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HOUSING IN GERMANY: ADDRESS SHORTAGES AND FACILITATE ACCESS

This is a translated version of the original German-language chapter "Wohnen in Deutschland: Knappheiten beheben und Zugang erleichtern", which is the sole authoritative text. Please cite the original German-language chapter if any reference is made to this text.

KEY MESSAGES

↘ The shortage of housing in urban areas is not only a social problem, but also a macroeconomic one, as it inhibits the influx of labour into particularly productive regions.

↘ The supply of housing can be increased by mobilising potential building land, increasing incentives to build and reducing building costs by harmonising building regulations. Housing could be used more efficiently by reducing social and financial barriers to relocation.

↘ In social housing policy, subject- and object-oriented support (i.e. subsidies for individuals and for buildings) can meaningfully complement each other, as object-oriented support improves access to housing for disadvantaged groups of people. Their social target accuracy should be improved by means of a misoccupancy levy.

EXECUTIVE SUMMARY

In recent years, there has **been a sharp rise in prices on the housing market, particularly in urban areas.** Demand for housing there has risen as a result of population growth and a trend towards fewer people per household; it has fallen in structurally weak rural regions. At the same time, the supply of housing is lagging behind the increase in demand because of insufficient construction activity.

Firstly, the lack of available housing in urban areas can restrict the access of labour to productive companies and thus inhibit macroeconomic development. Secondly, **low-income and disadvantaged population groups have limited access to adequate housing on the regular housing market.** This leads to evasive reactions and, in regions where demand is particularly high, to an increase in overcrowding, especially among socially disadvantaged groups.

In order to boost the construction of new residential housing, **building-land potential** should first **be mobilised. This can be** helped **by redensification**, which is facilitated by further **reductions** in **restrictive building regulations**. In tight housing markets, greater use could be made of greenfield development outside of the inner cities. **Incentives to use building land can** be improved by adjusting property tax. **Building costs can be reduced by more flexible and harmonised building regulations** that enable the increased **use** of **cost-effective serial and modular construction**. The **housing stock** could be **used more efficiently by removing social and financial barriers to relocation**. **Restrictive rent regulation** in the form of lowered rent caps and rent brake is **only** justifiable **on a temporary basis, and if effective measures to expand the supply of housing** are taken at the same time. An extension of the rent brake beyond 2028 should therefore be avoided, as should the lowering of rent caps in tight housing markets. **Ancillary purchase costs** could be **reduced** by lowering land transfer tax and estate-agent and notary fees.

In social housing policy, subject-oriented support by housing benefit payments for individuals aims to specifically give low-income households access to the housing market. For single parents, large families and immigrants – who are at a disadvantage on the regular housing market irrespective of their income situation – object-oriented support by social housing can facilitate access. The **target accuracy** of this support can be increased **by (re)introducing a market-related misoccupancy levy.**

I. INTRODUCTION

315. In recent years, there has been **a sharp rise in prices on the housing market**, especially in urban areas. ↘ ITEMS 323 FF. On the rental market, this increase has been seen mainly in new lets as a result of government regulation, so that the gap between existing and new rents has widened considerably. ↘ ITEM 325 The price increase in the urban areas can be attributed to both demand-side and supply-side factors. **Demand for housing** in Germany **has risen sharply** in recent years, partly due to a sharp increase in the number of households. ↘ ITEM 332 This is due to a trend towards households with fewer people and a general increase in the population as a result of immigration. Demand for housing is concentrated primarily in urban centres and economically strong rural regions. ↘ ITEMS 327 FF. By way of contrast, there was a significant decline in demand for housing in structurally weak rural regions, with a correspondingly subdued price trend. The picture also varies from region to region on the supply side. In shrinking regions, many apartments and houses are vacant because of the decline in demand, ↘ ITEM 351 while **the increase in the supply of housing** in growing regions **is lagging** behind the increase in demand, **mainly due to insufficient construction activity**. ↘ ITEM 350

316. The **housing market** differs significantly from other markets, above all in terms of its supply structure. Housing is **location-specific**, which means that the markets are spatially differentiated. In addition, the short-term fixed supply of building land and the long completion period for housing lead to a **short-term low elasticity of housing supply**. This can lead to a sharp rise in the market price if demand for housing increases. In addition, the housing market is characterised by **high transaction costs** (e.g. real estate transfer tax or search and relocation costs). ↘ ITEMS 357 FF. **The longevity** of housing compared to other consumer goods increases its attractiveness as an investment asset and makes the housing market susceptible to price distortions caused by speculative investment (GCEE Annual Report 2018 items 666 ff.).

317. The **allocation of housing** influences the geographical availability of labour and can thus have a noticeable **impact on macroeconomic development**. ↘ ITEM 348 To ensure an efficient use of labour as a factor of production, workers should be deployed where they are most productive. However, access to the productive companies is often only possible if these workers have access to housing nearby.

The low availability of housing in productive urban areas compared to demand is therefore relevant to the overall economy. The construction of new housing in urban areas is inhibited by a low availability of building land, strict regulatory requirements and the associated high construction costs. ↘ ITEMS 352 FF. At the same time, potential building land in neighbouring regions and existing housing potential in structurally weak regions are often not used because transport links are inadequate. ↘ ITEMS 355 F. In addition, **the efficient use of housing is hampered by social and financial hurdles to relocation**. The social hurdles lie in people's attachment to their own homes and the associated social environment. ↘ ITEM 356 The financial hurdles lie in the large regulatory gap between existing and

new rents and the high transaction costs on the purchase and rental markets. ↘ ITEMS 357 FF. As a result of these hurdles, there are few incentives to downsize and the average amount of residential space used increases with age. ↘ ITEMS 335 FF.

318. **Access to adequate housing is of great social relevance**. Low-income households have an above-average relative rent burden ↘ ITEM 367 and are correspondingly greatly affected by price increases on the housing market. On average, the rent burden in Germany has remained largely constant since the 2000s (Sagner et al., 2020). The fact that **overcrowding has increased in urban areas** may have contributed to this. ↘ ITEM 369 Single parents, large families and immigrants are particularly affected by cramped living conditions and the associated social consequences. Access to rental housing that is appropriate in terms of size, quality and rent is more difficult for them. ↘ ITEMS 369 F.

319. The various challenges in the housing market can be addressed with targeted policy measures. The availability of housing could be **increased by boosting the construction of new homes**. For example, the amount of building regulations that hinder redensification by adding storeys and converting lofts could be reduced nationwide. ↘ ITEM 388 The planned introduction of building type E, which dispenses with cost-intensive building standards, should **reduce construction costs**. ↘ ITEM 390 In addition, further harmonisation of regional building regulations could lead to the increased use of cost-effective serial and modular construction methods. ↘ ITEM 387

In regions with a high demand for housing and limited potential for redensification, **external development** could be used. ↘ ITEM 383 In addition, incentives for **denser development could be created** through adjustments to property tax, e.g. a stronger weighting of plots in the valuation procedures for land and property compared to the current structure. ↘ ITEM 384 Incentives to build on undeveloped plots ready for construction could be increased by using property tax C in municipalities with tight housing markets. ↘ ITEM 385

320. In order to use **the housing stock more efficiently, barriers to relocation** could **be removed** which often prevent people from reducing the amount of residential space they use, especially in old age. Mixing residential neighbourhoods with different types of housing and promoting local housing-exchange concepts could be helpful in enabling people to move without giving up their social environment. ↘ ITEMS 395 FF. Rent regulation could be adapted to strengthen the financial incentives to move house. **Restrictive rent regulation** in the form of lower rent caps and rent brake can **only be justified temporarily and generally if** effective **measures are taken** at the same time **to expand the supply of housing**. The rent brake should not be extended beyond 2028 to ensure that such measures are taken. In order to limit the gap between existing and new rents, the quality requirements for the preparation of rent indices could be increased and new rents weighted more heavily. Reduced rent caps in tight housing markets should be fundamentally called into question. ↘ ITEMS 398 FF. Furthermore, the efficiency of the purchase market could be increased by reducing transaction costs, e.g. real estate transfer tax and estate-agent and notary costs. ↘ ITEMS 403 F.

321. Social housing policy instruments can help to **ensure access to suitable housing for disadvantaged population groups**. Individual (subject-oriented) support in the form of housing benefit gives low-income households targeted access to the housing market. ↘ ITEM 378 In addition, social housing ensures access to appropriate housing for households for whom access to appropriate housing is more difficult even when they have the same ability to pay. ↘ ITEM 368 **Social housing** (object-oriented support) should therefore again be given a more important role in social housing policy in future, as it **can meaningfully complement subject-oriented support**. The problem of subsidised housing lacking targeting accuracy ↘ ITEM 373 can be addressed by introducing a market-related misoccupancy levy for social housing subsidies. ↘ ITEM 411 The revenue could flow to the federal states and be earmarked for social housing. In the case of housing benefits, the interaction between the housing benefit system and the basic income support system could be addressed by introducing a uniform transfer payment with only a small transfer deduction. ↘ ITEM 407

II. INITIAL SITUATION: THE HOUSING MARKET IN GERMANY

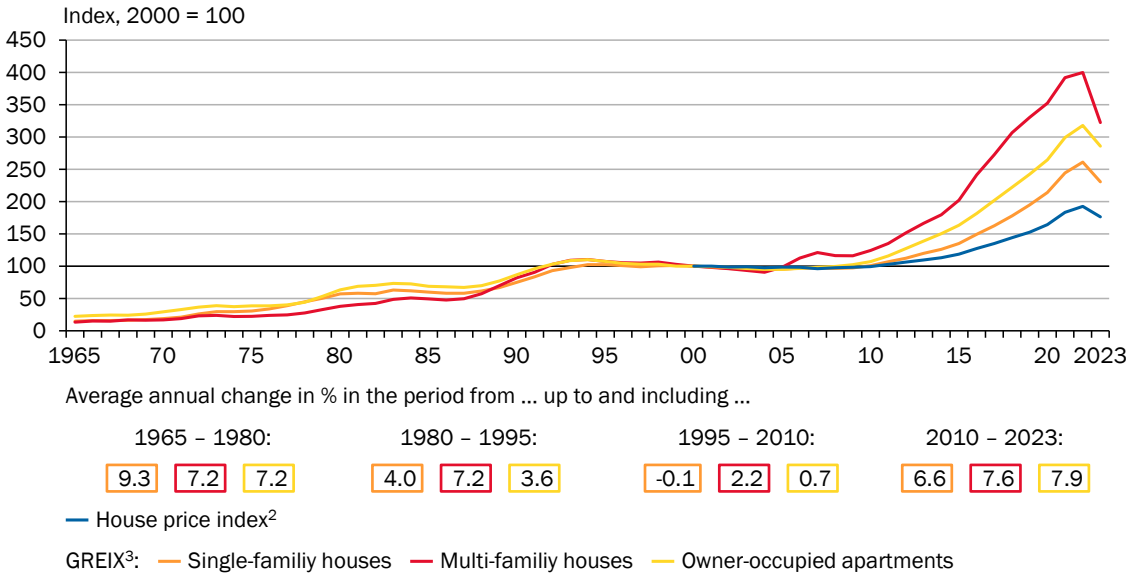
322. The situation on the housing market in Germany varies greatly from region to region. While **purchase and rental prices have risen sharply** since 2010, especially **in urban areas**, their development has been much less dynamic in rural areas. ↘ ITEMS 323 FF. **Demand for housing** in Germany has risen in recent years due to a trend towards fewer people per household and general population growth as a result of immigration. ↘ ITEMS 326 FF. It has **grown** particularly **in urban areas and economically strong rural regions**, while there has been a considerable **decline in structurally weak rural regions**. In regions where there has been a large increase in demand, **the expansion in the supply of housing is lagging** behind the increase in demand due to insufficient construction activity. Residential construction is being hampered by a lack of building land and strict regulatory requirements. ↘ ITEMS 337 FF.

1. Price trends

323. While residential property prices rose continuously until the early 1990s, they then stagnated until the beginning of the 2010s. ↘ CHART 71 ↘ BACKGROUND INFO 10 From **2010 onwards**, there was again a **strong increase in residential property prices** comparable to the increase between 1965 and 1980. Since

↘ CHART 71

Development of residential property prices in Germany[1]



1 – Indices are based on transaction data from the expert committees for property values and are quality-adjusted. 2 – Based on prices of all single- and duplex houses and owner-occupied apartments that are bought or sold in Germany as a combination of building and land. Comparability over time has been ensured since 2014, as the index was still in the development phase prior to this. 3 – German Real Estate Index.

Sources: Amaral et al. (2023), Federal Statistical Office, GREIX, own calculations

2022, there has been a decline in both transaction prices and the number of property transactions; this is probably related to the rise in general interest rates in Germany (Zdrzalek et al., 2024). ↘ BOX 20

↘ BACKGROUND INFO 10

Background: Transaction data and price determination

The **development of purchase prices** for residential property **can be measured using transaction** data collected by the expert committees for property values. The Federal Statistical Office's House Price Index (HPI) and the German Real Estate Index (GREIX) are based on this transaction data and show the price development of residential property since 2000 and 1965 respectively. The expert committees for property values were founded in 1960 with the aim of making the property market more transparent. Their work is based on the compilation of purchasing price data. For this purpose, notaries send copies of all property purchase agreements concluded in their area of responsibility. While an expert committee was originally only responsible for one municipality, by 2021 there were only around 250 appraisal committees serving correspondingly larger areas. As properties can vary greatly in quality and are only sold very irregularly, **transaction prices** must be **adjusted for qualitative changes** to ensure the comparability of purchase prices over time. In both the HPI and the GREIX, this is done by means of regressions that take into account changes in price-relevant characteristics such as residential space or year of construction.

↘ BOX 20

Background: Macroeconomic determinants of residential property prices

An extensive body of empirical literature has examined how macroeconomic factors affect residential property prices. Knoll et al. (2017) analyse the **development of real house prices from 1870 to 2012** in 14 advanced economies. Over this long period, prices in **Germany only rose by an average of around 0.4 % per year**, compared to 2 % in Australia, Belgium and Canada. The differences can be attributed in particular to the different dynamics since the Second World War. Prior to this, prices remained largely constant. The authors show that approximately 80 % of the increase since the Second World War can be explained by the rise in land prices. Using the same data set, Jordà et al. (2015) **examine the effects of interest-rate changes on residential property prices**. A **1% change in the short-term interest rate leads** to a cumulative **change in the relationship between residential property prices and income of 4 % over 4 years.** Adams and Füss (2010) estimate for 15 advanced economies that **residential property prices will rise by 0.6 % in the long term** when **economic activity increases** by 1 %. A 1 % **rise in construction costs** also increases residential property prices by around 0.6 %. A 1 % rise in long-term interest rates leads to a 0.3 % fall in residential property prices. How the supply of residential property can react to higher prices depends on the geographical conditions, such as restrictions on the available land area due to water or mountains, and regulatory restrictions, such as development plans (Green et al., 2005; Saiz, 2010).

For Germany, an analysis by the Deutsche Bundesbank (2020) on the determinants of residential property prices between 1993 and 2019 and in the German administrative districts (Kreise) in the period from 2004 to 2019 shows that they react positively to an increase in the disposable income of private households and negatively to an increase in interest rates for property financing. There was no evidence of a dampening effect of investments in residential

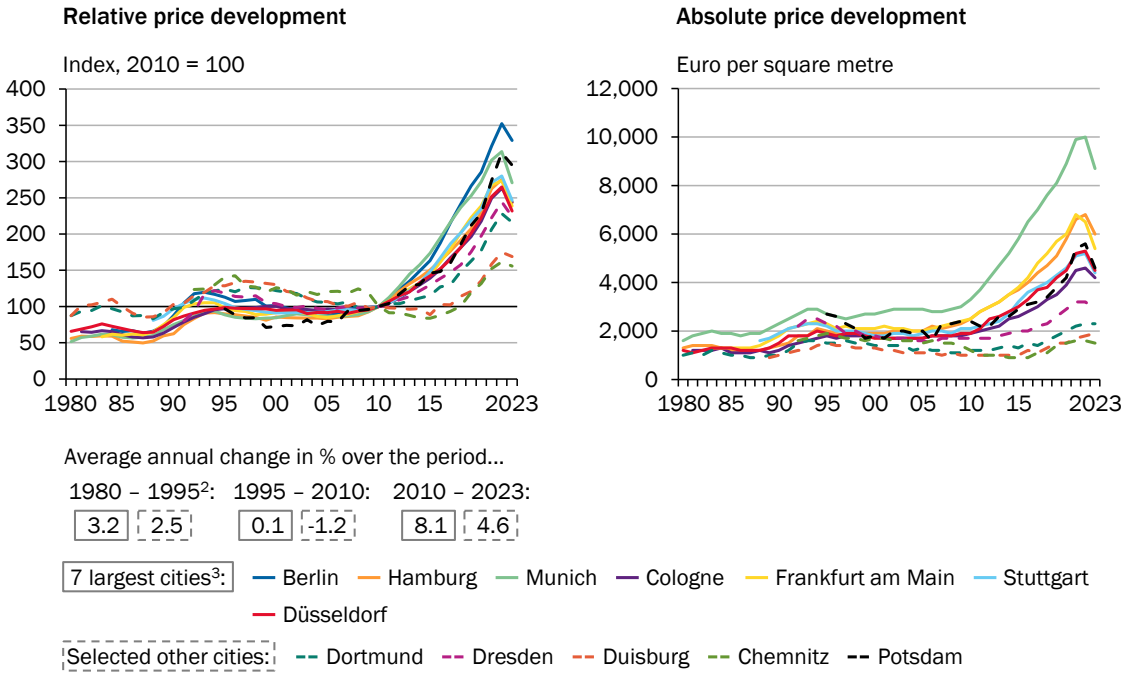
construction on real estate prices. According to the Deutsche Bundesbank, the reason for this is likely to be the high capacity utilisation in the construction industry, which has led to price increases for construction services. A **breakdown of residential property prices** into the development of building land prices and construction prices shows that the **increase in building land prices was responsible for the largest share of the increase in residential property prices**. The decline in mortgage interest rates played a significant role in the sharp rise in real estate prices from 2010 onwards. Both the Deutsche Bundesbank (2020) and Hanck and Prüser (2020) estimate that the rise in residential property prices can be explained more by falling interest rates than by other factors such as income growth. According to the Deutsche Bundesbank, the decline in residential property prices from 2022 onwards can be attributed to the reduced financing scope of many prospective buyers due to high inflation and increased financing costs. On the other hand, the sharp rise in construction costs and the small increase in the supply of housing had a price-driving effect.

324. The **rise in real estate prices** since 2010 has **varied greatly from region to region**. Up until 2015, the price increase was observed mainly in urban areas, while in the following years it also affected regions outside the cities (Deutsche Bundesbank, 2020; Hanck and Prüser, 2020). Interestingly, price trends also vary greatly between the different cities. ↘ CHART 72 Above all the seven largest cities – Berlin, Hamburg, Munich, Cologne, Frankfurt am Main, Stuttgart and Düsseldorf – saw particularly sharp price increases due to strong population growth. ↘ CHART 327 At the same time, prices rose less sharply in some other cities.

325. In addition to purchase prices, there has also been a **sharp rise in rental prices** in recent years, although this increase varied between existing contracts and asking rents. ↘ CHART 73 Since 2010, an average annual increase of around 1.4 % has been observed for existing rents, while asking rents have risen significantly faster at around 4 % per year. This growing divergence is mainly due to differences in the regulation of existing and new rents. ↘ ITEMS 357 FF. A breakdown by type of county shows that, as with purchase prices, the largest increases in asking rents occurred in the large cities.

↘ CHART 72

Heterogeneous development of residential property prices[1] in German cities



1 – The charts show the absolute and relative price development of owner-occupied apartments for selected cities based on transaction data from the expert committees for property values and are quality-adjusted. 2 – Only includes Hamburg, Munich and Düsseldorf for the 7 largest cities and Dortmund and Duisburg for the other cities due to lack of data availability. 3 – Measured in terms of population. No absolute real estate prices are available for the city of Berlin in the German Real Estate Index (GREIX).

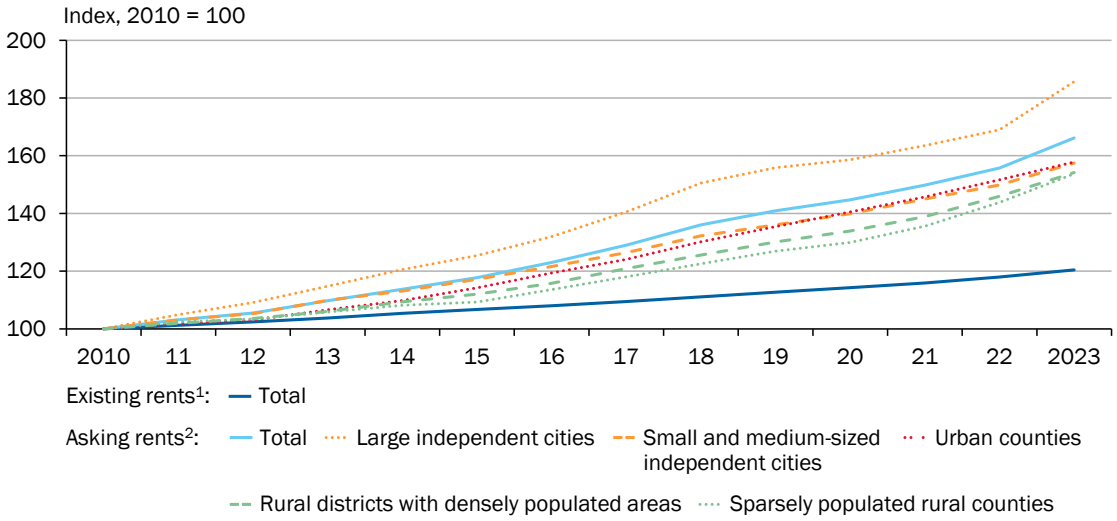
Sources: Amaral et al. (2023), GREIX, own calculations

2. Demand for housing

326. The **demand for housing** is determined by the **number of households**, **their composition and the demand for space per person**. The number of households is strongly correlated with population growth, but has been growing faster than the population in recent years due to a trend towards fewer people per household. At the same time, per-capita demand for housing is rising, leading to an even stronger increase in the demand for housing. The development of the demand for housing is a key driver of the price trends described above. At county level, a one percentage point increase in the number of people in the resident population between 2010 and 2022 was accompanied by a 1.8 percentage point increase in asking rents.

