

Switzerland

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The main tenures in Switzerland

The Swiss housing market may be a variant on the social market model that Tom Startup calls for. Historically the housing market was neither left to itself after the end of the 19th century, but nor has there ever been mass state provision of housing.

One striking feature of the Swiss housing market is the very low proportion of households that own their home. This proportion is the lowest in the OECD, at 31.3% in 1990. That compares to owner-occupation rates of twice that size in many other OECD countries. There is, however, wide variation within Switzerland. The owner-occupation rates in primarily urban cantons such as Geneva (13.8%), Basle-City (11.0%), and Zurich (20.9%) are much lower, while rural cantons have rates over 50%. The owner-occupied sector has always been a relatively small part of the housing market.

Table 1 Tenure statuses for dwellings of principal residence, Switzerland 1970-90

	1970	1980	1990
Full ownership	25.5	24.2	24.0
Shared ownership	2.4	3.5	2.9
Condominium ownership	0.6	2.4	4.4
Total ownership	28.5	30.1	31.3
Co-operatives	3.9	3.9	3.7
Ordinary rental	63.7	63.0	62.8
Farming lease	0.8	0.5	0.3
Service or free dwelling	3.1	2.5	1.9
Total rental	71.5	69.9	68.7
Source: Aebersold (1994, p. 11)			

The earliest data on the share of home-ownership are from a partial census in 1950: 37%. That figure is higher than the rate in the UK, the Netherlands or France at the same time and not much lower than in other European countries. However, all those countries saw their rates grow following the last War while the Swiss rate first declined to 28.5% in 1970 under the influence of strong immigration, then rose very slowly to possibly some 35% in 2000 (data to be published shortly). One important early factor was the legal impossibility, from 1912 until 1965, to buy an apartment in a multi-family unit and, since then, the hurdles placed in the way of the conversion of rental to owner-occupied apartments. Further reasons are detailed below.

However, the low proportion of home-owners does not mean that few people own real estate. It is quite common for tenants to own a secondary residence or even rental housing. In 1990,

68.8% of all housing units belonged to individuals¹ or 51.5% of all rental dwellings of main residence. However, much of that property is concentrated in the hands of few, with just 9% of Swiss households owning rental dwellings (Gerheuser, 2001, based on a survey in 1998).

As indicated, about one half of the Swiss rental market belongs to individuals. The remainder belongs to property companies, pension funds, insurance companies, co-operatives, and foundations. There is no statistical category which clearly identifies not-for-profit landlords, but the following categories of housing providers could be counted as mainly not-for-profit: co-operatives (7.5% of the rental stock in 1990), public sector (3.7%) and foundations and associations (2.5%). The total share of not-for-profit housing is thus 13.7%. Moderate rent regulation protects the other 86.3% of tenants from the odd greedy landlord.

About 10% of the housing stock is built with some form of public aid. However most of that aid is not reserved to needy households or to not-for-profit landlords, so it is very difficult to clearly identify and quantify social housing in Switzerland.

Housing policy

The relatively small size of the owner-occupied housing stock is not at all a sign of poor housing conditions. Its complement is a private rental sector that provides comfortable housing to most households and adequate opportunities to private investors. In comparison to other countries, regulatory interference (e.g. rent control) is moderate and housing policy is fair towards rental housing. The provision of rental housing relies heavily on private initiative. At the same time little is done to promote home-ownership, although the issue is often on political agendas.

In spite of that generally favourable assessment, housing policy is in the process of fundamental revision. Indeed, there are reasons for everyone to be dissatisfied. The Right bemoans the low share of home-ownership and excess rent regulation, while the Left complains about near-permanent housing shortage and a ratchet effect that has rents grow with costs but never decline when costs do.

The present situation is shaped by policies which were set up after the first oil-price shock and the ensuing deflation of a huge construction bubble. Earlier experience with rent control and housing aid also shaped that policy. There are essentially four pillars to current housing policy (Cuennet et al., 2002).

