILOG Conference* to be held in Paris (July 1990), Vienna, April.

- HENDERSON, J. Vernon and IOANNIDES, Yannis M. (1983), "A Model of Housing Tenure Choice", *The American Economic Review*, Vol. 73, March, pp. 98-113.
- KING, Mervyn A. (1980), "An Econometric Model of Tenure Choice and Demand for Housing as a Joint Decision", *Journal of Public Economics*, Vol. 14, October, pp. 137-159.
- LAFFONT, Jean-J. (1985), *Cours de Théorie Microéconomique*, Vol. II (Economie de l' Incertain et de l' Information), Paris: Economica.
- LAW - "Lei" - No. 47/85 of 20 September 1985, "Regimes de Renda Livre, Condicionada e Apoiada nos Contratos de Arrendamento para Habitação", *Diário da República*, I Série, No. 217, pp. 3041-3050.
- MANCHESTER, Joyce (1987), "Inflation and Housing Demand: a New Perspective", *Journal of Urban Economics*, Vol. 21, January, pp. 105-125.
- NAKAGAMI, Yasuhiro and Pereira, Alfredo M. (1989a), Housing Appreciation, Mortgage Interest Rates, and Homeowner Mobility, University of California-San Diego, Department of Economics, *Discussion Paper* No. 89-6, February.
- ____ (1989b), Housing Taxation in a Dynamic General Equilibrium Framework, University of California-San Diego, Department of Economics, *Discussion Paper* No. 89-46, October.
- ROSEN, Harvey S., ROSEN, Kenneth T. and HOLTZ-EAKIN, Douglas (1984), "Housing Tenure Choice, Uncertainty and Taxation", *The Review of Economics and Statistics*, Vol. LXVI, August, pp. 405-416.
- VARIAN, Hal R. (1984), *Microeconomic Analysis*, second edition, New York: Norton.
- WEISS, Yoram (1978), "Capital Gains, Discriminatory Taxes, and the Choice between Renting and Owning a House", *Journal of Public Economics*, Vol. 10, August, pp. 45-55.

DATA SOURCES

- INE (1):** Instituto Nacional de Estatística (1984), XII Recenseamento Geral da População e II Recenseamento Geral da Habitação, 1981 (Definitive Results), volume "Total do País", Lisbon: Imprensa Nacional-Casa da Moeda.
- INE (2):** _____ (several years), Estatísticas da Construção e Habitação (Mainland, Azores and Madeira), Lisbon: Imprensa Nacional-Casa da Moeda.
- INE (3):** _____ (1990), "Consumer Price Index (Lisbon and Oporto)", Public Relations Office (telephone call report), May.
- MOPTC (1):** Ministério das Obras Públicas, Transportes e Comunicação - Gabinete de Estudos e Planeamento (1990), informally supplied data on several variables.
- MOPTC (2):** _____ (1990), New Housing Prices in Lisbon and Oporto Regions, informally supplied sample data.
- MOPTC (3):** _____ (1990), Anos 90: as obras que estão a mudar Portugal, March, Lisbon.