↘ CHART 73

Heterogeneous development of rental prices in Germany



1 – Based on the consumer price index for net cold rent, also includes some new rents. 2 – Based on advertisements from property platforms and newspapers for new rentals in existing buildings (excluding new builds). Flats with living space of 40 to 100 square meters with average furnishings in average to good residential locations are considered.

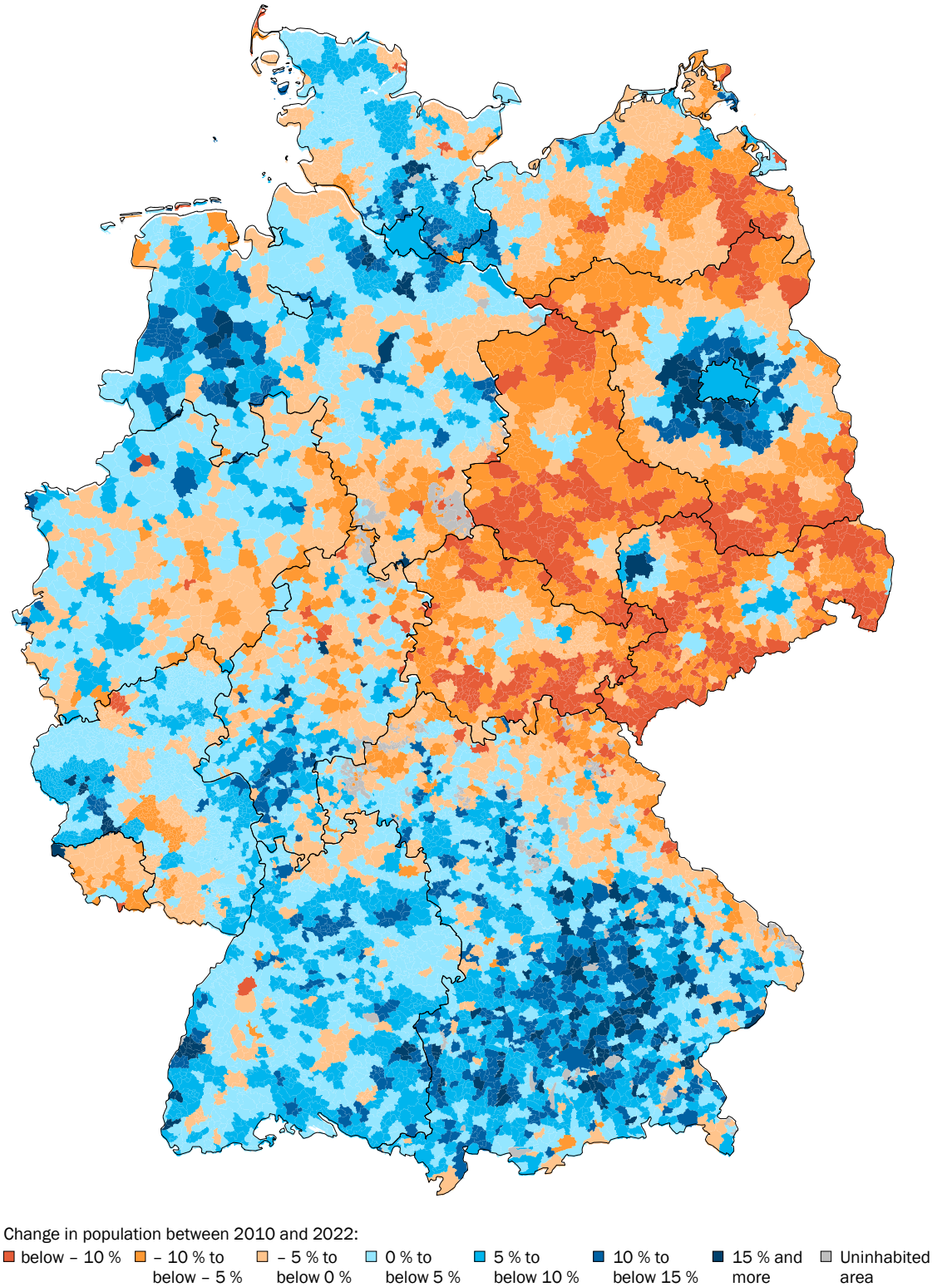
Sources: Federal Institute for Research on Building, Urban Affairs and Spatial Development, Federal Statistical Office, own calculations

Population development

327. The **residential population** in Germany fell by around 2.3 % between 2000 and 2011. By the end of 2022, however, the population increased by almost 3.5 % compared to 2011, i.e. by around 2.8 million people, in particular due to **internal EU migration** and the **influx of refugees from third countries** in 2015, 2016 and 2022. The population grew above all in urban areas and the directly neighbouring regions, but also in economically strong rural regions in the south and north-west of Germany. ↘ CHART 74 By contrast, the population declined in structurally weak rural regions, especially in eastern Germany.

↘ CHART 74

Regional population development[1]



1 – By municipal associations; territorial status as of 31 December 2022.

Sources: BBSR, Federal Agency for Cartography and Geodesy
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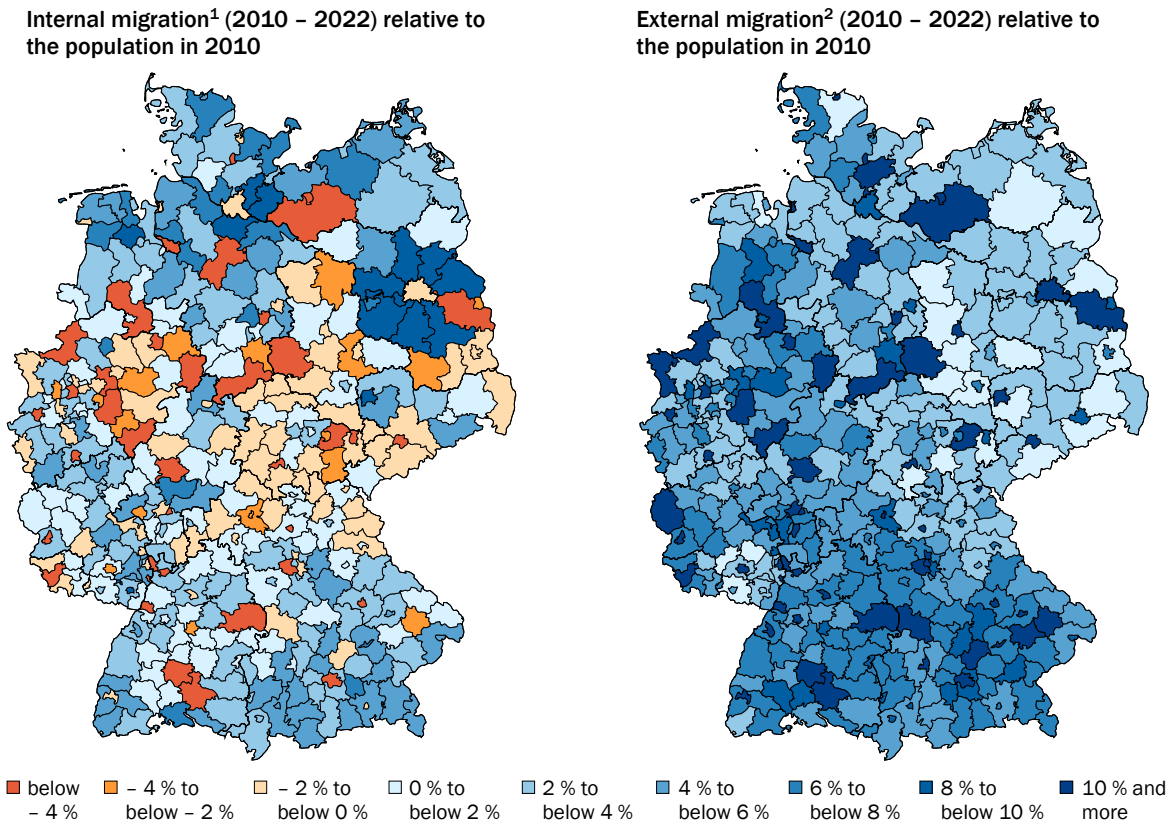
328. **Regional population development** can be broken down into three components: natural population development, internal migration ↘ ITEM 329 and external migration. ↘ ITEM 331 Natural population development is the difference between births and deaths; internal migration comprises all migration within Germany; external migration includes all immigration and emigration across Germany's borders. All three components show different regional trends at the county level. Regional **differences in natural population development** are **strongly influenced by migration movements**, as it is primarily younger population groups that migrate. Regions with net outward migration therefore tend to have a higher average age than regions with net inward migration (Maretzke et al., 2024), which results in a lower birth rate and a higher mortality rate in regions experiencing net outward migration.

329. Since 2010, **internal migration** has shown a trend towards suburbanisation, i.e. increasing migration from core cities to the surrounding areas. ↘ CHART 75 While the major cities have a neutral and, in some cases, negative internal migration balance, the directly neighbouring counties have high positive internal migration balances. By contrast, the majority of structurally weak rural counties in the periphery have a negative internal migration balance. The positive internal migration balances in the suburban areas are also likely to be influenced by high rents in the neighbouring large cities. An analysis of bilateral migration flows at the

↘ CHART 75
Development of internal and external migration



1 – Difference between inward and outward migration within Germany. 2 – Difference between immigration and emigration across the borders of Germany.

Sources: BBSR (2024), Federal Agency for Cartography and Geodesy, own calculations

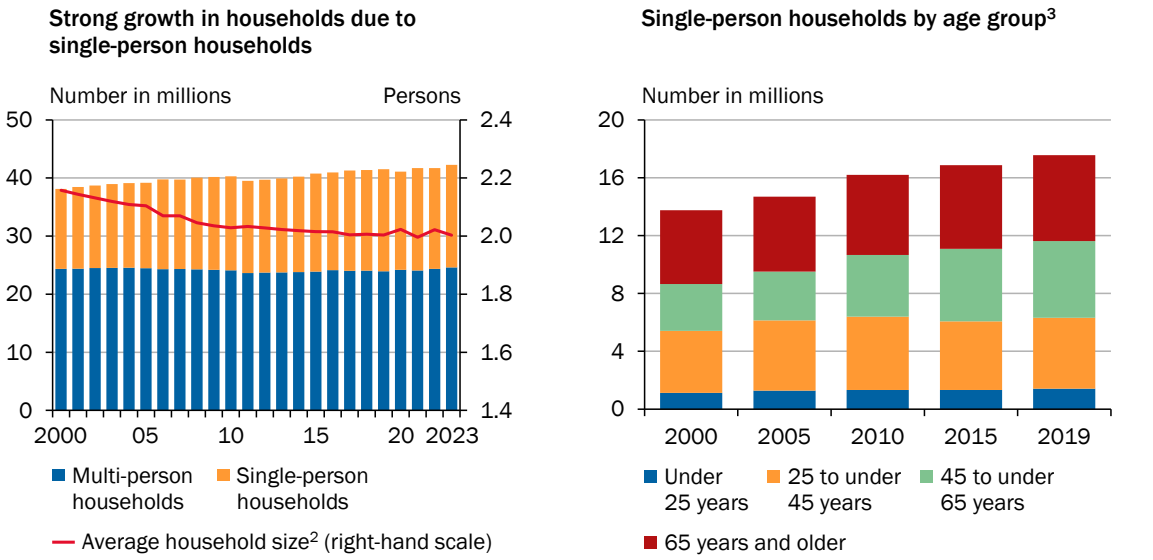
county level for the period 2004 to 2017 shows that rising rents reduce the migration balance in the affected counties (Stawarz et al., 2021).

330. **Rising rents in the urban areas lead to** less **internal immigration and** in some cases even to **internal emigration**. ↘ ITEM 329 Many people nevertheless gain access to the labour markets in urban areas by commuting to work or increasingly working from home. These two alternatives to moving home for work can take some of the pressure off the high demand for housing in urban areas. In 2023, around 23 % of all people in employment in Germany worked from home at least part of the time. Their share had thus almost doubled compared to 2019 (Federal Statistical Office, 2024a). Results from the 2022 Time Use Survey and data from the Federal Employment Agency show that, since the start of the COVID-19 pandemic, employees have been commuting less frequently than before but travelling greater distances (Coskun et al., 2024). As a result of these developments, there has simultaneously been a marked increase in office property vacancies. ↘ BOX 22

331. **External migration**, which includes all immigration and emigration across Germany's borders, shows a different picture. ↘ CHART 75 Here, all counties in Germany show a positive balance, i.e. net immigration. Particularly high positive external migration balances can be observed in the cities. Economic factors and network effects in the various immigration groups come into play here. Moreover, migration from countries of asylum origin is also characterised by institutionally influenced patterns. For example, individual counties with a reception centre

↘ CHART 76

Development of households[1]



1 – Households based on the microcensus, from 2011 onwards extrapolation using the population update based on the 2011 census, from 2016 onwards updated sample selection basis based on the 2011 census. Due to methodological changes in the microcensus, main and secondary households will be shown separately in the statistics from 2020 onwards; the values shown correspond to the sum of these two household types. 2 – Calculation based on the population; reference date: 31. December of the respective year. 3 – Age of the reference person; from 2005 onwards, the reference person corresponds to the main income earner. Secondary households reported from 2020 onwards (see footnote 1) are not shown by age group, therefore only values up to 2019 are shown.

Sources: Federal Statistical Office, own calculations

show a high positive external migration balance in the period from 2010 to 2022, while at the same time the internal migration balance in these regions is negative due to the subsequent redistribution.

Development of household size and residential space

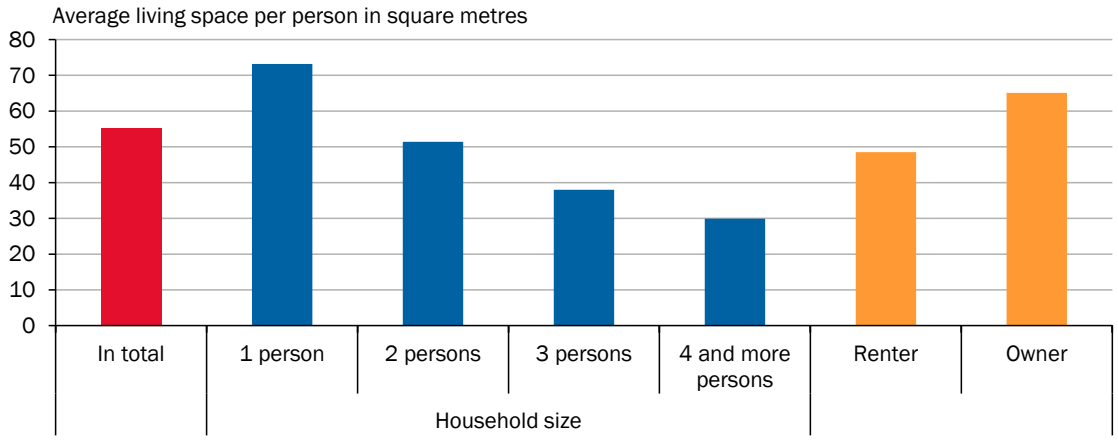
332. The **number of households has risen faster than the population** in recent years. One important reason for this is that the **proportion of single-person households** has **increased markedly** over time. ↘ CHART 76 LEFT Growth was mainly driven by the 45 to 65 age group. ↘ CHART 76 RIGHT In this age group, both the proportion of single-person households and the number of households have increased. In the over-65 age group, by contrast, the proportion of single-person households has remained constant, while the number of households has increased.

333. The **average residential space per person**, calculated as the sum of all residential spaces relative to the resident population, is rising continuously in Germany. Since 2000, it has risen from 39.5 square metres per person to 47.5 square metres per person (in 2023). Based on the microcensus, the average per-capita residential space is higher. In 2022, it was around 55 square metres and varies considerably with household size. ↘ CHART 77 While single-person households had an average residential space of around 73 square metres in 2022, the figure was only around 51 and 38 square metres per person respectively for two- and three-person households. Owner-occupied households also use significantly more residential space per person than tenant-occupied households.

334. The **average residential space** per person increases with **age**. ↘ CHART 78 ABOVE This is partly due to differences in the average number of people in the household. However, the average residential space for a given household size also increases with age. This is probably largely due to the so-called **remanence effect** (Weber, 2020). This describes the phenomenon that many people increase their

↘ CHART 77

Average living space by household size and ownership structure in 2022[1]



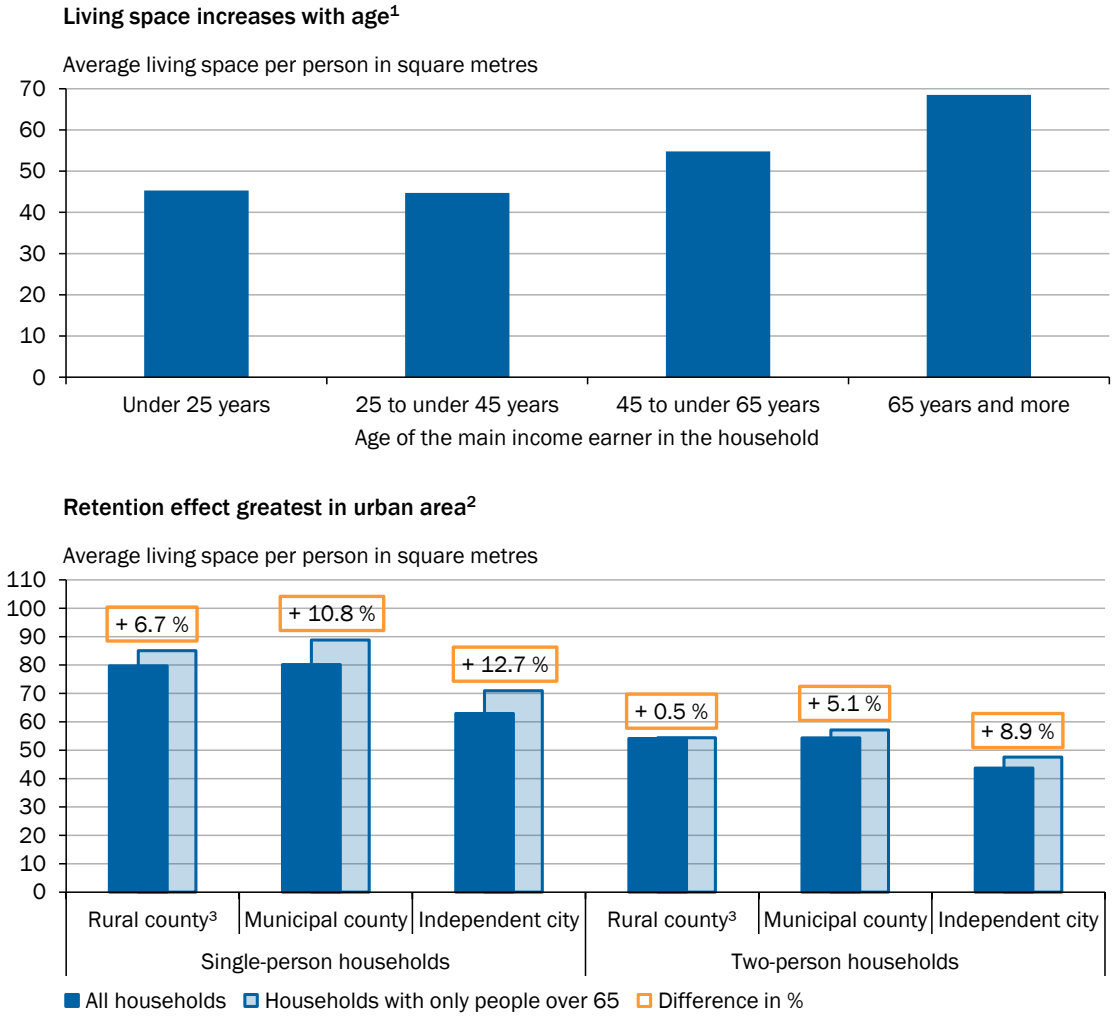
1 – Data from the 2022 microcensus, looking at households in buildings with living space (excluding halls of residence).

Source: Statistical Offices of the Federation and the Länder

residential space when starting a family, but do not reduce it again after family changes, such as children moving out. Data on relocation behaviour in Germany confirms this observation (Deutsche Post Adress, 2024; Hofmann and Rüger, 2024). People also move house less frequently as they grow older. In addition, many moves are motivated by family reasons and higher space requirements, while a lower space requirement is rarely cited as a reason for moving.

335. **The scale of the remanence effect** can be estimated by comparing the amount of residential space used by older people's households with residential space use in the average household. The average use of residential space per person in one- and two-person households with exclusively over 65-year-olds is around 82 and 54 square metres respectively. In contrast, the average residential space use of all one- and two-person households is around 72 and 51 square metres respectively. At around 6.1 million one- and 3.8 million two-person households with

↘ CHART 78
Average living space by age, household size and district type in 2022



1 – Data from the 2022 microcensus, looking at households in buildings with living space (excluding halls of residence). 2 – Data from the 2022 census. The average living space is calculated at county level and then broken down by county type. Settlement-structural county types according to the BBSR categorisation. 3 – Contains the settlement-structural county types „Rural county with densification approaches“ and „Sparsely populated rural county“.

Sources: Statistical Offices of the Federation and the Länder, own calculations

exclusively over 65-year-olds, this results in a total remanence effect of around 61 million square metres. This effect is most evident in urban areas. ↘ CHART 78 BOTTOM Assuming an average per-capita residential space use of 47.5 square metres, the remanence effect calculated in this way corresponds to residential space for just under 1.3 million people, around 0.45 million of them in the major cities alone.