Rent regulation

Wartime and post-war rent control was replaced in 1972 by regulation against 'abusive' rents, comparable to the UK's 'fair rents' system. Basically, rents are abusive if they provide landlords 'excessive' returns. Under that theory, a tenant may oppose the rent she pays and force her landlord to open his accounts and prove that he is not overcharging. In order to reduce uncertainty and litigation, the law sets criteria for raising rents every 6 or 12 months based on changes in typical costs (interest rates and inflation). Indeed, tenants typically challenge rent increases (more rarely decreases that are not granted) rather than initial rent levels. Neither rule allows not-for-profit supply to exert any influence on rent setting via rent regulation. There exists however a third rule, which lawmakers introduced in the law at the request of property interests: a rent is not abusive if it is close to those of comparable dwellings in the neighbourhood. That rule is designed to avoid a growing spread between the rents of new and old dwellings. Although

¹ That is the sum of 27.8% owner-occupied main residences, 30.4% rental housing and 10.6% secondary residences, vacant homes and others.

landlords frequently referred to that rule, courts have rarely accepted it due to the difficulty of comparing dwellings.

The government is revising rent regulation, due to growing dissatisfaction among both tenants and landlords. The aim is simplification without sacrificing tenant security. The solution found was to limit allowable rent increases to changes in the consumer price index. But this did not solve the problem of initial rent levels (for rents concluded with a new contract) nor of the absolute level of rents. For this reason, policy-makers considered a system based on the rule of comparable rents. A statistical service would define a set of average rents for all types of dwellings. However, tenant organisations found the system insufficiently transparent and landlord organisations opposed the dissemination of market information. No solution is in view today.

Promotion of rental housing

Two fundamental principles drive housing aid: (1) The market is primarily responsible for providing housing, and (2) public subsidy should be marginal (there is an informal ceiling of 10% new dwellings aided). Only a small proportion of new build is by public authorities, namely some cities. Rather, federal, cantonal and local authorities grant loans and facilitate private credit rather than handing out non-refundable subsidies. There are no general tax rebates for rental housing, but a few cantons use that instrument for non-profit housing for low-income households.

The primary instrument for promoting the construction of rental dwellings is a schedule of loans designed to lower the initial cost of new housing. The annual loans are reduced over time, and then they are reversed, so that the beneficiary pays back the loans with market interest. The schedule is set up for 20-30 years to make rents, which are then completely controlled, grow with the general trend of prices and incomes. Means-tested and non-refundable subsidies may further reduce charges. The builder may also apply for federal credit guarantee separately from the loan and subsidies. It allows him to borrow at a preferred rate with a smaller down payment.

Support is available for the construction, the purchase and the renovation of housing. Any landlord can apply for support, provided he abides by the terms of the contract with the authorities, including full rent control for 20 to 30 years. Nevertheless, not-for-profit societies (co-operatives, foundations)² are privileged partners of the housing authorities. Since they generally lack equity, the authorities help them with special loans. Their tax treatment is not particularly generous. They are taxed like regular corporations with few exemptions, such as no stamp duty on the emission of shares. Non-profit housing is by no means reserved to those who cannot afford regular market rents.

The deflation of the construction and price bubble in the early 1990s placed many landlords beneficiaries of federal aid in a very difficult situation, preventing them from raising rents and repaying the federal loans as scheduled and forcing the government to stand up for its credit guarantees. In the face of the losses and a slackening rental market, the federal authorities decided to scale back their aid massively and to suppress it completely by 2002.

Starting in 2004, federal rental housing aid will be reserved for not-for-profit landlords. Two thirds of the money will be for renovations and only one third for new build. It will take the form of free or cheap loans directly granted by the government for individual dwellings under conditions of occupation. That strange construct is the result of a compromise between those who wanted direct personal assistance to households in need and those who wanted to maintain aid to construction. Still, local authorities are invited to pay direct personal assistance.

² A society obtains that status if its statutes restrict its activities to building and acquiring dwellings of moderate rents or prices, forbid dividends exceeding 6% of social capital, and provide that residual equity after dissolution of the society be affected to similar use.

Promotion of home-ownership

Until 2001 the explicit instruments of aid to home-ownership were the same as those for rental housing, namely loans and credit guarantees (Thalmann, 1997). Non-refundable subsidies were never paid out. In the process of revising and focusing housing aid, it was nearly decided to drop federal aid to home-ownership, leaving it to the cantons to decide whether they want to promote home-ownership.³ But the federal government, in response to a campaign from the rural cantons, agreed to offer similar aid for home-ownership as for rental housing in areas without large rental markets.