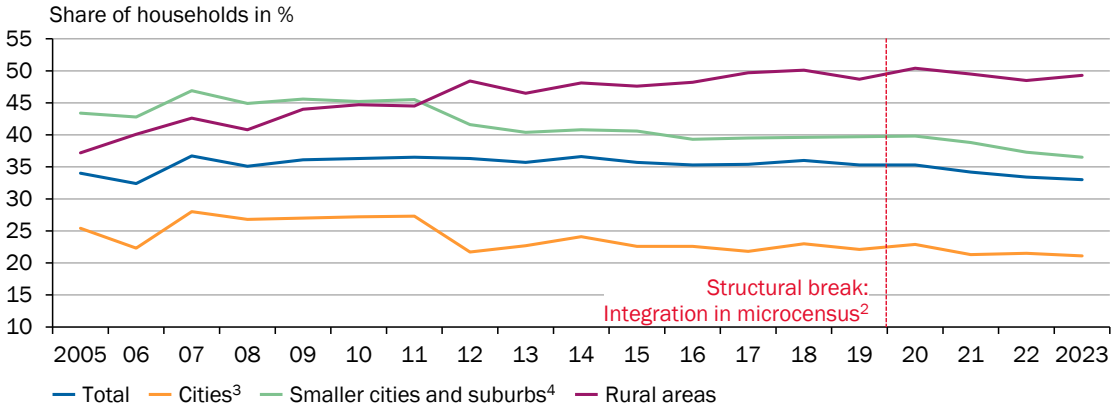
336. The use of residential space also differs according to the degree of urbanisation. While in 2023 **around half** of households in **rural areas** lived in **under-occupied housing** according to the EU definition ↘ GLOSSARY, this only applied to **around 20 %** of households **in cities** (Eurostat, 2024a). ↘ CHART 79

3. Supply of housing

337. The creation of housing is determined by the availability and prices of building land, capacity in the construction industry, regulatory requirements and financing conditions. The regional differences in the development of demand for housing compare with a **relatively inelastic short-term supply of housing**. While there are rising numbers of vacancies in the shrinking regions, the supply of housing in the growing cities is not increasing sufficiently.

↘ CHART 79

Under-occupancy[1] dwellings over time



1 – A dwelling is considered under-occupied if the household living in it has the following minimum number of rooms: One room for the household, one room for each couple in the household, one room for each single person aged 18 years and older, one room for each couple of single persons of the same sex aged between 12 and 17, one room for each single person aged between 12 and 17, not included in the previous category, one room for each pair of children under 12. 2 – In 2020, the random-based sample of the EU-SILC survey was more than doubled and an obligation to provide information was introduced. In addition other survey forms of questioning are used in addition to the paper questionnaire and the processing procedures have changed. Due to these methodological improvements, the results from 2020 are only comparable with previous years to a limited extent. 3 – Cities: At least 50 % of the population lives in adjacent areas (size one square kilometer) with a density of at least 1,500 persons per square kilometer and a population of at least 50,000 persons. 4 – Smaller cities and suburbs: Adjacent areas (size one square kilometer) with a population density of at least 300 persons per square kilometer and a population of at least 5,000 persons. 5 – Rural areas: More than 50 % of the population lives in areas outside urban areas.

Source: EU-SILC

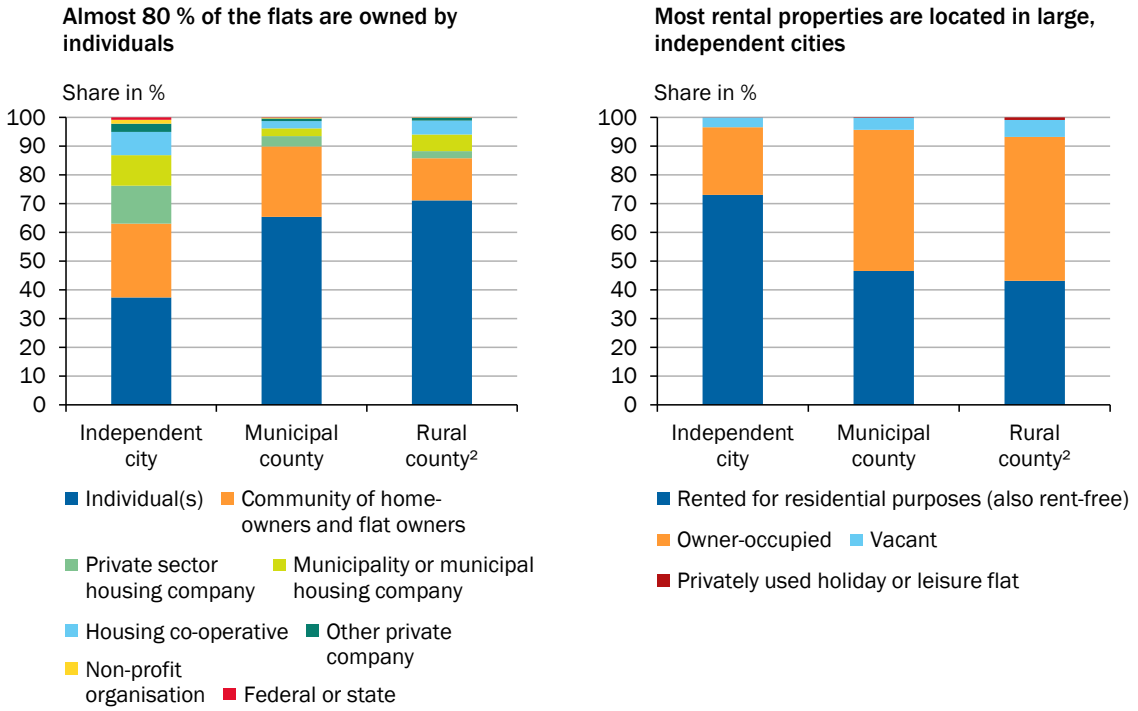
Housing stock and developments in residential construction

338. **The majority of apartments** (i.e. housing units) in Germany, **including rented apartments, are owned by private individuals** or by owners' associations. ↘ CHART 80 LEFT In larger cities, private housing companies, housing cooperatives and public, primarily municipal, housing companies are also increasingly active. Across all county types, municipalities and municipal housing companies own around 6 % and the federal and state governments around 0.3 % of the housing stock. Over 70 % of the apartments in larger cities are rented out for residential purposes. In other county types, apartments are more frequently owner-occupied. ↘ CHART 80 RIGHT According to Eurostat, Germany had a home-ownership rate of around 47 % in 2022, well below the EU average of 69 %. The reasons for this difference are manifold and can be attributed to institutional (Voigtländer, 2009; Kaas et al., 2021) and behavioural economic reasons (Malmendier and Wellsjo, 2024).

339. Housing in Germany is predominantly built by **private households** and **private housing companies**. ↘ CHART 81 Although public housing construction gained slightly in importance in the 2010s, it remains quantitatively insignificant with a share of 4.5 % of building completions in 2023. Outside Germany, the role of the state in housing construction is sometimes larger (OECD, 2024a). In Austria especially, and above all in Vienna, the state has traditionally played a major role in the creation of housing. ↘ BACKGROUND INFO 13

↘ CHART 80

Types of ownership and use of residential property by county type[1] in Germany in 2022

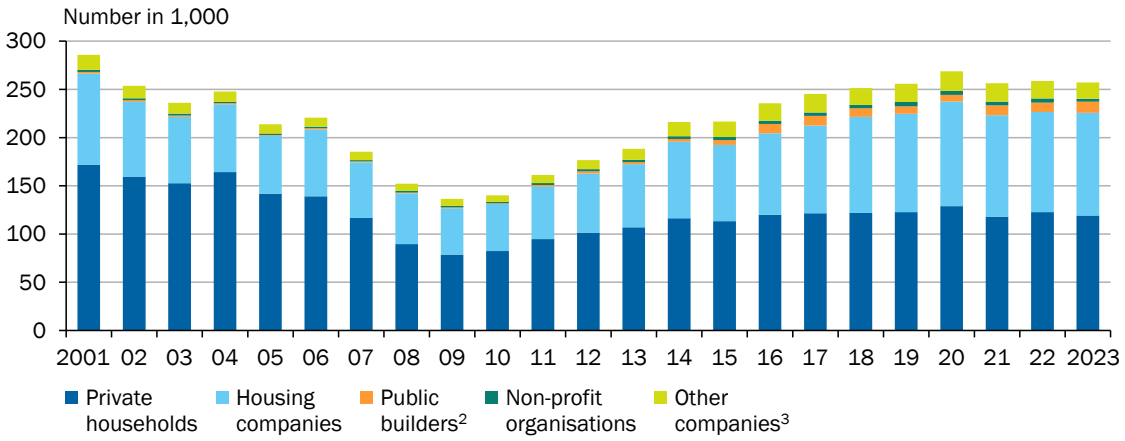


1 – Settlement-structural county types according to the BBSR categorisation. 2 – Contains the settlement-structural county types „Rural county with densification approaches“ and „Sparsely populated rural county“.

Sources: Statistical Offices of the Federation and the Länder, own calculations

↘ CHART 81

Development of building completions in residential construction[1] by client
Share of public housing construction remains comparatively low



1 – Construction of new residential buildings. 2 – Federal, state, local authorities and municipal housing companies in which the local authority, state or federal government holds more than 50 % of the nominal capital or voting rights. 3 – Includes property funds, companies in the agriculture, forestry and fishing, manufacturing, trade and other sectors.

Sources: Federal Statistical Office, own calculations

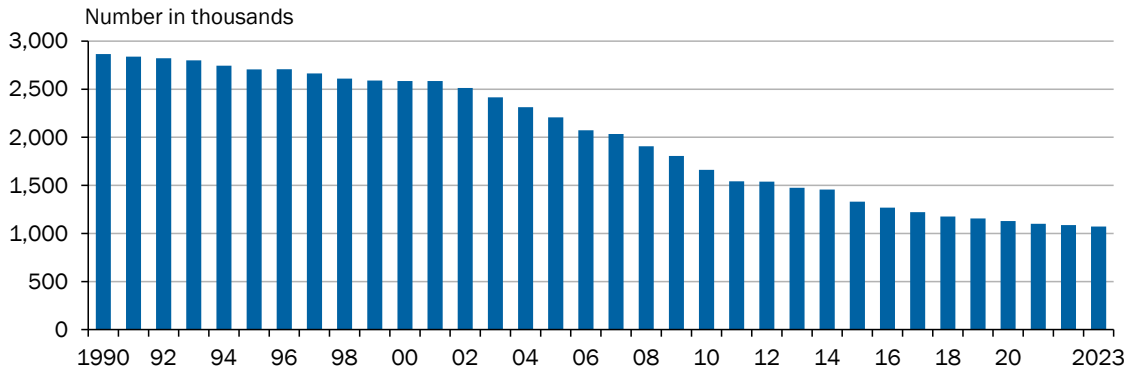
340. Public housing is not to be equated with social housing, which is subject to a legal commitment to only let to socially entitled tenants. **Social housing** refers to the **state-subsidised creation of housing subject to certain conditions** for groups of people who have difficulties finding affordable housing on the free housing market. ↘ BACKGROUND INFO 11 In all federal states, access to social housing requires a housing entitlement certificate. ↘ BACKGROUND INFO 11 ↘ TABLE 17 New construction, modernisation and the acquisition of occupancy rights ↘ GLOSSARY create new tied-rent and occupancy-controlled social housing. Once the commitment to only let to socially entitled tenants expires, social housing can be rented out at market prices. Since 1990, and especially since the early 2000s, the stock of social housing in Germany has been continuously declining (Deschermeier et al., 2023a). ↘ CHART 82 LEFT

The accelerated decline in the stock of social housing in Germany since the 2000s is primarily due to the fact that a large number of social housing commitments that had been created in previous decades have expired without the same number of new social apartments with commitments being created. In 2001, the Housing Promotion Act (WoFG) further developed the social housing system into a social housing promotion programme. ↘ BACKGROUND INFO 11 In addition to the creation of new social housing, which had previously been at the centre of funding policy, support was subsequently also given to upgrading the quality of the housing stock to meet contemporary housing needs. This was because the housing market was considered to be largely balanced towards the end of the 1990s (BBSR, 2011). In the years that followed, the amount of funding approved for social housing subsidies fell considerably, and the construction of new social housing was particularly affected by this decline (BBSR, 2011). In addition, many municipalities and federal states sold their public housing to private investors in the years between 1999 and 2011 for financial reasons (Held, 2011; Voigtländer, 2018).

↘ CHART 82

Development of the stock of social housing[1]

Number of social housing units in sharp decline



1 – All subsidised flats that were subject to occupancy restrictions at the relevant time.

Sources: BAGW (2023), Deutscher Bundestag (2024)

341. Calculations by Deschermeier et al. (2023a) show that an average of **40,000 apartments** will lose their **social housing status every year up until 2035**. In order to keep the social housing stock in Germany constant, more than twice as many new social housing units would have to be built each year or created through the acquisition of occupancy rights compared to recent years, in which around 20,000 additional social housing units were built each year. As a percentage of the total housing stock, Germany had a low stock of social housing by OECD comparison in 2022 (OECD, 2024a).

↘ BACKGROUND INFO 11

Background: Social housing and social housing support

The purpose of social housing support is to provide affordable rental housing and to support the creation of owner-occupied housing. The creation of housing suitable for the disabled and the energy-efficient modernisation of housing are also subsidised by many federal states and local authorities. The Federal Government supports social housing construction by granting financial assistance. **Social housing** refers to the area of social housing support that is eligible for federal financial assistance. This includes the **creation of new housing** (through new construction or the acquisition of occupation rights) and the **modernisation of housing**. Funding is provided by granting **low-interest loans and awarding subsidies which are tied to** rent controls and occupancy commitments that ensure the creation of rental housing for specific groups of people. Social housing support is aimed at both private investors and public corporations. In return for the subsidy, investors are obliged to create housing that is rented **at rates below the local reference rent during the commitment period** and only to households that can furnish a certificate of eligibility. As a rule, another condition is that the residential space provided must be proportionate to the size of the respective household. Local authorities issue a **housing entitlement certificate** if the relevant income limits, which vary according to household size, are not exceeded. ↘ TABLE 17 **The duration of the social commitment** varies from one federal state to another and depends on the funding conditions, but is **generally at least 20 years** (BMWSB, 2024a). Since socially deprived problem areas emerged especially in the 1970s where many social housing units had been built, the funding

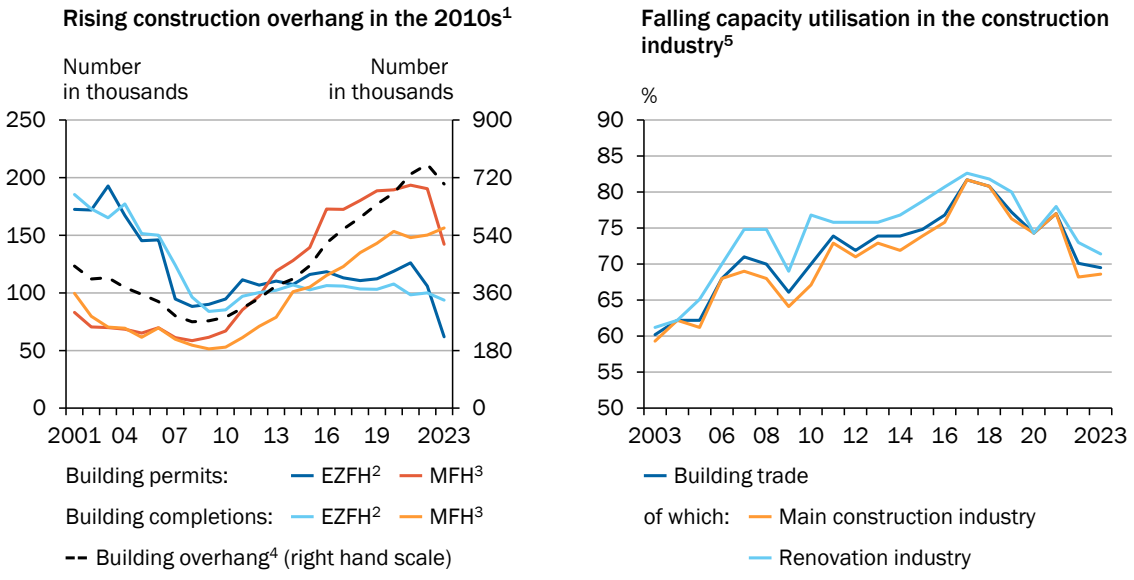
conditions of the federal states generally also contain clauses that are intended to ensure a socially mixed urban structure, for example via minimum quotas for non-subsidised housing. A special feature of Germany compared to other European countries is the existence of quasi-social municipal housing construction. Such projects are not subject to the legal social obligation of social housing support, but access is de facto restricted by similar rent and occupancy regulations based on decisions made by their public shareholders.

342. Since the Federalism Reform I in 2006, the **federal states** have had **exclusive legislative and enforcement powers for social housing support** ↘ BACKGROUND INFO 11. The Federal Government supports social housing construction in the federal states by providing financial aid, with the aim of slowing down and reversing the decline in the social housing stock (Bundesregierung, 2022). Between 2022 and 2028, the Federal Government plans to provide a total of €21.65 billion for social housing construction. Each euro from the Federal Government is currently co-financed with around €1.50 from the federal states. This means that about €54 billion should be available for social housing construction by 2028 (BMWSB, 2023). This corresponds to public spending of around 0.2 % of gross domestic product (GDP) per year, a significant increase compared to previous years. By OECD comparison, support for social housing would then be in the upper midfield, but lower than in Austria and France, for example (OECD, 2024a).

343. In the early 2000s, new residential construction focused primarily on the construction of detached and semi-detached houses (EZFH). In the 2010s, however, more multi-family houses (MFHs) were built, ↘ CHART 83 LEFT and the number of

↘ CHART 83

Building permits and completions by building type and capacity utilisation in the construction industry in Germany



1 – Apartments in new residential buildings. 2 – Residential buildings with 1 or 2 flats. 3 – Residential buildings with 3 or more flats. 4 – Number of construction projects in residential and non-residential buildings authorised but not yet completed (or not yet started) at the end of the year. 5 – Figures for the 4th quarter in each case.

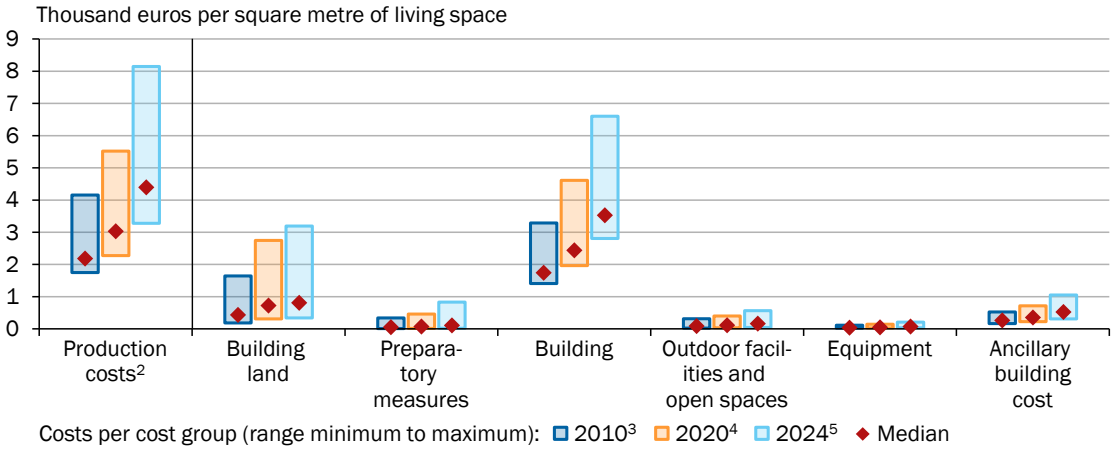
Sources: BBSR, Federal Statistical Office

building permits for MFHs increasingly exceeded the number of completions. This high construction overhang is due to the **sharp increase in permits for multi-family houses**, which require a longer construction period than single-family houses. Furthermore, the average **construction period** (after planning permission) has **increased**, which can be partly attributed to a high level of capacity utilisation in the construction industry (Simons et al., 2023). ↘ CHART 83 RIGHT Recently, rising construction costs, especially sharp increases in material and financing costs, have contributed to a slump in building permits, especially for the construction of single-family homes (Just, 2023; Michelsen, 2023). ↘ CHART 83 LEFT ↘ BOX 20 A sharp decline in the number of completions is not yet apparent. A large proportion of construction projects that have already been started will probably be completed, so that the decline is likely to be delayed. However, the construction backlog could decrease in the coming years, as many orders were cancelled in 2023 and there are currently hardly any new orders in residential construction (Leiss and Wohlrabe, 2024). ↘ ITEM 57

The energy-related modernisation of the housing stock in Germany has been **slow** to date. In order to achieve climate neutrality in the building sector by 2050 in line with the relevant voluntary commitments at the EU level, the Federal Government is currently aiming to modernise the energy efficiency of 2 % of buildings every year from 2020. The actual refurbishment rate in 2023 was just over 1 %; for multi-family houses, it is as low as 0.6 % (EEM, 2024; Knoche et al., 2024). One consequence of this is that home-owners already benefit to a greater extent from the more favourable operating costs of climate-neutral heating systems compared to tenants (Grimm et al., 2023).

↘ CHART 84

Range of production and building land costs for new residential construction in major German cities[1]



1 – Based on the evaluation of completed and invoiced construction projects for apartment blocks in major German cities (cities with more than 100,000 inhabitants). Gross costs incl. VAT according to the cost groups of DIN 276 (2018-12). 2 – Construction costs include all cost groups shown apart from building land costs. 3 – Annual average includes over 260 new construction projects with approx. 7,000 flats. 4 – First quarter includes over 590 new construction projects with approx. 18,000 flats. 5 – First quarter includes over 630 new construction projects with approx. 20,000 flats.

Source: ARGE e.V.

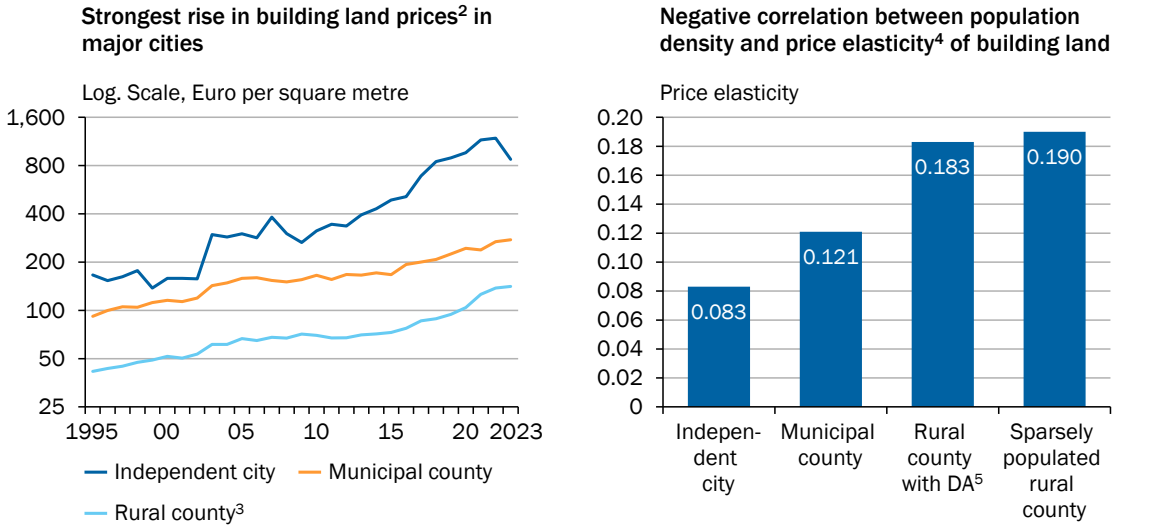
Cost trends in residential construction

344. The **prime costs for residential buildings rose sharply** between 2010 and 2024. ↘ CHART 84 Most of the costs are attributable to the construction of the building and the purchase of the land (including closing costs). Land costs rose particularly sharply between 2010 and 2020, especially in regions where the prices were already higher. In addition to the general price rises for building land ↘ CHART 85, the rise in closing costs, particularly the increase in real estate transfer tax, also had a noticeable impact here. ↘ CHART 84 ↘ BOX 24 Since 2020, construction costs have made a significant contribution to the increase in building costs for residential buildings. ↘ CHART 84 This is due both to higher prices for building materials and to higher quality standards and legal requirements, for example in terms of energy efficiency. ↘ BOX 21

345. The **increase in residential property prices** ↘ CHART 71 has been largely due to **rising building-land prices** since the early 2010s. ↘ BOX 20 Average purchase values of buildable but undeveloped land have risen the most in regions with a high demand for housing. ↘ CHART 85 LEFT This indicates an **increasing scarcity of undeveloped building land** in these regions. The price elasticity of building land is negatively correlated with population density. ↘ CHART 85 RIGHT Compared to urban regions, rural regions are expanding their residential building land significantly more in response to rising prices.

↘ CHART 85

Development of purchase values of building land ready for construction and estimation of building land elasticities by county type[1]



1 – Settlement-structural county types according to the BBSR categorisation. 2 – Weighted by number of sales of building land. Up to and including 2002 without values for Hamburg. 3 – Contains the settlement-structural county types „Rural county with densification approaches“ and „Sparsely populated rural county“. 4 – Results of an OLS regression, with the dependent variable comprising the logarithmised residential building areas in hectares and the explanatory variable the logarithmised purchase prices for residential building land in euros per square metre. For time-invariant factors, calculations were carried out at county level. Calculations based on the period 2008 to 2022. The calculation is only based on districts that had complete data for this period. 5 – Rural county with densification approaches.

Sources: Federal Statistical Office, Statistical Offices of the Federation and the Länder, own calculations

↘ BOX 21

Focus: The role of regulatory requirements for residential construction

Federal, state and municipal levies and requirements (e.g. taxes, fees, building regulations) **influence** the **construction costs of residential buildings**. According to an evaluation by the Institute for Sustainable Construction (Gniechwitz et al., 2023) for the fourth quarter of 2022, changes in these requirements have contributed to an increase in construction costs of €575 per square metre since 2000. This corresponds to approximately 12 % of the total costs for new residential construction in urban areas in the fourth quarter of 2022.
In principle, building regulations fulfil important functions in the field of danger prevention (e.g. fire protection, stability) and ensure the fulfilment of minimum requirements. In terms of contract law, residential construction is based on the generally accepted engineering standards, which are not defined by law. Courts take the fulfilment of all relevant standards into account when determining material defects (BMWSB, 2024b). This in turn means that construction companies orient themselves towards the highest standards, which increases construction costs. According to calculations by Deschermeier et al. (2023b), requirements such as the obligation to provide **parking spaces for cars and bicycles**, which is regulated in state building regulations or municipal ordinances, account for an average of around 10 % of the asking price of new-build apartments. The requirements for parking spaces are higher than the actual number of cars kept, especially in urban locations with many small apartments or households.

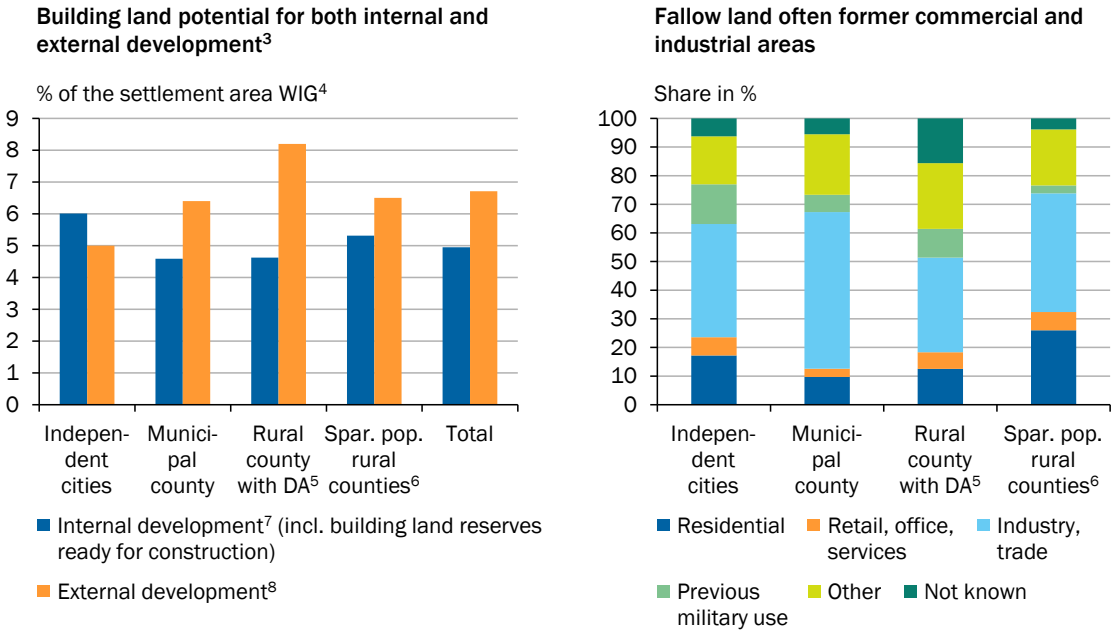
Due to the longevity of housing, building regulations also serve to set the course at an early stage for long-term societal goals such as climate neutrality. There is a conflict of objectives between improving the climate footprint of buildings and low construction costs. This can be seen in the energy requirements for buildings in accordance with the Building Energy Act and in the obligation to install a solar system on new buildings and significant roof structures introduced in Baden-Württemberg, Berlin and Hamburg.

In the past, the **construction of additional residential space in existing buildings**, e.g. by converting attics, adding storeys or changing use, was hampered by building regulations (BBSR, 2016; Deutscher Bundestag, 2019). These included stricter requirements if there was a need to change the building class, the abolition of the protection of existing buildings, and the mandatory installation of lifts above a certain number of storeys. These **obstacles** were **largely addressed** as part of the amendments to the Model Building Regulation in 2022 and 2023. For example, in future, the additional parking space obligations and accessibility requirements will no longer apply to loft conversions and extensions. In addition, fewer fire protection requirements must be met for loft conversions compared to before, even if a higher building class is achieved due to the larger number of apartments. In addition, the protection of existing buildings was extended for changes of use for residential purposes. Furthermore, a change of use for residential purposes does not require authorisation in the case of attics. However, the changes only become legally binding once they have been adopted into the respective state building regulations. Up to now, only the states of Bremen, Lower Saxony, Schleswig-Holstein and Thuringia have transposed these amendments to the model building code into state law.

346. The options for **designating new building land** (external development) tend to be **more limited in large cities** than in rural regions. ↘ CHART 86 LEFT In order to increase the supply of building land, municipalities are required to prioritise the use of potential building land by activating brownfield sites or gaps between buildings (internal development potential) and building land that is already available for building (Section 1 (5) BauGB). ↘ CHART 86 LEFT In large cities, this potential consists mainly of brownfield sites that were previously mostly used by industry and commerce or military facilities. ↘ CHART 86 RIGHT According to the 2020 Building

↘ CHART 86

Building land potential[1] and previous utilisation of brownfield sites by county type[2]



1 – Weighted results based on the representative building land survey of the BBSR. The survey was conducted at municipality level. 2 – Settlement structure county types according to the BBSR categorisation. 3 – Large, independent cities have a more comprehensive coverage of building land potential than rural counties, which is why the differences between the county types can only be interpreted to a limited extent. 4 – Settlement area for housing, industry and commerce. 5 – Rural county with densification approaches. 6 – Sparsely populated rural county. 7 – Activation of brownfield sites or gaps between buildings. 8 – Designation of new building land. External development is made up of long-term development plan potential (raw building land; without secured development) and long-term potential from the land utilisation plans (building land). The survey did not differentiate between the intended type of use.

Sources: BBSR, Building land survey 2020, calculations by the IOER on behalf of the BBSR/BMI, BBSR

Land Survey, almost all major cities expect a further increase in inner-city development potential over the next five years (Blum et al., 2022). In 40 % of cities, this will result from the relocation of businesses to the outskirts and in 20 % from the abandonment or relocation of agricultural or horticultural land. The directly usable land potential in Germany in 2020, assuming the current building density, amounts to 1.1 million residential units. The direct mobilisation of this potential could cover the demand for housing for the next three to six years, depending on existing housing demand forecasts. ↘ ITEM 350

↘ BOX 22

Focus: Conversion potential for commercial properties

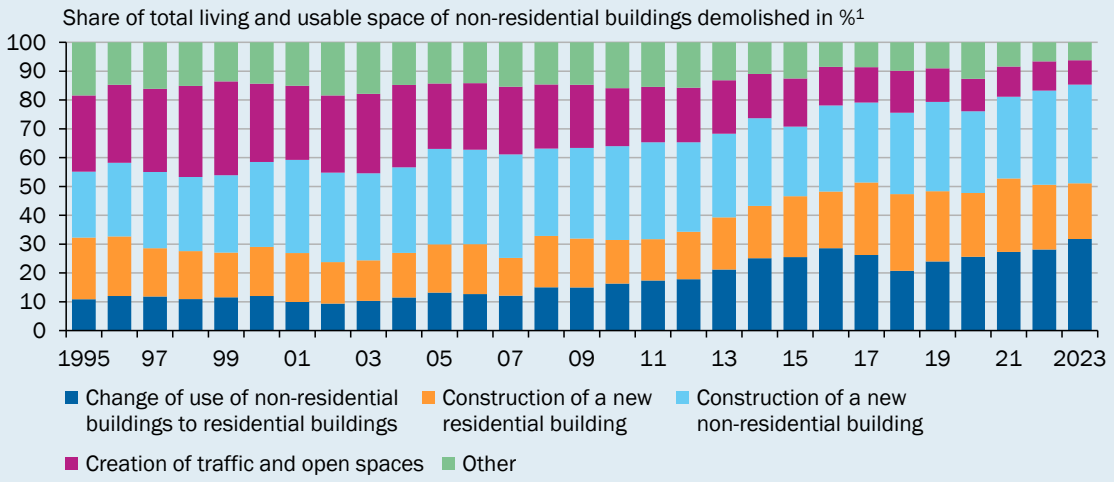
Demand for commercial property has been **declining** for several years, both for office and retail properties (Krause et al., 2024). On the one hand, many employees have been working from home since the COVID-19 pandemic; ↘ ITEM 330 on the other, bricks-and-mortar retail has been recording significantly lower sales growth than online retail for some time now (Federal Statistical Office, 2022). A structural change in the use of commercial property can already be seen in the disposals from the non-residential capital stock. ↘ CHART 87 These include all non-

residential buildings that either remain in place and are converted into residential buildings, or are completely demolished, rebuilt and used as new residential buildings, non-residential buildings or transport and open spaces. Relative to the total number of non-residential disposals, the **conversion of non-residential buildings to residential buildings** in particular **has been on the increase since the 2000s**. The construction of new residential buildings has also increased over time, although this trend has slowed in the last two years due to weak building activity.

In view of the sharp rise in demand for housing, vacant commercial properties could increasingly be converted into residential units. In 2021, the Institute for Sustainable Construction estimated the conversion potential of office and administrative building space at a total of 235,000 new residential units across Germany up to 2025. By 2040, a total of 1.86 million apartments could be created in this way (Walberg and Gniechwitz, 2020). A recent study based on the office-market database of the Colliers firm of property consultants estimates the conversion potential of office properties in the 21 largest German cities at a maximum of 170,000 to 200,000 new residential units (Colliers et al., 2024). Another study based on linking the Colliers office-market database with the ifo Institute's corporate surveys on the use of home offices estimates the future conversion potential of office properties in the seven largest German cities at a maximum of 60,000 new apartments (ifo Institute, 2024). The studies' results differ because different regions were considered and different assumptions were made on home office quotas and conversion costs.

↘ CHART 87

Change of use of non-residential buildings to residential buildings on the rise since the 2000s



1 – The following causes of disposals are counted as disposals of non-residential buildings: Non-residential buildings that either remain and are converted into residential buildings, are completely demolished and then built and used as new non-residential buildings, new residential buildings or traffic and open spaces, and other. The residual items (inadmissibility under building regulations, exceptional events and other reasons) are summarised under other.

Sources: Federal Statistical Office, own calculations

Although rents for apartments exceed those for offices in the lower segment, there could be incentives for corresponding capital formation from a private-sector perspective (Ochs, 2023). Several new building regulations also simplify the design and development of mixed neighbourhoods (Mixed-Use Immobilien; Bundesrat, 2021; Bunzel et al., 2023; Machts, 2023). However, property developers continue to expect **high conversion costs** (Heintze, 2024). In addition to the high building standards, there are major **hurdles in the approval process**, for example when it comes to providing evidence of green spaces and parking. ↘ BOX 21 Furthermore, the

regulatory requirements in the energy sector increase the planning risks under building law, so that, depending on the structural conditions, a conversion can be similar to a new build in terms of costs.

III. CHALLENGES: AVAILABILITY AND ACCESS TO HOUSING

347. The tight situation on the housing market is generating **a macroeconomic and a social challenge**. Firstly, there is a **low availability of housing in urban areas** compared to demand, caused by low construction activity ↘ ITEMS 350 FF. and frictions in relocation behaviour ↘ ITEMS 357 FF. This could restrict the access of labour to productive companies and thus have a negative impact on macroeconomic development. ↘ ITEM 348 F. Secondly, there is limited **access to adequate housing for low-income and disadvantaged population groups**. ↘ ITEMS 366 FF. This can be caused by high housing costs and discrimination in tight housing markets. In regions where demand is especially high, overcrowding occurs, especially among socially disadvantaged groups. ↘ ITEMS 369 FF.

1. Lack of availability in urban areas

348. The growing **scarcity of housing** in urban areas can **restrict** the **spatial mobility of labour** in Germany. The analysis of internal migration in Germany shows that high rents have a steering effect, i.e. they can reduce the influx into a region and even increase the outflow from large cities. ↘ ITEM 329 However, urban areas have a higher average productivity than rural areas (Belitz et al., 2019). This could become even more pronounced in the future if the economic structure shifts towards knowledge-intensive services, as these benefit particularly from agglomeration effects (Eckert et al., 2022; Chen et al., 2023). Measures that give workers access to more productive companies can **increase macroeconomic productivity** in Germany. ↘ BOX 23

↘ BOX 23

Background: Macroeconomic productivity effects of the housing market

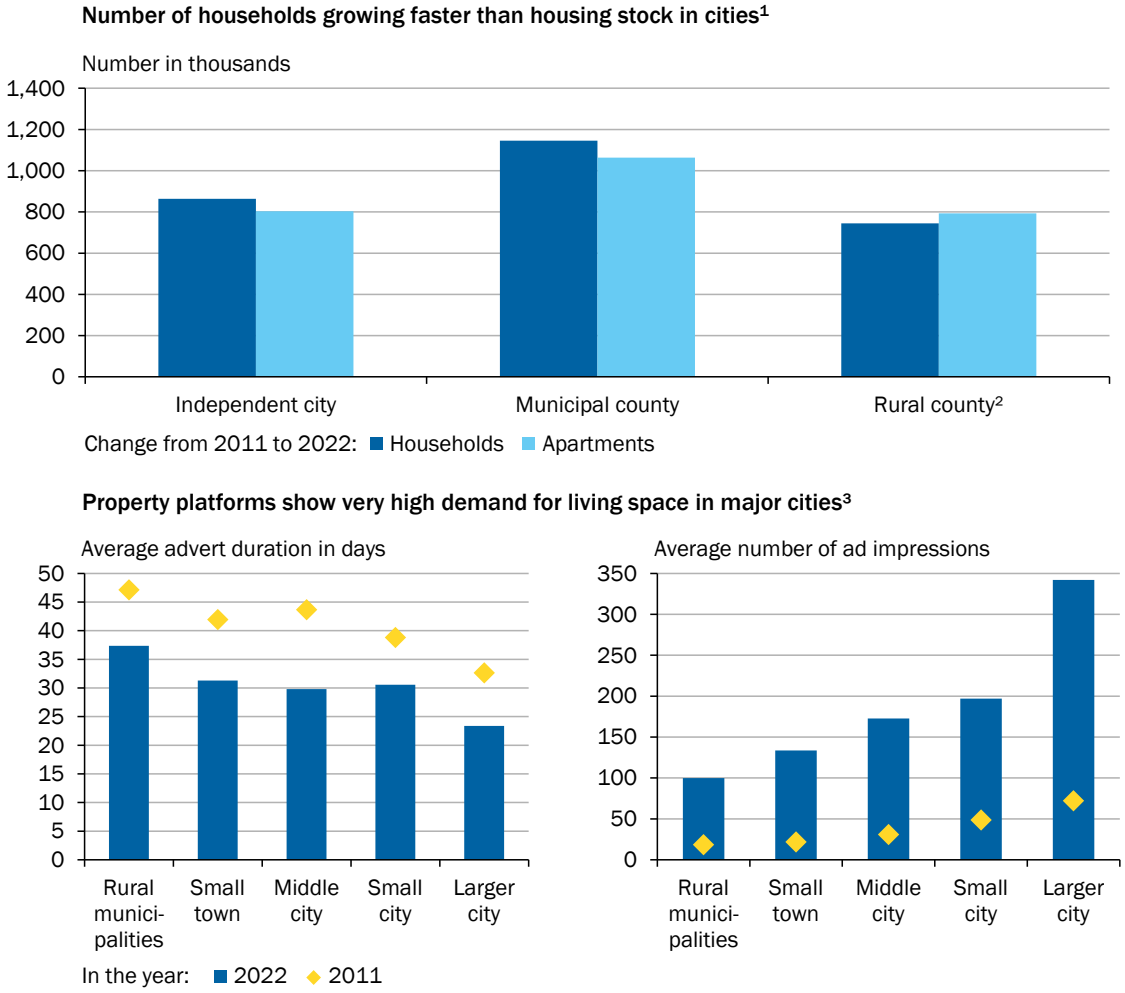
For Germany, there is as yet no estimate of the macroeconomic productivity effects of frictions on the housing market. **Studies for the United States** indicate that the s**low expansion of available housing in** particularly **productive regions** in recent decades has also slowed the influx of labour and thus **dampened macroeconomic development** (Ganong and Shoag, 2017; Herkenhoff et al., 2018; Hsieh and Moretti, 2019). Above all in New York and California, there are particularly strict land-use restrictions that make it difficult to expand the supply of housing (Saiz, 2010). Herkenhoff et al. (2018) estimate that reducing these restrictions to the 1980 level would have increased macroeconomic productivity in the United States by 7 % and

consumption by 5 % in 2014. Hsieh and Moretti (2019) estimate that if land-use restrictions in New York, San Jose and San Francisco had been reduced to the level of the median for US cities, GDP in the United States would have been 3.7 % higher in 2009. However, these studies may be overestimating the actual macroeconomic effects (Glaeser and Gyourko, 2018). For example, they assume that any negative externalities of additional housing are the same in every region and that there are no regional differences in construction costs. It is also unclear whether employees are actually as willing to relocate as the studies assume.

349. The availability of housing also poses a challenge in view of the planned future **immigration of foreign workers**. For example, an annual net immigration of 400,000 people would be necessary to achieve a constant labour-force potential up to 2035 (GCEE Annual Report 2022 item 356). Based on previous external migration movements, immigration at this level is likely to **additionally**

↘ CHART 88

Regional development of demand and supply of housing



1 – Settlement-structural county types according to the BBSR categorisation. 2 – Contains the settlement-structural county types „Rural county with densification approaches“ and „Sparsely populated rural county“. 3 – Calculations are based on information on advertised flats and houses for rent on the ImmobilienScout24 platform. City and municipality types according to the BBSR categorisation.