Tax treatment of the tenures

In money amounts, the principal support for home-ownership is through tax rebates, even though Swiss tax authorities are not very generous to home-owners. The playing field for the tenures is clearly not as tilted towards ownership as in the UK.

In order to compare the taxation of owner-occupied and rental housing, we must consider similar situations: a household that owns its home and a similar household that owns a dwelling but rents it to another similar household. Their taxes are summarized in the following table.

³ Thalmann (1999) provides arguments for decentralisation.

Comparison of the taxes paid by a pair landlord and renter with the taxes paid by an owner-occupant

Taxes paid by the landlord ⁽¹⁾ and the tenant	Taxes paid by the owner-occupant
Income taxes	
Rental income is added to owner's taxable income	An implicit rental income is added to owner's taxable income
Owner may deduct from taxable income his costs: mortgage interest, maintenance and other expenses	Idem
In four cantons, the tenant may deduct rent paid from taxable income ⁽²⁾	–
Wealth and property taxes	
An estimate of the property's value is added to the owner's taxable wealth	Idem
In about half of the cantons, the owner pays a complementary property tax; in certain cantons, the tax is higher for incorporated owners; the tax base is the gross value of the property, i.e. without deduction of debts	Idem. Only one canton treats differently rental property and owner-occupied property
Transaction taxes	
The owner pays various rights and duties at the purchase or the sale of a dwelling, mainly transfer and recording duties	Idem, except in two cantons which apply a lower rate to the sale of one's principal dwelling under certain conditions
The owner pays a special tax on capital gain in all the cantons but not at the federal level	Idem, except that the owner who sells his dwelling profits from carry forward of tax in almost all the cantons in the event of reinvestment within a limited period
<p>(1) We suppose that the landlord is a private individual and that the building belongs to his private fortune.</p> <p>(2) This was introduced in the late 1980s with a view to offsetting tax advantages granted to home-owners. It disappeared recently with federal tax harmonisation.</p>	

The table shows that the tax treatment of owner-occupied and rental housing is basically equivalent, implying a system that is tenure neutral in this respect. Indeed, the Federal Court has repeatedly ruled that tax equity takes precedence over the promotion of home-ownership. Nevertheless, practical considerations give the cantons some leeway to favour home-owners, which all use to varying degrees. It is particularly difficult to assess implicit rents for owner-occupied dwellings and the cantons tend to underestimate them. The Federal Court accepts under-estimation by no more than 40% and it can safely be assumed that 30% is the standard. On the other hand, two tax factors play against home-ownership: (1) the landlord may be incorporated or even tax exempt (e.g. pension funds), in which case income taxes are less (but note that more than half of the home-owners declare negative net income from their home after deducting expenses); (2) home-owners pay transaction taxes every time they change residence.

Our simulations with real tax data show that home-owners benefit from lower housing costs after four to five years of residence (Thalmann and Favarger, 2002).

Obviously, current tax advantages to home-owners are not targeted at encouraging accession (and even less mobility), since they grow with the length of ownership. Imputed rents are estimated less frequently than changes in rental rates on the market. The assessment of apartments for wealth and property taxes is even less frequent and, in most cantons, a rebate is granted which increases with the length of the holding period. Even the capital gains tax is lower for longer holding periods (to prevent speculative trading). Of course, tax advantages granted beyond the year of purchase are also valuable to home-owners and may influence the choice of tenure. However, households, which discount the future, attach less value to those advantages at the time of deciding to buy than their cost in current public budgets. Furthermore, any under-estimation of economic income and wealth is more profitable to households in high tax brackets. Those households are not the marginal homebuyers.

The tax treatment of owner-occupied housing is also being revised. The most likely outcome will be the removal of the imputed rent together with the deductibility of interest payments. This is seen mainly as a simplification. Open questions concern the deductibility of maintenance and other expenses, with a view to encouraging proper maintenance, as well as some deductibility of interest for new owners over their first years.

Federal organisation and tenure apportionment of housing policy

The central government plays the leading role as regards the promotion of housing construction and renovation and the promotion of home-ownership. That is not true, however, when tax rebates are taken into account since the federal government, the cantons and the municipalities share income taxes roughly in equal proportions and all wealth, property and transaction taxes are cantonal and local. Some cantons augment federal housing aid. The larger municipalities promote housing for low-income households. Some provide housing themselves. The local authorities have always been very important in implementing national policies.