Sources: RWI and ImmobilienScout24 (2024a, 2024b), Statistical Offices of the Federation and the Länder, own calculations

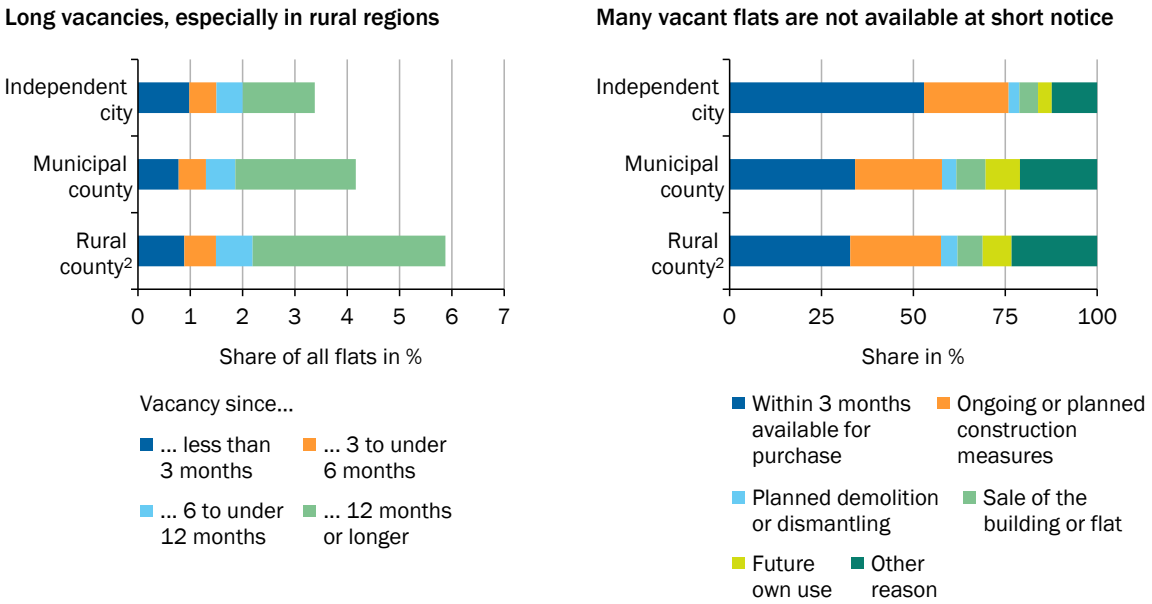
increase the demand for housing, especially in urban areas. ↘ ITEM 331 An even greater tightening of these housing markets could reduce Germany's attractiveness as a country of immigration. In addition, the lack of housing and high housing costs in urban areas could reduce acceptance of immigration among the population. According to a representative population survey, the majority of respondents in Germany state that immigration is a burden on the welfare state, leads to problems in schools and creates housing shortages in urban areas (Wieland, 2024).

Insufficient development of housing

350. Despite high demand and rising prices for housing, the **housing stock** in large cities and urban counties **grew more slowly** between 2011 and 2022 than household growth. ↘ CHART 88 ABOVE However, this analysis probably underestimates the actual demand for housing due to unrealised demand (e.g. relocations that were not carried out due to a lack of supply). An analysis by the GCEE based on advertisements on the real estate portal Immobilienscout24 shows that the number of days an advertisement runs in the major cities is significantly lower and the average number of views per day is significantly higher than in the other county types. ↘ CHART 88 BOTTOM Although successful transactions can be expected to occur more quickly in larger property markets due to a higher probability of finding a suitable buyer or seller (Nenov et al., 2016), the results indicate that the demand for housing considerably exceeds supply in the major cities. Estimates on the future need for additional housing, which are based on the extrapolation of previous developments, range between 168,000 (in the years 2024 to 2027) and 302,800 apartments per year (in the years 2026 to 2030) (Braun and Grade,

↘ CHART 89

Duration and reasons for residential vacancies by county type[1] in 2022



1 – Settlement-structural county types according to the BBSR categorisation. 2 – Contains the settlement-structural county types „Rural county with densification approaches“ and „Sparsely populated rural county“.

Sources: Statistical Offices of the Federation and the Länder, own calculations

2024; Deschermeier et al., 2024). The calculated requirements are mainly concentrated in the urban areas and depend heavily on the assumed level of immigration.

351. In the past, demand pressure in major cities could still be partially absorbed by **reducing vacancies**. These reserves have now been largely used up (BBSR, 2021). ↘ CHART 89 LEFT A large proportion of the housing stock in the major cities has been placed on the market and, if still vacant, is available for occupation at short notice. ↘ CHART 89 RIGHT If apartments cannot be occupied in the short term, this is usually due to planned or ongoing construction work. **Vacant apartments are mainly found in rural and economically weaker regions**.

352. **A key obstacle to the expansion of the housing supply** is the insufficient **availability of building plots**. The designation of new building land is slow and does not necessarily take place where the demand for housing is highest. ↘ CHART 85 RIGHT Since 2010, according to calculations by the GCEE, residential building land in rural counties has grown by 29.7 %, almost twice as much as in urban counties (14.9 %). One reason for this is the lower overall land potential in cities. Another is the higher proportion of derelict land in urban areas, which is more difficult to convert into residential building land than new land. ↘ CHART 86 RIGHT For the major cities, it can be assumed that around 60 % of the land potential is directly usable or can be mobilised at short notice (within the next five years). Factors that make mobilisation more difficult are the unwillingness of owners, complex ownership structures, high costs of building land development and the unattractiveness of the plots (Blum et al., 2022).

353. **High building costs are a further obstacle to residential construction**. ↘ ITEM 344 In addition to price increases for building materials and higher labour costs, **more demanding legal requirements** also have an impact. ↘ BOX 21 In order to avoid legal risks, residential construction is always built to the highest standard at the respective point in time (generally accepted engineering standards), even if these only increase living comfort and have no relevance to safety issues (BMWSB, 2024b). This makes new builds, extensions and refurbishments more expensive. In addition, the differences between regional building regulations hinder the use of economies of scale in residential construction using serial and modular construction methods.

354. The designation of new building land always requires a balance to be struck between the interests of the local resident population ('insiders') and the creation of additional housing as a societal objective. Particularly in densely populated regions, there is often **resistance to new building land and residential projects** (Oberhuber, 2019; Niemann, 2020; Haimann, 2021; Effern, 2024; Haufe, 2024). Resident property owners fear a loss of value. The local residential population fears noise pollution, an excessive strain on the infrastructure and an increase in rents and real-estate prices (Hankinson, 2018; Hager et al., 2022; Nall et al., 2024). The potential loss of a residential neighbourhood's cultural and social characteristics can also trigger resistance (Ahlfeldt, 2011). Local resistance to construction projects makes it more difficult for outsiders to access housing and can prolong approval processes and increase construction costs. From an

economic perspective, however, an increase in supply is likely to lead to falling prices for housing. Yet in the immediate vicinity of new buildings, prices can also rise depending on the residential location and building size if the new buildings contribute to an upgrading of the neighbourhood (Zahirovich-Herbert and Gibler, 2014; Diamond and McQuade, 2019; Li, 2022; Asquith et al., 2023).

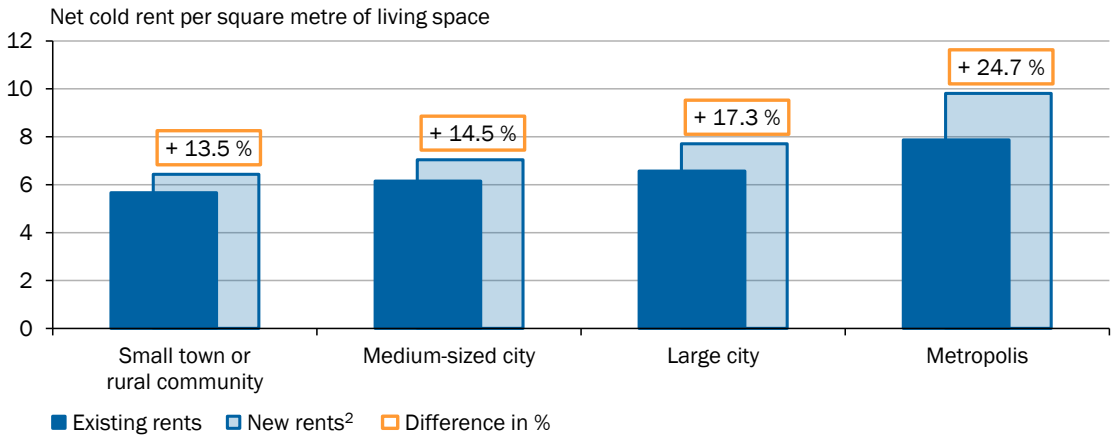
355. **The housing potential in the areas surrounding** major cities is hitherto not yet being **used to the same extent everywhere**. The accessibility of major cities can be an important factor in the choice of where to live. In the 20 most populous major cities, there is a positive correlation between public transport connections to neighbouring counties and the proportion of commuters. The accessibility of the city centre by public transport increases the attractiveness of the surrounding regions (Gibbons and Machin, 2005; Ahlfeldt and Wendland, 2008). Analyses by the Federal Office for Building and Regional Planning (BBSR) show, for example, that population growth around Hamburg was particularly high in regions with a travel time of less than 60 minutes to the city centre (Pütz and Schönfelder, 2018).

Obstacles to the reallocation of residential space

356. In addition to developing new housing, part of the increased demand for residential space could also be met by **more efficient use of the existing space**. However, this is made more difficult by both social and financial barriers to relocation. Social hurdles lie, for example, in an **attachment to one's own home** and the associated **social environment**. For many people, this increases, the longer they live in the same place; it thus inhibits their willingness to move, especially among older people (remanence effect). ↘ ITEM 335 For people with health-related restrictions, the organisational and physical burden of moving can play a role.

↘ CHART 90

High gap between existing and new rents in major cities in Germany[1]



1 – Size by population: small town or rural municipality up to less than 20,000 people; medium-sized city 20,000 to less than 100,000 people; large city 100,000 to less than 500,000 people; metropolis 500,000 and more people. 2 – New tenants are tenants who moved into their current home less than two years ago. Based on the supplementary housing survey of the 2018 microcensus.

Sources: RDC of the Federal Statistical Office and Statistical Offices of the Länder, DOI: 10.21242/12211.2018.00.00.1.1.3, own calculations

Furthermore, the fact that people do not reduce their residential space in old age can also be attributed to the wish to keep guest rooms for family members or, in the case of owners, to an inheritance motive.

357. However, the efficient use of residential space is also hampered by the **low financial incentives to downsize** as a result of rent regulation and the high transaction costs on the purchase market. On the rental market, the increasing gap between existing and new rents is a particular obstacle. ↘ CHART 73 If this gap is large, tenants have little incentive to downsize their residential space, as a higher new rent reduces the financial benefits of downsizing. The gap between existing and new rents is greatest in large cities. ↘ CHART 90 The large gap between existing and new rents in Germany can mostly be attributed to legal regulations.

358. In Germany, **existing rents** are regulated by so-called **rent caps** (Section 558 of the BGB). These stipulate that the rent may not be raised cumulatively by more than 20 % within three years and up to a maximum of the standard local reference rent. ↘ BACKGROUND INFO 12 In addition, the federal states can, at their discretion, designate municipalities in which they say the supply of rental housing to the population at reasonable conditions is not guaranteed and introduce a rent cap of 15 % for a maximum period of five years. Index-linked tenancy agreements, where the rent is tied to the development of the consumer price index, and graduated tenancy agreements, where future rent increases are already agreed in the tenancy agreement, are exempt from the cap.

359. Some new rents are also regulated. Since 2015, the federal states have been able to designate regions as 'tight housing markets' for five years and apply the so-called '**rent brake**' there (Section 556d of the BGB). This regulation is currently limited in time until the end of 2025; an extension until the end of 2028 is being coordinated by the ministries. In tight housing markets, the amount of the new rent may not be more than 10 % above the level of the local reference rent. According to the definition of the rent brake, a tight housing market exists either if rents are rising significantly faster than the national average, the average rent burden for households is significantly higher than the national average, the resident population is growing without the necessary housing being created through new construction, or there is a low vacancy rate with high demand. Exceptions include fixed-term tenancy agreements and index-linked tenancy agreements. In addition, a rent that exceeded the upper limit in the previous tenancy may also be agreed in future contracts. **New buildings** that are let for the first time after 1 October 2014 **and completely renovated apartments** are also **not subject to the regulation of the rent brake.**

In principle, the rent brake also applies to the **letting of furnished apartments**, although it is **often difficult** for tenants to recognise breaches of the rent brake as the furnishing surcharge does not have to be explicitly stated in the rent. The proportion of furnished apartments has risen in recent years, especially in large cities. An analysis by the property platform ImmobilienScout24 shows that in 2022, 36 % of the rental apartments advertised on the platform in the five largest cities were offered furnished, so their share has doubled since 2018. A survey of tenants in Munich furthermore indicates that they often either do not notice

breaches of the rent brake or do not take action against them for fear of negative consequences (Sommer et al., 2024). Non-compliance with the rent brake is not sanctioned beyond the reimbursement of overpaid rents.

↘ BACKGROUND INFO 12

Background: Rent index

A **rent index is an overview of the customary local reference rent** which is drawn up or recognised by the competent authority under state law or jointly by landlord and tenant interest groups. The local reference rent is formed from the customary rents that have been agreed or changed in the municipality or a comparable municipality for housing of a comparable type, size, furnishings, quality and location in the past six years. Municipalities with a population of over 50,000 are required by law to prepare a rent index and must adapt it to market developments every two years. However, there are **no requirements regarding the type and quality of the survey**. By contrast, some local authorities use 'qualified' rent indices, which are prepared in accordance with recognised scientific principles. Qualified rent indices must be adjusted to market developments after two years and revised after four years.

The weighting of new and existing rents is not stipulated by law when preparing rent indices. In addition, rents from providers who (often according to their statutory mandate) charge lower rents than the market rate (e.g. housing associations) are also included. Various studies show that the **standard local reference rent** determined on this basis is **up to 36 % below the market price** for new lettings, especially **in highly sought-after residential areas** (Held et al., 2014; Sebastian, 2016).

360. **Limiting increases in existing rents** to protect tenants can be justified on economic grounds. Although tenants can theoretically move house to avoid excessive rent increases by landlords, in practice **relocation often involves considerable costs**. These costs are made up of the direct costs of moving, but more significant are usually the indirect costs that arise from the loss of the location-specific amenities that have been built up over the course of the tenancy (Diamond et al., 2019). These can include the loss of the social environment and a greater distance to the place of work or the child's school. The higher these costs are, the worse the **tenants' negotiating position** is and the higher the rent increases landlords can impose on existing tenants. State regulation of existing rents therefore protects especially tenants who would otherwise face high relocation costs.

361. **Limiting new rents** through the **rent brake** leads to a **redistribution from landlords to tenants** if the regulated rent is below the market price. Particularly in tight housing markets, tenants are thus protected from sharp price increases that can arise due to temporary shortages caused by the long time it takes to build new housing. ↘ ITEM 316 At the same time, the rent brake can help limit the extent to which existing and new rents in urban areas drift apart; it thus maintains the financial incentives for the efficient use of housing within the regulated rental market.

362. However, **rent caps** and a **rent brake** lead to a **market segmentation** that favours tenants who manage to obtain an apartment at a regulated rent

('insiders'). People looking for accommodation who can only find an unregulated rental property are put at a disadvantage. In addition, the surplus demand created by regulation leads to a rationing of regulated housing, which penalises those looking for accommodation who are unable to find an apartment even though they would be prepared to pay the regulated rent ('outsiders'). Rent regulation in this form is therefore not suitable as a distribution-policy instrument due to its lack of precision. Dworczak et al. (2021) argue that rent regulation only has the desired redistributive effects if there is a sufficiently large difference in quality between regulated and unregulated housing, so that higher-income tenants prefer unregulated housing despite the higher prices.

The **side effects of rent regulation** have been analysed in several international studies. Some show that artificially low rents can lead to a misallocation of households in regulated housing (Glaeser and Luttmer, 2003; Skak and Bloze, 2013; Oust, 2018). In extreme cases, a polarisation occurs in which tenants in price-regulated apartments have a greatly increased residential space per capita, while those in unregulated apartments can only afford very little residential space due to the high rents. In addition, it has been shown that tenants in regulated housing stay in their homes longer than those in unregulated housing, thus reducing overall spatial mobility (Munch and Svarer, 2002; Svarer et al., 2005; Diamond et al., 2019).

363. The past effects of the rent brake on the housing market in Germany have been evaluated. It turns out that the **rent brake effectively slows** the increase in **rents paid** for regulated apartments (DIW, 2018; Kholodilin et al., 2018; Henger et al., 2019; Breidenbach et al., 2022; Kholodilin, 2024). At the same time, however, the rent brake leads to **rising rents in the unregulated new-build segment** and reduces the mobility of tenants living in rent-controlled housing (Mense et al., 2023). **The exemption of newly built apartments and major renovations** from the rent brake **maintains investment incentives** (Gemeinschaftsdiagnose, 2018; Mense et al., 2019). To date, there has been no empirical evidence of a negative effect of the rent brake in its current form on new housing construction (DIW, 2018).

364. In the **purchase market for residential property**, the willingness to move is reduced by **high transaction costs**. These typically amount to between 10 and 15 % of the purchase price and include costs for the notary and the entry in the land register (1-2 %), a (possible) estate agent's commission (6-7 %) and real estate transfer tax (3.5-6.5 %). The real estate transfer tax set by the federal states ↘ BOX 24 in particular is high by European standards. The national average rate in 2022 was 5.3 %, well above the European median of 2 % of the purchase price (Barrios et al., 2019). Notary fees vary across Europe, ranging from 0.3 – 0.4 % in the Netherlands (Voigtländer, 2016) to 1 – 3 % in Austria (BMJ Austria, 2024).

International studies show that **transaction costs** in the residential property purchase market **reduce the number of property transactions** and thus the spatial mobility of households (van Ommeren and van Leuvensteijn, 2005; Hilber and Lyytikäinen, 2017; Best and Kleven, 2018; Eerola et al., 2021). For Germany, several studies have shown negative effects of the real estate transfer tax on

transaction volumes in particular (Petkova and Weichenrieder, 2017; Fritzsche and Vandrei, 2019; Christofzik et al., 2020). Fritzsche and Vandrei (2019) estimate that a 1 percentage point increase in the real estate transfer tax reduces the number of single-family home transactions by around 7 %. Petkova and Weichenrieder (2017) calculate on the basis of an estimated price elasticity for property transactions that a 1 % increase in real estate transfer tax reduces the number of transactions for single-family homes by 0.23 %, which implies a reduction in the number of transactions of around 4.3 % based on an average real estate transfer tax of 5.3 %.

365. **Brokerage commissions** in **Germany** are also **high** by European comparison. The average commission rates are less than 2 % in Sweden, Norway, the Netherlands and the United Kingdom and a maximum of 3 % in Denmark, Finland and Belgium (Stoll, 2023). Since the reform of estate agent fees in 2020, buyers in Germany have had to pay a maximum of half of the commission themselves. From the buyers' point of view, the average estate-agent commission has fallen as a result of the split. However, the total commission paid by both sides has risen, as some estate agents have raised the rates in cases where buyers used to pay the commission themselves (Stoll, 2023). At the same time, however, the proportion of commission-free offers has risen (Sagner and Voigtländer, 2021).

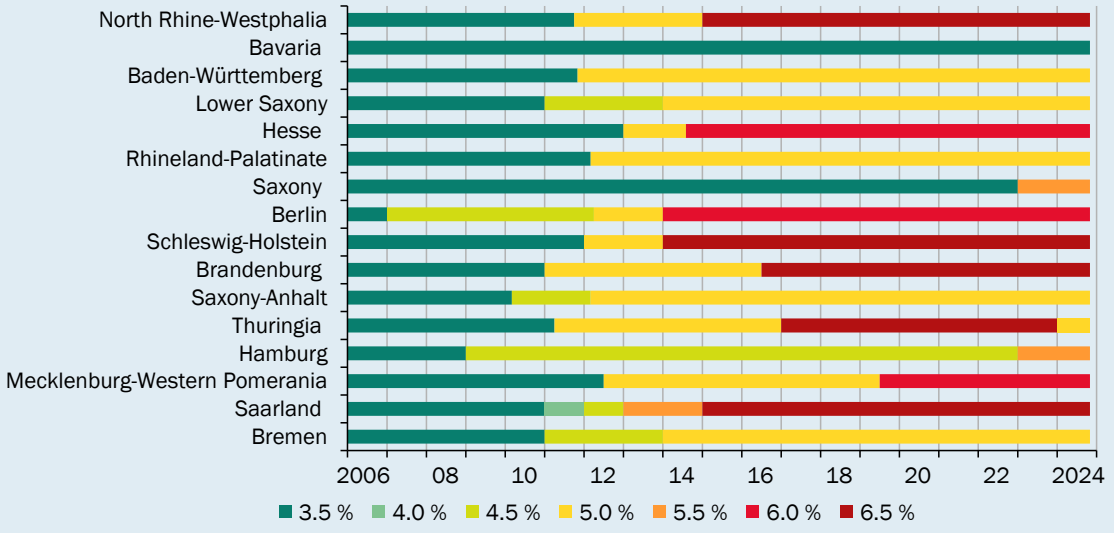
↘ BOX 24

Background: Real estate transfer tax

Real estate transfer tax is a **state tax**; since the federalism reform of 2006, each federal state has been able to set the **tax rate independently**; the revenue is solely due to the states. It has since been increased in almost all federal states. ↘ CHART 91

↘ CHART 91

Development of real estate transfer tax rates in the federal states



Source: Legislation of the federal states
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One reason for the rising tax rates is probably the otherwise very limited revenue autonomy of the federal states (Broer, 2015). Furthermore, the **Financial Equalisation Scheme** between

the federal states provides **incentives to increase taxes**. To enable the states to generate additional revenue from the real estate transfer tax without this being redistributed too much via the **Financial Equalisation Scheme**, the average tax rate of all federal states is used to determine the revenue strength of the respective federal state instead of the actual tax rate. Simulations indicate that this increases the incentive for further tax increases, as the states are partially compensated for revenue losses due to reduced transactions and lower prices as a result of a tax increase via higher transfers from, or lower contributions to the Financial Equalisation Scheme (Boysen-Hogrefe, 2017; Büttner and Krause, 2018).

The real estate transfer tax **places a particular burden on frequent** property **transactions**, since, in the case of repeated transactions, it is not only the interim increase in value that is taxed but always the entire purchase amount. **New construction** is also **particularly burdened** by real estate transfer tax, as double taxation often occurs (Rappen, 2012) if the buyers purchase the new building from a property developer who has already paid real estate transfer tax when buying the property.

real estate transfer tax can be avoided via so-called **'share deals'** by bundling properties in a specially created company. If less than 90 % of this is sold, the transaction is not subject to real estate transfer tax and the remaining shares can be purchased tax-free after ten years. Share deals are used in particular for large-volume property transactions (Bundesregierung, 2021).

2. Access for low-income and disadvantaged population groups

366. High real-estate prices and rents restrict **access to the housing market for low-income and disadvantaged households**. This is especially true in urban areas with particularly tight housing markets. **The high social relevance of rising rents** results from the fact that low-income households have an above-average relative rent burden. In 2022, tenant households in Germany spent an average of 27 % of their disposable income on housing. ↘ CHART 92 While the rent burden for households in the first quartile of the income distribution is 36 %, it is only 16 % in the fourth quartile. Overall, the rent burden for 16 % of all renter households was above the 40 % threshold at which, according to the EU definition, a household is financially overburdened (Federal Statistical Office, 2023; Eurostat, 2024b).