The federal government allocates funds for aid to rental and owner-occupied housing roughly in proportion of those tenures' shares of the market. Thus, housing aid is in effect tenure neutral, although there is no law requiring that. Full assessment would need consideration of tax rebates to home-owners on the one hand, implicit rebates to tenants under rent monitoring on the other hand.

Housing policy for low income households

Rent control helps keep rents low in the face of housing shortage. It is not particularly targeted at low-income households, though, and may even place them in a very difficult situation when they must change residence. More effective aid is provided in the form of means-tested income assistance, which is basically the sum of an allowance for rent, an allowance for health insurance and an allowance for other expenses. The larger cities build housing directly or through not-for-profit foundations that they try to reserve for lower-income households. There are, however, long waiting lists for those dwellings, in part because tenants whose economic conditions improve are rarely made to move out. So in effect income assistance often picks up the rents for standard market housing.

Eligibility for income assistance and reduced-rent housing is based on self-registration and self-reporting of income and wealth. There exists not special treatment for the unemployed.

Performance of the housing market

Most aggregate indicators of housing market performance are quite satisfactory. Housing expenditure has been growing quite steadily but slowly from about 12% of total consumption at the end of the War to some 16% today. That was accompanied by steady growth in comfort, measured in particular by surface per dwelling and even more in terms of surface per inhabitant. In general the housing stock is in very good shape, with standards for rental dwellings that exceed the standards for condominiums in many European countries. The price of that comfort is high though, with rents far exceeding the levels in neighbouring countries in spite of a long history of low interest rates. Indeed, Switzerland is in first position of all European countries as regards the construction cost of its dwellings. A standard family dwelling costs between 6 and 7 times the median annual income. Even higher income families that buy their dwelling spend 5.5 times their annual income (Thalmann and Favarger, 2002)

There are swings in house prices as in other countries. Between 1970 and 1989/1990, the average price of single-family houses offered in newspapers grew by a factor of 3.5 while the CPI grew by a factor of 2.3. Then house prices declined to 75% of their peak value, while the CPI grew by a further 25% (Swiss National Bank data). The swing in rents for dwellings offered on the market was even more pronounced, with a peak in 1992 at 4.5 times the 1970 level, followed by a downswing by a third until 1999 and strong recovery since then. That does not concern all dwellings, though. The rent index for all occupied dwellings grew more or less regularly to 3.3 times today of its 1970 level.

The incredible swing in rents for dwellings offered on the market is the result of a supply of new dwellings almost never able to keep up with demand. Since the end of the last War, the proportion of vacant dwellings never exceeded 2% and it exceeded the 1% mark only in two periods: after the first oil-price shock and in the second half of the 1990s. In 1990, just before the index for rents offered on the market peaked, the vacancy rate was only 0.44%. There were virtually no vacant dwellings in the larger cities. Such a situation is recurring these days.

Low vacancy rates are clearly the main problem for most households, particularly of course for those that arrive on the market or must move. Fortunately, it does not express itself in homelessness but rather in long waiting lists and inadequate densities (crowding and under-occupation).

The responsiveness of house-building to demand

That vacancy rates can fall below 1% and stay there for several years is witness enough that house-building is not very responsive to demand. Just now, Switzerland is traversing a very paradoxical situation with vacancy rates falling from a (small) peak of 1.85% in 1998 below 1% today and new building also falling to historical lows. The 31,000 dwellings built in 2002 are only 0.86% of the stock, a ratio never seen since in fifty years of statistics. The current situation is thus quite similar to that in the UK, in that levels of new building are clearly unresponsive to changes in demand.

Private builders carry the main burden of construction in Switzerland and they have cut back their activity. They blame excessive regulation of the market (rents and contracts), which thwarts adequate returns. In fact, regulation is much less strict than in many neighbouring countries and it did not get any stricter recently. But there is clearly increased uncertainty due to the current difficult overhaul of housing policy mentioned earlier. Tenant associations point at investors who go after quick profits on the financial markets; but the recent downturn of those markets did not help construction.