367. **On average, the rent-burden ratio** in Germany – i.e. gross rent as a percentage of disposable income – has remained **largely constant since the 2000s** (Sagner et al., 2020) and has even fallen slightly since 2015 (Kholodilin and Baake, 2024). However, price trends vary greatly from region to region. ↘ ITEM 324 In addition, existing and new rents have not risen to the same extent due to rent regulation. ↘ ITEM 325 In recent years, nominal income growth (in the denominator of the ratio) has had a favourable effect, although incomes have not developed equally for all household types (GCEE Annual Report 2023 items 290 ff.). As a result, the rent burden varies between individual household types, tenant types and regions. However, there has been no significant increase in the rent burden within these groups since 2010. ↘ CHART 92

368. In tight housing markets, tenants can be discriminated against on the basis of certain characteristics when accessing housing, regardless of their income situation. The General Equal Treatment Act (AGG) prohibits discrimination in access to housing. However, various field experiments show that **discrimination on the basis of various characteristics** nevertheless takes place on housing markets in Canada, the United States, Germany and other OECD countries. This particularly affects immigrants (Flage, 2018; Auspurg et al., 2019; Sawert, 2020), but also single parents (Lauster and Easterbrook, 2011).

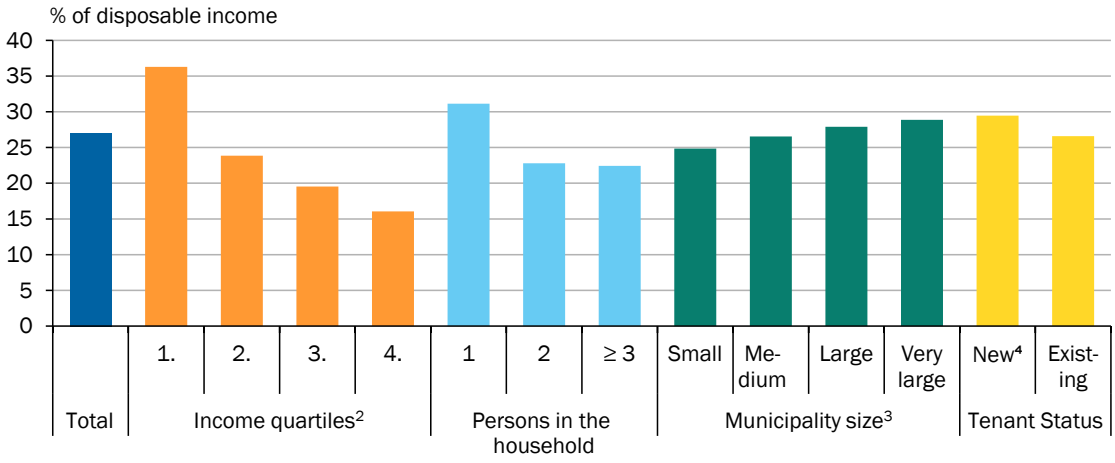
Consequences of payment and access difficulties

369. It cannot be concluded from the observation of a largely constant rent burden over time that the sharp rise in residential property prices since 2010 ↘ ITEM 323 has not resulted in any social burdens. Rather, the **rent burden** is being **kept low by** more evasive reactions, especially by the **overcrowding** ↘ GLOSSARY **of apartments**. It can be observed that more and more low-income households are living in overcrowded apartments. In 2023, just under 9 % of households not at risk of poverty lived in overcrowded housing, while the figure was just under 27 % among people at risk of poverty ↘ GLOSSARY. This has an impact on social inequality, including opportunities for social advancement. For example, Solari and Mare (2012) show for the United States that cramped living conditions have a negative impact on a number of indicators of children's well-being and lead to the intergenerational persistence of social inequality.

370. Households in large cities, **single parents** and **large families are particularly affected by cramped living conditions**. ↘ CHART 93 In 2023, more than a quarter of single parents in Germany lived with their children in overcrowded

↘ CHART 92

Rent burden rate[1] by income, household characteristics and region



1 – The rent burden rate is the share of net cold rent plus cold ancillary costs relative to the disposable income. Based on the supplementary housing survey of the 2018 microcensus. 2 – Disposable income: 1st quartile to under 1,850 euro; 2nd quartile 1,850 euros to under 2,750 euro; 3rd quartile 2,750 to under 3,800 euro; 4th quartile 3,800 euro and more. 3 – Size by population: small under 20,000 people; medium 20,000 to under 100,000 persons; large 100,000 to less than 500,000 persons; very large 500,000 and more persons. 4 – New tenants are tenants who moved into their current home less than two years ago.

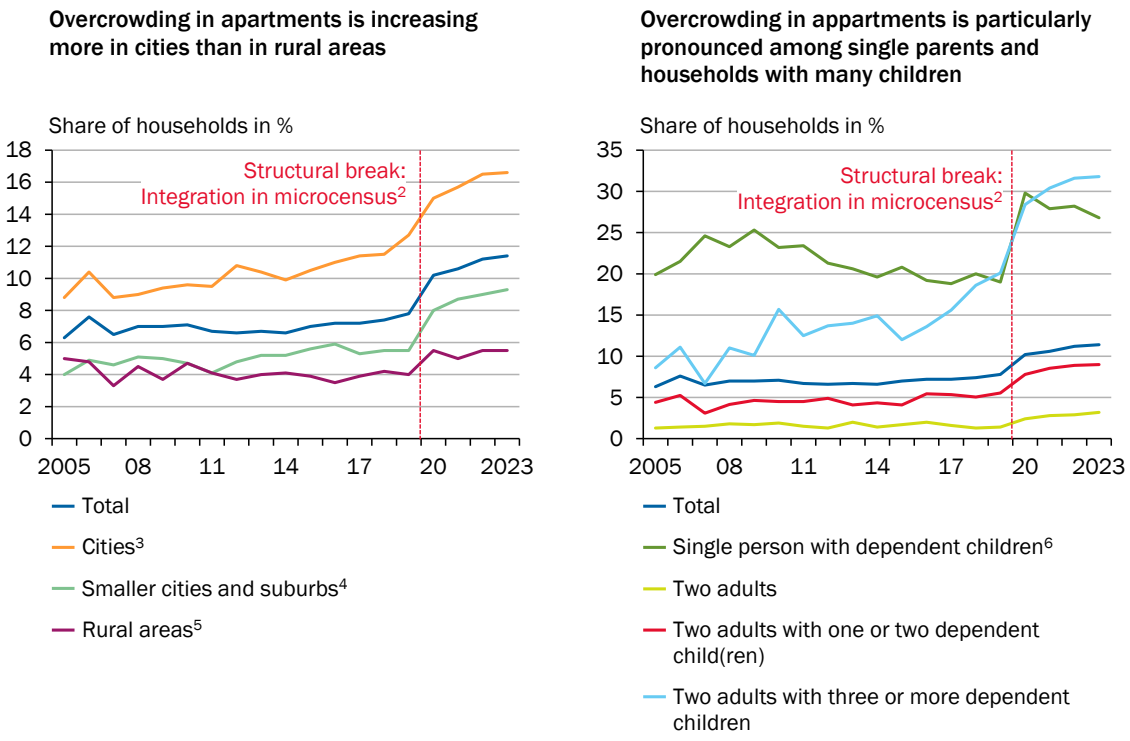
Sources: RDC of the Federal Statistical Office and Statistical Offices of the Länder, DOI: 10.21242/12211.2018.00.00.1.1.3, own calculations

housing. Around a third of large families with three or more children lived in cramped housing conditions in Germany in 2023. The housing situation of people with and without a **migration background** also differs significantly: on average, immigrants live in poorer residential areas, have less residential space and pay higher rents per square metre (Winke, 2016; Auspurg et al., 2017; Liebig et al., 2022; OECD, 2024b). This cannot be fully explained by structural differences (e.g. shorter duration of residence, urban context) and socio-economic status.

371. Discrimination and access difficulties can lead to gentrification, i.e. the **displacement of lower-income households by wealthier households** from inner-city neighbourhoods. Such displacement can lead to **different population groups living** separately from each other **in different neighbourhoods** (segregation). Up to now there have been few empirical studies in Germany that

↘ CHART 93

Overcrowding[1] of flats over time



1 – A flat is considered overcrowded if at least one of the following rooms is not available: One shared room, one room per couple living in the household, one room per additional person aged 18 and over, one room for two children under 12, one room for two children of the same sex aged between 12 and 17, one one room per child aged between 12 and 17 if they are of different sexes. 2 – In 2020, the random-based sample of the EU-SILC survey was more than doubled and an obligation to provide information was introduced. In addition other survey forms of questioning are used in addition to the paper questionnaire and the processing procedures have changed. Due to these methodological improvements, the results from 2020 are only comparable with previous years to a limited extent. 3 – Cities: At least 50 % of the population lives in adjacent areas (size one square kilometer) with a density of at least 1,500 persons per square kilometer and a population of at least 50,000 persons. 4 – Smaller cities and suburbs: Adjacent areas (size one square kilometer) with a population density of at least 300 persons per square kilometer and a population of at least 5,000 persons. 5 – Rural areas: More than 50 % of the population lives in areas outside urban areas. 6 – Dependent children include all persons under the age of 18, as well as persons aged 18 to 24 who live with at least one parent and are economically inactive.

Sources: EU-SILC, own calculations

attempt to systematically measure **gentrification and segregation** and analyse their effects. Döring and Ulbricht (2018) show clear gentrification effects for Berlin, both in the city centre and in more distant districts. Schulz (2017) also analyses gentrification in Berlin and comes to the conclusion that the proportion of annual internal migration attributable solely to property appreciation and corresponding increases in asking rents is 4.1 % across the city. In individual neighbourhoods, however, this proportion is much higher, at up to 14 %. The figures determined in this study are comparable with the estimates of economic displacement rates by Newman and Wyly (2006) for New York City in the 1990s. International studies have also identified gentrification in London (Atkinson, 2000, 2004), Amsterdam (Boterman and van Gent, 2014) and several US cities (Smith et al., 2020). **Segregation favours societal division** and is associated with external costs. Helbig and Jähnen (2018) show that, as in the United States, social segregation in cities affects families with children more than the population as a whole. For the United States, Kulkarni and Malmendier (2022) show that higher segregation correlates with lower social mobility for children from low-income households.

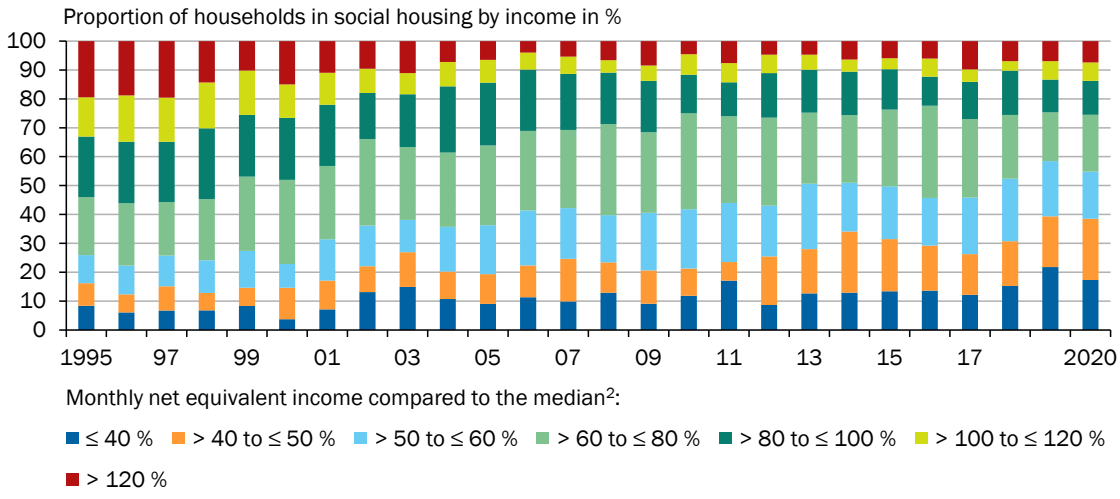
Social housing policy to combat payment and access difficulties

372. **Social housing policy** in Germany aims to reduce the housing cost burden for disadvantaged population groups **by means of object- and subject-oriented support**, i.e. social housing and housing benefits, ↘ ITEM 367 and to enable or facilitate their access to the housing market. ↘ ITEM 368

373. The eligibility of a household to move into an apartment subsidised by the social housing scheme is usually only checked once on moving in. An important criterion

↘ CHART 94

Income of households in social housing[1]



1 – Only flats with occupancy commitment. Proportion of tenant households in subsidised housing by income based on the median of the equivalised monthly disposable income of all households in the respective federal state. 2 – Interpretation aid: Proportion of households in subsidised housing whose monthly net equivalent income is, for example, less than 40 % of the median in the federal state in which they live.

Sources: SOEP v38, own calculations

here is the household income. If it increases over time, the household does not lose its right of residence because of Germany's general protection against unwarranted eviction. Analyses from previous years indicate a **high level of misoccupancy** and **low social target accuracy in social housing** (Schier and Voigtländer, 2016; Board of Academic Advisors to the BMWi, 2018; Sagner et al., 2020). However, the authors do not measure misoccupancy based on the income limits of social housing, but based on the poverty threshold. Misoccupancy of social housing is difficult to determine in Germany because the income thresholds for housing entitlement certificates vary greatly and can differ significantly from one federal state to another and according to the number of people and the subsidy channel. ↘ TABLE 17 APPENDIX However, in 2020 around 26 % of social housing tenants earned more than 80 % of the median income in their respective state, which roughly corresponds to the income threshold for entitlement to housing benefit. About 14 % reached more than 100 % of their state's median income. ↘ CHART 94 Individual states estimate that between 10 % and 30 % of subsidized apartments are occupied by non-entitled tenants (HMWEVW, 2021; Menzl and Ebbers, 2023). Over time, however, the social target accuracy of social housing, measured by the proportion of households in social housing with a net equivalent income of less than 60 % of the median, has increased significantly. ↘ CHART 94

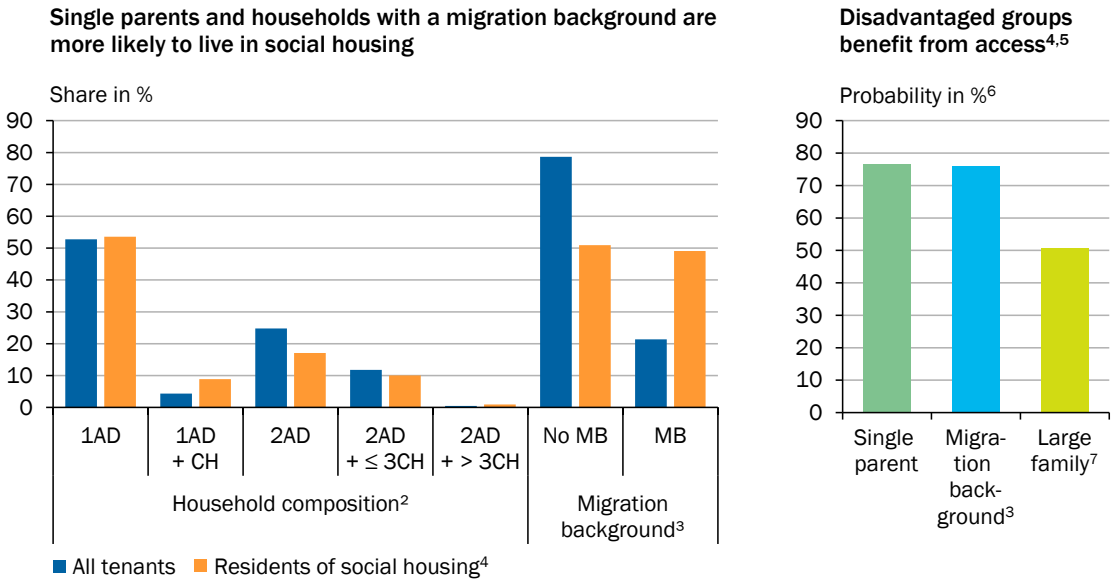
374. Social housing fulfils an **important supply function for households whose access to the regular housing market is difficult**. ↘ ITEM 368 For example, single parents, large families and immigrants are particularly likely to benefit from access to social housing. ↘ CHART 95 RIGHT These groups of people often do not have access to rental housing that is appropriate in terms of size, quality and rent and are therefore affected by overcrowding particularly often. ↘ ITEMS 369 F. The funding conditions for social housing, ↘ BACKGROUND INFO 11 which, among other things, contain specifications on apartment size per resident, ensure that apartment overcrowding is avoided, which is otherwise a typical evasive reaction to payment and access difficulties. ↘ ITEM 369

375. In 2024, the Federal Government decided to reintroduce non-profit housing, which had been abolished in 1990 (BMWSB, 2024c). As from 1 January 2025, **non-profit housing companies** will receive **tax exemptions for non-profit housing** (Neue Wohngemeinnützigkeit NWG) if they provide permanently subsidised housing. This instrument thus differs from social housing, which is only available for a limited period of time because the social commitment is only temporary. ↘ BACKGROUND INFO 11 The aim is to create a new market segment with permanently affordable housing as a second pillar alongside social housing. Although non-profit housing companies as defined by this policy instrument can be either private or public, the aim is to strengthen in particular municipal, cooperative and other non-profit housing companies and to ensure the long-term provision of social (i.e. affordable) housing. According to the Federal Ministry of Housing, Urban Development and Building (BMWSB), around 100 entities – e.g. non-profit foundations, associations or socially oriented companies – and around 105,000 tenants could initially benefit from the scheme (BMWSB, 2024d).

376. In the post-war period, the majority of social housing was built by non-profit housing companies, mostly with direct subsidies and always with tax exemptions

↘ CHART 95

Access to social housing[1]



1 – The proportions shown are average values for the years 2016 to 2020. The migration background category is analysed at individual level, while the household composition is analysed at household level. 2 – 1AD-Household with one adult, 2AD-Household with two adults, CH-Child(ren) under 18. 3 – MB-Migration background. Only households with information on migration background. Migration background in first or second generation. 4 – Only flats with occupancy commitment. 5 – The results shown here are based on a logistic regression, controlling for equivalence-weighted income and other household characteristics. The coefficients for single parents and migration background are significant at the 1 % level, the coefficient for large families at the 5 % level. 6 – Probability of living in social housing based on odds ratios. Odds ratios allow a statement to be made about the extent to which the presence or absence of a characteristic is related to the presence or absence of another characteristic and how strong this relationship is. They result as $e^{\text{Regression coefficient}}$ from the logit regression carried out here. Odds > 1 indicate that it is more likely that the event will occur than that it will not. For the migration background factor, for example, an odds ratio of 1.76 means that the probability of living in social housing is 76 % higher for a person with a migration background than for a person without a migration background.
7 – Large family: More than three children.

Sources: SOEP v38, own calculations
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for the companies. As a result, **non-profit housing companies played a major role on the housing markets** until the end of non-profit housing in **1990**. In large cities, they provided up to a third of the housing supply (Kuhnert and Leps, 2017). Comparable instruments exist in other member states of the European Union. Austria, in particular, has many years of experience with interlinking housing subsidies and non-profit housing. ↘ BACKGROUND INFO 13

↘ BACKGROUND INFO 13

Focus: Public housing construction in Vienna

In Vienna, 60 % of the population live in subsidised housing or municipal apartments with capped rents (Ludwig, 2017). Municipal housing refers to apartments built by the City of Vienna itself. In addition, there is social housing in Vienna which is operated by non-profit housing associations and subsidised by the city. **As a rule, subsidised housing** remains socially tied in the long term under the Non-Profit Housing Act. This law grants non-profit building associations a tax advantage and special access to housing subsidies if they create long-term social housing. Vienna's housing policy aims to continuously increase the proportion of

public and non-profit housing. Around 600 million euros a year are channelled into housing construction subsidies for this purpose. About 7,000 new subsidised housing units are built in Vienna every year (Ludwig, 2017). In Austria, subsidised state housing accounts for approximately 26 % of all rental apartments – the majority in Vienna (Punz, 2019). In Germany, social housing accounts for less than 5 % of the total stock of rental housing. **Opening up municipal housing** not only to low-income households but also **to broad sections of the population** is a declared political objective in Vienna; it aims to ensure affordable housing for all and a social mix of tenants (empirica, 2020). Accordingly, the **income limits for state-subsidised housing** in Vienna are **very high** compared to those for German social housing and extend into the upper middle class. The development of income is no longer reviewed after a household moves into a municipal apartment and, under certain conditions, the residents can even pass the apartment on to close relatives if they move out or die. This has sometimes been the subject of controversial debate in Vienna in the past (Ludwig, 2017).

377. The federal states have exclusive legislative and enforcement powers in the field of social housing. ↘ ITEM 342 The Federal Government can only support the states by granting financial assistance. With the introduction of NWG, the Federal Government is expanding its **scope** and can use NWG to contribute to the creation of housing with a permanent social commitment and thus permanently subsidised rents.

The income limits of NWG are derived from the standard rates of social assistance. Companies that let rental apartments to people whose income is no more than five or (in the case of single people and single parents) six times the social assistance rate according to the German Social Security Code (SGB) XII should be able to make use of the regulation. This means that a single person would be able to earn a maximum monthly income of €3,378 gross in order to qualify for subsidised housing. For a family with two adults and two children aged six and 15, the limit is €9,365 gross per month. The income limits are thus significantly higher than those envisaged in the original draft bill (Bundesregierung, 2018) and than the income limits for housing entitlement certificates. ↘ TABLE 17 They are set in such a way that around 60 % of households in Germany could benefit from the new housing benefit scheme (BMWSB, 2024c). As in the case of the social housing subsidy, compliance with the income limit is only checked at the beginning of the tenancy (BMWSB, 2024d), so that rising tenant incomes are not detrimental to non-profit status; the **accuracy of the subsidy is** therefore **not guaranteed**.