Land is certainly a key factor in explaining construction levels, as in the UK. Switzerland is a small country that tries to protect its landscape through a demanding planning system. In theory, there is sufficient land set aside for housing construction. In practice, builders find it very difficult to locate adequate land, owners willing to sell and local authorities disposed to provide the additional infrastructure and to authorize building. Those hurdles are particularly high for large projects, so that no large housing estate has been built recently which is comparable to those that helped face rapid population growth in the 1950s and 1960s.

The social status of the different tenures

A large survey of Swiss households in 1996 showed that a majority of them dream of home-ownership (Thalmann and Favarger, 2002). In fact, most of them combine an aspiration for home-ownership with a desire for detached housing, which puts that dream even further out of reach. So there is this pull factor for home-ownership. However, other standard pull factors such as the protection against economic instability, access to better neighbourhoods, a higher social status or important tax advantages hardly exist. What are missing most are the push factors. In repeated survey, Swiss tenants have expressed great satisfaction with their housing conditions and even with the rents they pay.

As a result, there is not the same sharp social divide between renters and home-owners as in other countries. Many higher income households are very happy in long-term private rental - a rarity it seems in the UK. One fifth of the tenants report gross yearly income above CHF 120,000 (Gerheuser, 2001), which is about twice median household income. Econometric analysis of our 1996 survey (Thalmann and Favarger, 2002) shows that by far the main determinant of ownership is the desire to own one's home, and that desire is only weakly correlated with income and wealth or other personal characteristics, except children and age (retired persons very rarely dream of home-ownership). Income and wealth are nevertheless direct determinants of home-ownership in enabling it. In a nutshell, the likelihood of a household to own its home is higher when it strongly desires such ownership, when it is married, when it is wealthy, when it is Swiss, and when its head is independent rather than salaried and over 40 years old. The median age of moving into ownership is 35 years, the mean 38. Fifty-eight per cent of all home-owners live in a single-family house as compared to 6% of all renters.

Almost one half of the households surveyed could not pay down the standard 25% deposit out of their own equity. Standard lending conditions provide for slow amortization to about 60% of the property's assessed value. So Swiss owner-occupants are relatively highly indebted, accounting for a ratio of private household mortgages to GDP of about 75%. That is clearly a reflection of the long tradition in economic stability and growing property values. Nevertheless, the surprisingly sharp increase in interest rates in 1989-1990 put many recent home-owners in difficulty, leading to foreclosures, a marked decrease in prices and losses for lending institutions in the billions.

Concluding assessment of the current system

The Swiss housing market has enviable features. Tenants and home-owners express great satisfaction and do not call for fundamental changes. The small proportion of home-ownership need not be a problem and could even be a plus point in the face of business cycles and geographic reshuffling (see the 'Problems of Mass Home-Ownership' in Chapter 1 and Thalmann, 1997). Even the low vacancy rate can be seen as evidence of efficient management of the housing stock.

Nevertheless, housing policy has become an intricate mesh of sometimes-contradictory instruments and rules over the last 30 years. Reforming that mesh is proving extremely difficult in the face of many vested interests. Nevertheless, such reform and a clear result are urgent, if only to restore sufficient predictability that will encourage investors to address pent-up housing demand.

Specific categories of households face particular hardship on a tight market. Relief is sought in income support and some public housing provided by local authorities. Federal support allows for better burden sharing. Our analysis of household budgets shows that only some 4% of all renter households face hardship because of adverse housing conditions (they pay excessive rents) (Thalmann, 2003). They are the prime candidates for targeted housing aid. The other 17% of all renter households whose income is not sufficient for basic needs after they paid their rent actually need general income support rather than housing aid.

The country must urgently address the difficult choice between expanding the housing stock to meet all desires for more housing surface on the one hand, and protecting the remaining green fields on the other hand. Rent regulation is fine if it stabilizes rents over the business cycle, not if it keeps rents below economic costs over the long run in spite of continued housing shortage. More realistic rents and fewer tax barriers to mobility would allow re-equilibrating the market without a non-sustainable expansion of the housing stock. If the concern is that landlords benefit from excess returns thanks to housing shortage, rent regulation could use the rents charged by not-for-profit providers as a reference.

As a general matter, not-for-profit housing providers could assume a greater leadership role: in catering to low-income and special-needs households, in providing a steady flow of new building, and possibly in setting the reference for rent regulation, or providing a market leading role. To that end, public authorities should provide them greater support, mainly in the form of credit and access to land.

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