378. Since the 1990s, the intention has been to cushion the decline in the stock of social housing in Germany by strengthening subject-oriented support (Sinn, 1995). ↘ CHART 82 However, **housing benefit** ↘ BACKGROUND INFO 14 has never been able to fully play its intended role due to its insufficient adjustment to rent and income trends. As a result, many households lost their eligibility every year because they exceeded the nominal income limit but in fact received hardly any income growth in real terms (Deutscher Bundestag, 2021a). **The housing benefit** has only been regularly **dynamised** since the beginning of 2022. The major **advantage** of the instrument compared to social housing in its current form is its **social accuracy**. Housing benefit must be reapplied for every year. This means that increases in

income are automatically reflected in the housing benefit entitlement and the transfer can be precisely targeted to the household's current needs (Board of Academic Advisors to the BMWi, 2018).

↘ BACKGROUND INFO 14

Background: Housing benefit

Housing benefit is an **income-related transfer to households** that have a low income that is above the basic income support threshold but who are unable to fully cover their housing costs themselves. Housing benefit can be claimed up to an income limit that varies depending on the number of household members. Around 1.2 million households in Germany, i.e. about 2.8 % of households with a registered main residence, received housing benefit in 2023 (Federal Statistical Office, 2024b). The **number of households receiving housing benefit** thus **increased by 80 % compared to the previous year**. The average monthly housing benefit entitlement was €297 per eligible household. The federal and state governments spent a total of €4.3 billion on housing benefit in 2023, about twice as much as in the previous year. The reason for these developments is the **'Wohngeld plus' ('housing benefit plus')** reform, which was introduced at the beginning of 2023 and aims to significantly increase both the use of housing benefit and average benefits (Bundesregierung, 2023). In future, housing benefit will be adjusted every two years in line with rent and income trends (**housing benefit dynamisation**).

379. International empirical evidence suggests that rent subsidies can lead to an increase in rents paid due to the recipients' increased ability to pay in the event of an inelastic housing supply (Susin, 2002; Gibbons and Manning, 2006; Sayag and Zussman, 2020). For Germany, **however**, a review conducted in 2015 confirms that **housing benefit is well targeted and efficient in terms of** its **social policy objectives**. According to the study, housing benefit effectively reduces regional differences in the housing cost burden without leading to an increase in rents (BBSR, 2015a). However, this could also be related to rent regulation in Germany. There are no other empirical studies on the relationship between housing benefit and rent levels in Germany.

380. There is **tension between** the **high social accuracy of** housing benefit and **incentives for gainful employment**. Particularly at the interface between the citizen's allowance (Bürgergeld) and housing benefit, there are jumps in the marginal burden. As a result, the marginal burden on additional earned income is very high. In addition, high transfer deduction rates reduce the incentives to expand gainful employment (Advisory Board to the Federal Ministry of Finance, 2023; GCEE Annual Report 2023 items 309 ff.). Also, unlike social housing, housing benefit is **not always suitable for providing access to the housing market for hardship cases** among low-income households when the housing supply is rationed, as it does not restrict discrimination based on tenants' personal characteristics. Furthermore, housing benefit **does not prevent overcrowding** in tight housing markets. ↘ ITEM 369

IV. OPTIONS FOR ACTION

381. Various options for action are suitable for addressing the macroeconomic and social challenges on the housing market. The availability of housing in urban areas could be increased by **boosting** the **construction of new housing, improving land availability** ↘ ITEMS 384 FF. and **reducing building costs**. ↘ ITEMS 386 FF. Building land potential in neighbouring regions and housing potential in structurally weak regions could also be used by improving (transport) connections ↘ ITEMS 391 FF. At the same time, **existing housing** could be used more efficiently. By removing barriers to relocation, changes of residence could be facilitated in both the rental and purchase markets and, above all, become more cost-effective. ↘ ITEMS 395 FF. **Subject- and object-oriented support can meaningfully complement each other** in social housing policy. The **target accuracy** of social housingand the NWG **should be increased**. ↘ ITEMS 408 FF.

1. Boost new residential construction

Unlock space potential

382. A key obstacle to residential construction in urban centres is **the lack of building plots**. ↘ ITEMS 345 F. Although the statutory priority of internal over greenfield development (Section 1 (5) of the BauGB) is welcome in terms of land consumption, internal development will probably only be able to meet the demand for land for a few years given the current building density. ↘ ITEM 346 **Denser development**, i.e. an increase in residential space relative to the plot area, can be achieved by various measures. In **existing buildings**, densification can be achieved by **adding storeys and roof extensions**. ↘ ITEM 388 In addition, gaps between buildings could be closed and brownfield sites used. ↘ ITEM 346 In **new builds**, local authorities could **allow additional storeys** where possible. However, these measures should also take into account the quality of living, the use of the surrounding infrastructure, the impact on the urban climate and soil sealing.

383. For regions with a high demand for housing, where denser development is difficult to achieve or will not be sufficient in the foreseeable future, greater use could be made of **greenfield development outside of the inner cities**. To this end, local authorities could activate long-term building land potential to a greater extent than hitherto by **quickly drawing up development plans** for these areas and thus turning them into building land. The preparation of these development plans often takes several years. In Berlin, for example, the preparation of plans that were finalised in 2023 took an average of around nine years (bulwiengesa, 2024). The acceleration of these procedures as envisaged by the BMWSB – aiming to shorten the completion period after the end of the participation procedures to twelve months – could help shorten these procedures and accelerate the creation of building land (BMWSB, 2024e). An **obligation to build on newly created building land** within a certain period of time could be provided for: if construction does not begin within the corresponding period, municipalities could be

granted a right of first refusal. Local authorities could also make greater use of their right of first refusal for interim purchases when land ready for construction or brownfield sites is sold in tight housing markets. Conditions similar to those for new building land should then also apply to resale.

384. **Incentives to build more densely on land could be increased by orienting property tax more closely towards the value of the land rather than on the value of the building**. In the land-value model introduced in Baden-Württemberg, property tax is calculated independently of the building development on principle. Compared to the models of the other federal states, it is thus most strongly orientated towards the land value. ↘ BOX 25 In addition, the tax payment is 30 % lower for residential buildings. In the case of the area, residential-location and area-factor model, the incentives for denser development could also be strengthened compared to the current structure by increasing the equivalence or area figure for properties. It should be noted in this context that the property tax can also be used to pursue other objectives in addition to the goal of denser development. For example, covering local infrastructure costs or the comprehensive taxation of real-estate assets may represent further objectives that could justify a stronger focus on building value. When aligning the property tax, a balance must therefore inevitably be struck between these objectives, as the different valuation models fulfil these objectives to varying degrees (Fuest et al., 2018; Büttner and Zimmermann, 2020).

↘ BOX 25

Background: Property tax reform in Germany

In a judgement adopted in 2018, Germany's **Federal Constitutional Court** declared the former **property tax valuation of land based on** the **standard values** in 1964 (West Germany) and 1935 (East Germany) to be **unconstitutional** (BVerfG, 2018). The legislature was requested to revise the valuation rules by the end of 2019. The federal and state governments have since agreed on a federal model, but also approved an opening clause that allows the federal **states** to **develop their own models**.

Some states have adopted the federal model in full or with minor deviations. ↘ TABLE 16 The model provides for residential properties to be valued using the capitalised earnings value method. The net income of a developed property is determined from the residential space and rent level minus the operating costs, whereby there are special features for buildings with very large plots of land. Five states have made use of the opening clause (BMF, 2021). ↘ TABLE 16

In Baden-Württemberg, a land-value model is used in which only the area of a plot of land is taxed without taking into account the area of the buildings on it. However, the location of the property is included in the valuation. As building on land with residential buildings does not increase the tax burden, this tends to encourage denser development and, in the case of residential use, even reduces the tax burden via the planned valuation discount. A similar effect could be achieved by property tax C on undeveloped, ready-to-build plots if designed accordingly. ↘ ITEM 385

In Bavaria, an area model is used in which the building area is taken into account in addition to the land area. However, the location of the property is not assessed. Hesse and Lower Saxony use area factor-models in which the location of the property is taken into account with a supplementary factor in addition to the plot area and residential space. Hamburg also includes the residential location in the valuation of properties. There, the valuation is based on the plot area,

living area and usable area; the areas are multiplied by an equivalence number depending on the residential location.

↘ TABLE 16

Overview of property tax models in Germany

	Surface model	Modified land value model	Residential model	Area factor model	Federal model
Federal state	Bavaria	Baden-Württemberg	Hamburg	Hesse, Lower Saxony	Other federal states[1]
Plot area	✓	✓	✓	✓	✓
Building area[2]	✓		✓	✓	✓
Standard land value		✓		✓	✓
Average standard land value[3]				✓	
Value-independent equivalence/ area number[4]	✓		✓	✓	
Property tax rate	✓[5]	✓[5]	✓[6]	✓	

1 – Berlin, Brandenburg, Bremen, Mecklenburg-Western Pomerania, North Rhine-Westphalia, Rhineland-Palatinate, Saarland, Saxony, Saxony-Anhalt, Schleswig-Holstein, Thuringia. 2 – The area factor model is based on the living space and not the building area for residential use. 3 – The average standard land value in the municipality is used in the area factor model to calculate a factor (standard land value/average standard land value in the municipality). This leads to a muted translation of rising standard land values of certain properties to the property tax. 4 – In the area model, the residential location model and the area factor model, a different amount is used for the equivalence/area figure for land (0.04 euro/square metre) and buildings (0.50 euro/square metre). 5 – In the area model and the modified land value model, the property tax rate is reduced by 30 % for residential use, which favours residential use for tax purposes. 6 – In the residential location model, the property tax base is used to include the quality of the residential location in the calculation in addition to a general reduction of 30 % for residential areas. For residential areas, the measurement figure is 70 % for good locations, 45 % for normal locations and 20 % for listed and socially subsidised buildings.

Sources: Federal and state legislation, own presentation

385. Under the 2019 property tax reform, **municipalities will be able to levy property tax C from 2025**. ↘BACKGROUND INFO 15 This allows municipalities to **levy a higher rate for undeveloped plots that are ready for building in** the relevant **parts of the municipality** if there are urban development reasons, such as an increased need for housing. This also includes land with buildings that cannot be put to permanent use (Section 246 (2) of the Valuation Act). The tax makes the mere holding of these plots more expensive and thus increases the incentives to build on them. The introduction of a comparable tax in Finland in 2001 increased residential construction activity by 8.7 % in the municipalities concerned (Lyytikäinen, 2009). If property tax C is introduced by municipalities, it should be taken into account that the development of land can take some time, for example due to long approval procedures, capacity bottlenecks in the building industry or financing obstacles (Simons et al., 2023; GCEE Annual Report 2018 item 727). This could be achieved by a transitional period after the introduction of the tax or after designation as building land, or by staggering the timing of the assessment rate following designation as building land. The introduction of property tax C in Hamburg from 2025, for example, includes a transitional period of three years.

↘ BACKGROUND INFO 15

Background: Property tax C in the years 1961/1962

Property tax C, also known as building-land tax, was levied as early as 1961 and 1962. It enabled **local authorities** to set four-times-**higher tax rates** for undeveloped plots that are ready for building; the rates could rise to six times higher over time. Furthermore, local authorities were able to **determine** a **higher assessment rate** for these plots; it was set at 1,000 % in cities such as Frankfurt am Main or Regensburg (Schupp, 1964). The tax paid could be refunded if development took place within two years. **Just two years after** its **introduction**, property tax C was abolished **again due to the overheated building sector at** the time. The distribution effects and construction incentives of this measure were not empirically analysed.

Reduce construction costs

386. **Building to the highest standards increases the cost** of new buildings and makes it more difficult to create affordable housing. ↘ ITEM 353 The efforts of the Federal Ministry of Justice (BMJ) to adapt construction contract law and to define the generally accepted engineering standards more clearly may reduce legal uncertainty (BMJ, 2024a). However, it remains to be seen whether it will be possible to clearly separate standards of comfort from safety standards (BMJ, 2024b). According to calculations by the Institute for Sustainable Construction (Walberg et al., 2024), the planned **introduction of building type E**, which offers builders and construction companies a legally secure option to deviate from the generally accepted engineering standards, could reduce construction costs by up to 25 % (BMWSB, 2024b)

387. **Serialised and modular housing construction** can also help to cut construction costs and increase efficiency. Large building and room elements are industrially prefabricated and assembled on the construction site. Despite the standardisation of components, modularisation enables the construction of visually individual buildings (Nagel, 2024). Due to lower labour requirements and lower planning costs, this approach offers potential savings of around 20 % compared to conventional residential construction (Walberg et al., 2024). Industrial prefabrication is particularly suitable for public housing construction and other standardisable projects by large property developers. However, the different state building regulations hinder the realisation of significant economies of scale, which is why these should be further harmonised.

388. The **conversion of attics and the addition of extra storeys to residential buildings** can help to increase the supply of housing. It is estimated that around 1.1 to 1.5 million residential units could be created in existing residential buildings (Tichelmann et al., 2019). The economic viability of such projects can be limited due to the loss of the protection of existing buildings and the associated strict requirements that apply to the entire building, such as fire safety or distance requirements. The **amendment of the Model Building Regulations** addressed key obstacles, ↘ BOX 21 but only four federal states have comprehensively adopted them into state law up to now.

Lower Saxony has gone beyond the Model Building Regulations when it comes to protecting existing buildings. In its amendment to the building regulations passed in July 2024, the state introduced an **orientation towards the building standard of the respective year of building in the case of additions, conversions, extensions and changes of use** for walls, struts, ceilings, floors, roofs and stairs (Section 85a of the NBauO). Requirements for stability and energy efficiency remain unaffected by this. Other states could follow suit and thus further harmonise their building regulations.

389. Residential construction activity could also be promoted by **accelerated rules on depreciation**. This reduces the tax burden on letting in the short term, but increases it in the longer term. The resulting positive liquidity effect increases investment incentives. Empirical evidence shows that special depreciation programmes can favour investment decisions and volumes and are used most frequently for investments in assets with long useful lives (House and Shapiro, 2008; Zwick and Mahon, 2017; Eichfelder et al., 2023). While accelerated depreciation in times of high capacity utilisation is likely to lead primarily to higher prices, it increases real investment activity when capacity utilisation is low. As the building industry is currently experiencing a high level of underutilisation, ↘ ITEMS 343 AND 138, temporarily accelerated depreciation rules are likely to have a particularly strong effect in stimulating residential construction activity. The higher straight-line depreciation introduced in 2023 and the temporary introduction of special depreciation for particularly climate-friendly new builds therefore made sense. Against this backdrop, it is also positive that declining-balance depreciation (depreciation for wear and tear) was reintroduced for six years for new residential buildings constructed from 1 October 2023 as part of the Growth Opportunities Act.

390. A **reduction in property acquisition tax on new builds** could also have a positive impact on residential construction. ↘ ITEM 403 According to a recent estimate, a 50 % reduction in real estate transfer tax on all transactions could increase the number of building permits by 9 %. Due to the high correlation between building permits and building completions, a similar effect on completions can therefore be assumed, albeit with a certain time lag (Sagner and Voigtländer, 2024).

Open up housing potential in other regions

391. **Improved transport connections to neighbouring regions** could **enlarge the commuting area of housing markets in urban areas** and thus create more potential for housing. ↘ ITEM 355 To this end, public transport could be expanded in counties near major cities that have been poorly connected up to now. Shortening the journey time to the major cities, e.g. by direct or fast connections, could also encourage more people to move to neighbouring regions and thus help alleviate the housing shortage in the major cities.

392. While the previously discussed options for action are mostly focused on urban areas, **increasing the attractiveness of structurally weak regions** could provide additional relief for tight housing markets. Many of the regions currently receiving support from the joint Federal Government/Länder programme to

improve regional economic structures (GRW) are characterised by high vacancy rates in existing housing and low housing costs (Ammann et al., 2021). In the context of targeted economic policy support for these regions, the high **availability of housing** could be used as a locational advantage that prevents labour migration and attracts new workers.

393. Targeted promotion of central locations in structurally weak regions is especially promising. The establishment of business clusters could create positive agglomeration effects. The fundamental prerequisite for this is **ensuring good location conditions** for companies. In addition, jobs could be created by locating certain areas of public administration in these regions. The increased popularity of working from home ↘ ITEM 330 increases the **attractiveness** of these regions **as a place to live**. However, as many activities still require a regular presence on site, an acceptable **transport connection between central locations and supra-regional conurbations** would have to be ensured.

Further measures to increase the supply of housing

394. There is also a small amount of **residential potential** in **unused commercial properties**. ↘ BOX 22 However, high conversion costs considerably restrict the conversion of these spaces. Targeted funding programmes could provide incentives for converting these properties, but could also lead to deadweight effects. The BMWSB has launched a funding programme for the conversion of vacant commercial properties into (climate-friendly) housing units (BMWSB, 2024f). Furthermore, the KfW and BAFA (Federal Office for Economic Affairs and Export Control) also provide funding for the energy-efficient refurbishment of non-residential buildings, the conversion of which is intended to contribute to the creation of additional housing (BAFA, 2024; KfW, 2024). In addition, local authorities could grant exemptions for conversion projects that, in principle, are suitable for conversion but where this is not possible under existing building regulations.

2. Increase incentives for the efficient use of housing

Reduce barriers to relocation

395. To ensure an efficient use of housing in a way that is geared towards individual needs, it is important that people can easily adapt their use of housing to changing life situations in the course of their lives. However, this often does not happen, especially in old age. ↘ ITEM 335 One of the obstacles here is the loss of familiar surroundings as the result of a move. ↘ ITEM 356 In order to increase the willingness of older people in particular to move, it is therefore helpful if there is a **sufficient mix of different apartment sizes** within a neighbourhood. This makes it easier for people who are willing to move to find a suitable apartment in the same neighbourhood. To achieve this, building concepts could be promoted which specifically **create housing that** allows **subsequent changes to be made to the size or use of the apartment**. One example of this is so-called **Vario**

apartments ↘ GLOSSARY, which are subsidised by the BMWSB in cooperation with the BBSR (Federal Institute for Research on Building, Urban Affairs and Spatial Development) (Dorn-Pfahler et al., 2021).

396. Barriers to relocation could also be reduced by making greater use of **home swapping**. This involves tenants who want to downsize swapping their apartment with tenants who want to move into a larger apartment (Landeshauptstadt Düsseldorf, 2024). In practice, however, **home swaps are not very common because many hurdles are involved** (empirica, 2022). Landlords have little financial incentive to agree to an exchange of tenancy agreements while retaining the existing rental conditions, as they can often demand significantly higher rents for new tenancies. If the rent is increased as part of an exchange, the financial incentives for tenants to downsize are reduced. Furthermore, the cost of moving tends to be higher in the case of an apartment swap, as both parties have to move in and out at the same time, so that a high level of coordination is needed (Melcher, 2023). It has also been shown that the demand for larger apartments for exchange often exceeds the supply (empirica, 2022). For these reasons, some cities have introduced programmes that provide financial support for downsizing by paying a lump sum even without a direct exchange partner (Stadt Marbach, 2019; Stadt Mannheim, 2024; Wohnbau Lörrach, 2024).

In order to increase the use of home-exchange concepts, **public counselling services** could be **expanded**. However, directly approaching potential exchange partners in under-occupied apartments has not proved useful in practice, as it has often led to uncertainty and fear of losing one's own apartment (empirica, 2022). The financial hurdles of exchanging apartments could be reduced for **landlords** by offering a **bonus for successful exchanges**. For **tenants**, a **subsidy to cover the increased relocation costs** could increase their willingness to exchange homes. However, the effectiveness of such a subsidy depends crucially on the difference between the new rent and the existing rent.

397. Apart from moving into a smaller apartment, **shared housing projects for older people** could enable more efficient use of residential space. One example of this is the 'Home for Help' housing project, which provides unused residential space in the apartments of (mainly) senior citizens to students in 30 cities in Germany, (University of Cologne, 2024). Instead of paying rent, the students help in the household or garden, but do not provide any care or medical services. There is also the concept of seniors sharing accommodation, in which senior citizens live together in one apartment. Many of these projects also use the help of a mobile care service when required and can therefore make it unnecessary to a move to a care home in the longer term (BMG, 2024). **Raising the profile of** such shared housing projects **could** increase the **participation of older people**, but it seems **questionable whether** these projects can be **more than a niche solution**. Many older people do not want to live with a stranger in their household (Galler, 2021).

Improve rent regulation

398. The **regulation of rents by the rent brake and rent caps does not solve the causes of the housing shortage** in tight housing markets. It can be used to temporarily protect tenants from excessive price increases on the housing market. In addition, a certain regulation of existing rents can be meaningful in order to strengthen the negotiating position of tenants in existing tenancies, as the high cost of moving creates a lock-in situation. ↘ ITEM 360.

However, **regulation that is too restrictive** is likely to **reduce private incentives to invest in housing**. It also **prevents the efficient use** of housing. Both effects are all the stronger, the further the regulated existing and new rents are below the unregulated market price. **Furthermore**, rent regulation **is not very socially accurate** and is therefore less suitable as a distribution policy instrument than social housing policy. The regulatory slowdown in in the increase of existing rents provides relief in particular for those tenants who have lived in their home for a long time and are therefore paying a rent that is well below the market price. This means that immobile and older people in particular benefit, while young people and people who move frequently, e.g. for professional reasons, are burdened by higher new rents.

399. **Restrictive regulation** in the form of lowered rent caps and the rent brake is therefore only **justifiable temporarily** and as a rule **only if sufficient measures are taken at the same time** to **expand the supply of housing**. For this reason, these regulations should only apply temporarily, as already provided for by law today, and should be linked to the mobilisation of previously unused local housing potential.

400. Adjustments could be made to the existing regulations in order to increase incentives for investment and an efficient use of housing. The **gap between existing and new rents for comparable apartments** should not become too large to ensure the efficient use of housing. Regulated existing and new rents are linked to a certain extent to the market price of unregulated new rents via the local rent index. ↘ BACKGROUND INFO 12 In practice, however, the rent index deviates in some cases greatly from the market price of unregulated rents, with the result that the gap between regulated and unregulated rents has grown in recent years. ↘ ITEM 325 Against this background, the mandatory use of qualified rent indices could **raise the quality requirements for drawing up rent indices**. In order to better reflect current market developments, the extension (from four to six years) of the period for which the local reference rent is determined, which has been in force since 2020, could be reversed and **new rents could be weighted** more heavily.

401. In the regulation of new rents, the empirical evidence to date has **not shown any negative effect of the rent brake in its current form on new construction**. ↘ However, experience with the far more restrictive Berlin rent cap (Borck and Gohl, 2021; Dolls et al., 2021; Hahn et al., 2023; Sagner and Voigtländer, 2023) and from other European countries (Granath Hansson, 2017; Causa and Pichelmann, 2020; Kholodilin, 2024) suggests that more restrictive regulatory intervention in pricing could have a significant negative impact on the housing

market and housing construction. For this reason, at least the **cut-off date regulation for new builds** (first lettings after 1 October 2014) should remain unchanged and the **exemptions for modernisations should be retained** in their present form. The expectation must not be created that new buildings constructed after the cut-off date will also be subject to the rent brake in future. It is therefore to be welcomed that these regulations have been retained in the current draft bill to extend the rent brake until the end of 2028. A further extension of the rent brake beyond 2028 should be avoided. This is the only way to create a credible commitment that effective measures will be taken by then to expand the supply of housing.

The increasing proportion of furnished apartments on the rental market means that the rent brake could increasingly be circumvented, as it is difficult to recognise violations. ↘ ITEM 363 An **obligation to disclose the furnishing surcharge** in the tenancy agreement could **increase transparency** and **counteract any circumvention of the rent brake**.

402. The **gap between new and existing rents** in tight housing markets **is widened by lowering the cap** for increases in existing rents from 20 % to 15 %. This is exacerbated if the costs of a rent increase (possible legal dispute, personal relationship with the tenant) exceed the small rent increase when the rent increases and individual landlords therefore refrain from an increase. The lowering of the rent caps and a further reduction to 11 %, as envisaged in the coalition agreement, would further widen the gap between new and existing rents. The lowering of rent caps in tight housing markets should therefore be avoided.

Reduce ancillary purchase costs

403. In the purchase market for residential property, relocations are made more difficult by high transaction costs: the ancillary purchase costs. ↘ ITEM 364 A **reduction in** real estate transfer **tax** could be an effective means of **reducing** these transaction costs. The incentives for federal states to increase taxes, which result from the Financial Equalisation Scheme, ↘ BOX 24 should be reduced. While maintaining the states' revenue autonomy, this could be achieved by not including the income from real estate transfer tax in the Financial Equalisation or, alternatively, at least not including the transactions at the average tax rate of all federal states, as is currently the case, but only at a tax rate of 3.5 %, the current minimum of the federal states (GCEE Annual Report 2018 item 749).

404. Larger effects on relocation and construction could be achieved by **introducing an allowance** for real estate transfer tax. A general **reduction in tax rates** would also be conceivable, or only making the increase in value subject to taxation. To increase incentives for new construction, the real estate transfer tax for new buildings could be reduced. ↘ ITEM 390 The proposed reforms could compensate for possible declines in revenue for the federal states by **closing off opportunities for avoidance** ('share deals') and **abolishing the speculative period for real estate in income tax** (Fuest et al., 2021). Such an abolition would result in income tax being payable on the capital gains from the increase in value when a property is sold, even after a 10-year holding period.

405. As in the rental market, the **customer principle** should apply consistently to **estate agent fees**: i.e. the person who commissioned an estate agent pays the agent's commission. When the customer principle was introduced in the rental market, there were no signs of brokerage costs being passed on to the rent (Deutscher Bundestag, 2021b). However, in particularly tight housing markets, the greater negotiating power of sellers could lead to estate agent commissions being passed on to sales prices (DIW Econ, 2019). In the longer term, however, the customer principle increases the incentives to negotiate commissions (DIW Econ, 2019; Stoll, 2023) and can thus reduce estate agent fees through more competition between estate agents. **A reduction in notary fees** could be achieved **by lowering the fee rate** or by **introducing a flat rate**.

3. Combine subject- and object-oriented support in social housing policy

406. The **instruments of social housing policy can usefully complement** each other. Housing benefit is particularly effective when it comes to reducing the housing cost burden for low-income households. Social housing also especially benefits households for whom access to suitable housing in line with the size of their household is difficult, regardless of their income situation. ↘ ITEM 374

407. **Housing benefit** can better play its intended role as a social housing policy instrument for low-income households through regular dynamization. ↘ BACKGROUND INFO 14 Suitable reforms could also address the **interface problems between the housing benefit and basic income-support systems**, which have an unfavourable impact on work incentives. ↘ ITEM 380 This is most likely to be achieved if housing benefit and the inclusion of accommodation costs in basic income support are in future integrated into a uniform transfer payment with a low transfer deduction (GCEE Annual Report 2023 items 309 ff.).

408. **Strengthening social or quasi-social housing construction** ↘ BACKGROUND INFO 11 **in Germany could be** achieved by various means. On the one hand, the already planned increase and stabilisation of financial aid to the federal states for social housing support could contribute to this. ↘ ITEM 342 On the other hand, the introduction of the new non-profit housing (NWG), which supports the establishment of non-profit housing construction companies, for example in municipal hands, could also be helpful. In addition, the Institute for Federal Real Estate (BImA) could be enabled to take out loans in order to generate additional funds for its own investment and to continue to support municipal construction (SPD, Bündnis 90/Die Grünen and FDP, 2021).

409. A regulatory framework can reduce the misallocation of subsidies in social housing promotion. ↘ BACKGROUND INFO 11 To this end, a **misoccupancy levy** adapted to the respective market conditions could be introduced. This would increase the incentive to **release unoccupied apartments**, making them available again to eligible households. A misoccupancy levy is levied in Hesse (HMWEVW, 2024). There, tenants of social housing are liable to pay the levy if their income exceeds the income threshold for occupying the apartment by at least 20 %. The tenants

affected then pay a monthly compensation to the municipality based on the difference between the social rent currently paid and the local reference rent. A review of the income and the calculation of the misoccupancy levy is carried out every three years. The misoccupancy levy generates annual income of around €10 million, which is earmarked for the construction of new social housing (HMWEVW, 2021).

A different model is being pursued in Bavaria as part of the **income-orientated subsidy (EoF)** (StMB, 2024). Subsidised apartments are rented out at market prices to entitled households. However, the **beneficiary households receive** an **ongoing subsidy to reduce their housing costs** depending on their income. A new application must be submitted every two years, when the income is reviewed. If the income exceeds a certain limit, the subsidy is reduced or may be cancelled altogether.

410. NWG is unlikely to change conditions on the housing markets abruptly, especially as initially only a **small number of non-profit companies** are likely to benefit from it. ↘ ITEM 375 In the medium term, however, the favourable tax treatment could **strengthen** the **incentives for individual players** to create and **maintain quasi-social housing in the long term**. This could help counteract the accelerated expiry of social commitments since the 2000s. ↘ ITEM 341

However, the **high income limits** and the **lack of an income test** as part of NWG should be **criticised**. ↘ ITEM 377 In addition, NWG is not limited to tight housing markets, which could result in high deadweight effects. The attempt to create state-supported rental housing for broad sections of the population with NWG based on the Viennese model ↘ BACKGROUND INFO 13 is not very promising. In Germany's current situation, with a very small state role in housing construction, ↘ CHART 81 this would involve the use of considerable state funds and could only succeed in the very long term at best. It would make more sense to specifically target those households for whom accessing adequate housing is more difficult.

The target accuracy of NWG could be increased if the tenant had to make a **compensation payment if their income rises above the permissible income limits of NWG after the tenancy agreement has been concluded**. NWG differs from social housing promotion in that it does not address misoccupancy in the strict sense, as this is explicitly permitted by the legislator in the case of NWG (BMF, 2024). The draft bill originally submitted by the Bündnis 90/Die Grünen parliamentary group in 2020 provided for a compensation payment (Deutscher Bundestag, 2020), but this was no longer taken into account in the subsequent implementation.

411. The **disadvantage** of levying a **misoccupancy levy or an equalisation payment** would be that they could involve a relatively high level of **bureaucracy**. For this reason, most federal states have refrained from levying an misoccupancy levy. However, a disproportionately high administrative burden could be avoided if, for example, the misoccupancy levy or equalisation payment had to be automatically paid after three years unless the tenants prove that their income is still below the relevant limit. **Possible segregation tendencies** could be an argument against levying such payments. In the past, the abolition of misoccupancy

levies in some countries was justified as protection against negative effects on the social urban structure (Menzl and Ebbers, 2023). One of the reasons given for the generous income limits under NWG is to prevent the formation of neighbourhoods with one-sided occupancy structures (BMF, 2024). However, this argument has lost its significance, as a balanced social mix is ensured in current subsidised rental housing construction through minimum quotas for non-subsidised housing. ↘ BACKGROUND INFO 11 Inadequate misoccupancy levies or compensation payments also harbour the risk of weakening **incentives to work at the means-test threshold**. However, this does not represent a specific disadvantage of an misoccupancy levy compared to housing benefit, because such a conflict of objectives between a high level of social security and incentives to work also exists there. ↘ ITEM 380 In order to limit a negative effect on work incentives, it could make sense to introduce the misoccupancy levy or compensation payment for the respective household gradually.

A differing opinion

412. One member of the GCEE, Veronika Grimm, would like to emphasise **possible undesirable developments in the regulation of rents** more explicitly than the Council majority and present various further-reaching options as to how these undesirable developments could be remedied.

413. Regulation in the form of the **rent brake** and **rent caps** has the potential to **exacerbate shortages on the housing market**. Various academic studies have shown that regulation that is too tight is likely to reduce private incentives to invest in housing (Borck and Gohl, 2021; Dolls et al., 2021; Hahn et al., 2023; Sagner and Voigtländer, 2023; Kholodilin, 2024). However, in the view of the Council majority, this evidence only leads to the conclusion that "*restrictive regulation, in the form of lowered rent caps and the rent brake [... is] therefore only justifiable temporarily and as a rule only if sufficient measures are taken at the same time to expand the supply of housing*." ↘ ITEM 399 Unlike the Council majority, the dissenting Council member points out that, **due to the effects of the housing shortage**, it is probably **appropriate to already** gradually **phase out** the **rent brake by 2027** and that not only the lowering of the **rent caps** should be waived, but they could rather be **relaxed overall**. The current regulation also stands in the way of the investments required to achieve the climate targets in the building sector.

414. **If the current regulations lead to lower investment incentives** for new builds and less willingness to offer housing for rent, this would increase price pressure on the housing market. This, in turn, could increase political pressure to tighten regulation. However, as the state, within its financial leeway, would not be able to close a growing gap between housing supply and demand, **the situation on the housing market would worsen, particularly with regard to the insider-outsider problem**. ↘ ITEM 362

415. In order to prevent a possible **spiral of intervention from the outset**, more far-reaching measures than those mentioned in the main text could therefore be considered. At this point in time, although a **relaxation of regulation** could lead to a somewhat stronger increase in housing prices, a larger supply could be expected to **improve the availability and accessibility of housing**. Breidenbach et al. (2022) also show that (after an initially dampening effect on rents) the **rent brake** does not effectively reduce rents due to a lack of measures to enforce it (see also Thomschke, 2019), but it does have a **negative effect on the quality of rental housing**, as no modernisation is carried out. This suggests that relaxing the restrictions will not necessarily cause prices to rise significantly (Hiller and Schultewolter, 2014; Kholodilin and Ulbricht, 2014), but could reduce bureaucracy and increase investment in the quality of the housing.

416. An **extension of the rent brake**, which from the outset was established as a temporary regulation, **increases the uncertainty for investment** in residential construction and should therefore be critically scrutinised. In particular, a

tightening – such as the introduction of sanctions for non-compliance with the regulations – could lead to a further reluctance to invest. Based on historical experience (Kholodilin and Ulbricht, 2014), investors are also likely to expect adjustments to the cut-off date regulations for new construction, ↘ ITEM359 and this also impairs investment incentives.

The Council majority does not criticise the planned extension of the rent brake in its current form (BMJ, 2024c) and merely calls for a further extension beyond 2028 to be avoided. ↘ ITEM 401 However, **if the regulation continues** in its current form **until 2028**, it can be assumed **that the political pressure for an extension** beyond 2028 **will remain high**. In this case, it is questionable whether the desired 'credible commitment' ↘ ITEM 401 to take effective measures to expand the supply of housing by then will materialise. Private investment incentives are also likely to remain subdued.

417. When deciding whether to extend the rent brake "until there is a noticeable easing on the regional housing markets" (BMJ, 2024c), it must therefore be taken into account that the easing of the housing markets is likely to become less likely if the regulation is extended. In the event of an extension, consideration could therefore be given to **establishing a transitional regulation that sets out a path to the expiry of the rent brake**. For example (in addition to the proposed improvements in the preparation of rent indexes ↘ ITEM 400), the permitted deviation from the local reference rent could be gradually increased from 10 % to 15 % over two years before being withdrawn in the third year. In regions with smaller rent increases, the regulation could be relaxed completely at an earlier stage, while in very tight markets it is relaxed more slowly. The advantage of such an approach would be the **greater credibility of the exit from regulation**, which should have an immediate positive effect on private investment incentives.

418. Furthermore, the main text of the report rightly points out that **the current design of the rent caps widens the gap between new and existing rents in tight housing markets**. ↘ ITEM 402 If the rent brake were to expire as originally planned (or the transitional regulation proposed above were applied), this could also happen under the current regulation with a cap on rent increases of 20 % within three years.

419. Furthermore, the rent caps could affect the supply of housing. A rent increase of 20 % over three years may seem sufficient at first glance, but there are several reasons why this limit could make the supply of housing unattractive, especially for private landlords. For example, **the adjustments may not be sufficient to cover the increased costs in times of high inflation**. Moreover, interest rates on property loans have risen in recent years. Landlords who have to finance new properties or refinance existing loans have higher costs that may not be covered by the cap. This can be a problem, above all for the many small private landlords (BBSR, 2015b) who have to maintain financing for the property and may not have gone to the limits of what is possible when setting rents at all times. Excessively complex decisions and low yields could lead to an increase in sales to owner-occupiers, for example, who could then terminate the tenancy on grounds of personal need.

420. The current rent regulation **can** furthermore **make it difficult to switch to heat pumps or other climate-friendly heating systems in apartment blocks**. The costs of such a modernisation are often not easy for landlords to pass on (in full) to the rent. Tenancy law does allow 8 % of modernisation costs to be passed on to the annual rent (before 2019 it was 11 %). However, the scope for landlords is limited and the uncertainties are considerable, since rent increases in practice entail a high administrative burden and there are further restrictions and exceptions, for example due to rent caps (Henger et al., 2023). As a result, landlords may not be able to fully refinance the conversion costs, which reduces the willingness to invest. It is not without reason that the energy-related renovation rate in Germany is only around 1 %, which is below the Federal Government's target of 2 % (EEM, 2024); in apartment buildings, it is as low as 0.6 % (Knoche et al., 2024), so that owners are already benefiting to a considerable extent from the lower operating costs of climate-neutral heating systems compared to tenants (Grimm et al., 2023) ↘ ITEM 343. The option of realising rent increases via the modernisation apportionment is also rarely used (Knoche et al., 2024). **The consequence** in this case **is that tenants** will increasingly **have to bear the rising costs of fossil fuels** in future, which could jeopardise acceptance of the energy transition (EEM, 2024).

421. Various **adjustments to the regulations on rent caps** could therefore **be considered** beyond the proposals of the Council majority. One possibility would be to raise the maximum rent increase to 25 % within three years. Alternatively, annual adjustment options could be established. To a certain extent, a possibility should be created to make up for missed rent increases. This could be particularly helpful for private landlords who do not always plan the costs of maintenance and repairs precisely in advance and are sometimes unable to refinance the financial expenses in the event of a missed rent increase. Unforeseen repairs can become necessary, especially in older buildings, which can cause high costs in the short term. The current limit on rent increases could make it more difficult to compensate for these costs.

422. The proposed relaxation of regulation can contribute to **three objectives simultaneously**: (1) a **strengthening of supply** through higher investment incentives, (2) a **reduced need for fine-tuning by the state** in order to regulate the misallocation of housing and resources away from the market, and (3) a **reduction in bureaucracy**. Based on two aspects discussed in the chapter, the necessary fine-tuning and the associated bureaucracy will be briefly discussed here in conclusion.

423. ↘ ITEMS 382 FF. discuss the property tax reform in Germany under the title 'Unlock space potential' and rightly conclude that a land-value model provides the strongest incentives for building on the available land. The land-value model introduced in Baden-Württemberg reduces the tax payment for residential development by 30 % and thus makes it relatively more expensive to simply hold land. Furthermore, the Council majority also tends to favour the reintroduction of the option to levy property tax C. ↘ ITEM 385 However, it is to be expected that **the levying of property tax C will be accompanied by a high level of bureaucracy, particularly due to delimitation difficulties** (Deutscher Bundestag, 2017a,

2017b; Henger, 2018). Furthermore, the tax could lead to an additional financial burden for owners without achieving the desired effect, namely a faster development of the properties. If owners are unable to build because of financing difficulties, bureaucratic hurdles or a lack of infrastructure, the tax could put them under pressure to sell to professional investors, which could lead to a concentration of property in areas with a tight housing market. It is unlikely to be possible to deal with the many individual circumstances of property owners in a legally secure manner or to take proper account of structural obstacles to development. This was one of the reasons why property tax C failed back in 1961.

424. Similarly, the discussion on reducing the barriers to relocation, which begins in ↘ ITEM 395, illustrates **that it is unlikely to be possible to counteract the increase in residential space per person via** housing swaps, counselling services, shared apartments for students and older people, and other **relatively uninvasive, voluntary measures**. Rent regulation that makes housing available below the market price even for solvent tenants and makes it financially increasingly unattractive for tenants to change their housing situation leads to an increase in space consumption per person and reduces mobility. This happens at the expense of housing availability (e.g. because people no longer reduce their residential space in the course of their lives) and also increases the hurdles to changing jobs that go hand in hand with a move. **Rent regulation** in conjunction with social housing policy **could ultimately result** in **access to affordable housing for middle-income households being severely restricted**.

APPENDIX

↘ TABLE 17

Overview of the income limits for housing entitlement certificates in various federal states

Federal state	Income limits[1]	Special features
Federal borders	**Single-person household: €12,000; Two-person household: €18,000**	**Plus for each additional person included in the household: €4,100; plus for each child: €500**
Berlin[2]	Single-person household: €16,800 (WBS 140), €19,200 (WBS 160), €21,600 (WBS 180), €26,400 (WBS 220); Two-person household: €25,200 (WBS 140), €28,800 (WBS 160), €32,400 (WBS 180), €39,600 (WBS 220)	Plus for each additional person belonging to the household: €5,740 (WBS 140), €6,560 (WBS 160), €7,380 (WBS 180), €9,020 (WBS 220); Supplement for each child belonging to the household: €700 (WBS 140), €800 (WBS 160), €900 (WBS 180), €1,100 (WBS 220)
Bremen	Federal borders	
Hamburg	Single-person household: €19,200 (1st funding channel), €24,000 (2nd funding channel); Two-person household: €28,800 (1st funding channel), €36,000 (2nd funding channel);	Plus for each additional person in the household: €8,100 (1st funding channel), €12,200 (2nd funding channel)
Baden-Württemberg[3]	Single-person household: €57,800; also two-person household €57,800	Plus for each additional person belonging to the household: €9,000; Single parents can deduct the tax relief amount from their income; dependants can deduct maintenance payments from their income.
Bavaria[4]	Single-person household: €17,500; Two-person household: €27,500	Plus for each additional person belonging to the household: €5,000
Brandenburg	Single-person household: €18,500; Two-person household: €26,000	Plus for each additional person belonging to the household: €5,800
Hesse	Single-person household: €18,166; Two-person household: € 27,561	Plus € 6,265 per year for each additional person belonging to household; income limits increased by a further €833 per year for each child belonging to the household
Mecklenburg-Western Pomerania	Federal borders	
Lower Saxony	Single-person household: €17,000; Two-person household: €23,000	Plus for each additional person belonging to the household: €3,000; plus for each child included in the household: €3,000
North Rhine Westphalia	Single person: €20,420; two-person household: €24,600; single parent (1 child): €25,340; 3 persons (1 child): €31,000; 4 persons (2 children): €37,400; 5 persons (3 children): €43,800	
Rhineland-Palatinate	1 person: €18,500; 2 persons: €26,500; 3 persons: €32,700; 4 persons: €38,800; 5 persons: €54,000	Plus for each child in the household: €1,200
Saarland	Federal borders	

1 – With the exception of Baden-Württemberg, the net income is decisive when applying for a housing entitlement certificate (WBS). 2 – In addition to the housing entitlement certificates mentioned here, there is also the WBS 100, where the federal limits apply. 3 – Gross income. Corresponds to an annual net income of 36,378 euros for a single-person household with tax class 1. 4 – Districts/cities can set other income limits on their own authority if there is an „increased housing need“. 5 – In addition to those mentioned here, there are other types of WBS in individual cities, five more in Dresden alone with their own income limits.

Sources: Federal and state legislation, own presentation

↘ CONTINUATION OF TABLE 17

Overview of the income limits for housing entitlement certificates in various federal states

Federal state	Income limits[1]	Special features
Saxony[5]	Single-person household: €16,800 (first income limit), €21,000 (second income limit); Two-person household: €25,200 (first income limit), €31,500 (second income limit)	Plus for each additional person in the household: €5,740 (first income limit), €7,175 (second income limit); plus each child in the household: €700 (first income limit), €875 (second income limit)
Saxony-Anhalt	Federal borders	
Schleswig-Holstein	Single-person household: €14,400; Two-person household: €21,600	Plus for each additional person belonging to the household: €5,000; plus for each child: €600
Thuringia	Single-person household: €14,400; Two-person household: €21,600	Plus for each additional person belonging to the household: €5,000; plus for each child: €1,100

1 – With the exception of Baden-Württemberg, the net income is decisive when applying for a housing entitlement certificate (WBS). 2 – In addition to the housing entitlement certificates mentioned here, there is also the WBS 100, where the federal limits apply. 3 – Gross income. Corresponds to an annual net income of 36,378 euros for a single-person household with tax class 1. 4 – Districts/cities can set other income limits on their own authority if there is an „increased housing need“. 5 – In addition to those mentioned here, there are other types of WBS in individual cities, five more in Dresden alone with their own income limits.

Sources: Federal and state legislation, own presentation

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