

This February, Registers Iceland (RI), in collaboration with the Housing Financing Fund, began publishing data on paid rent, categorised by location and size of property. RI had previously published monthly data on the number of registered rental agreements. From now on, data published each month will extend to the number of registered rental agreements, the average rent price by property location and size, and the greater Reykjavík residential rent index, which shows the change in the weighted average price per square metre.

Various indices for the rental market

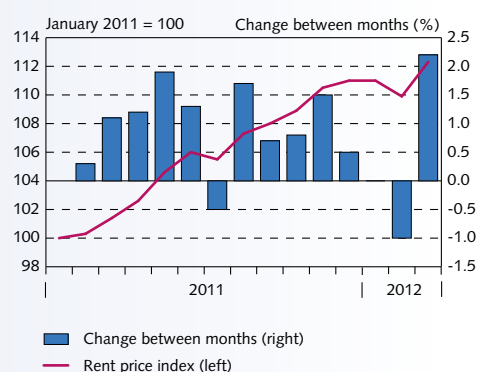
The rental market has grown by leaps and bounds in recent quarters, due in particular to financial hardships faced by a large number of households in the wake of the financial crisis. Hitherto, the index for paid rent, which Statistics Iceland (SI) compiles and uses as an input into the calculation of the consumer price index, has been the only information available on developments in rent prices. There is some difference between SI's paid rent index and the new rent price index from RI. The SI paid rent index is based on information for the entire country, while the RI rent price index includes only registered leases in the greater Reykjavík area. The calculation of the SI paid rent index is also based on rent information from municipalities where Reykjavík Social Housing is by far the largest landlord (50%) and from associations dominated by students and the Icelandic Federation for the Handicapped. Information on the general market is obtained from the rent subsidy allowance system. As a consequence, rental data compiled by SI strongly reflect rental agreements subsidised by the Government and therefore do not necessarily reflect true market prices.

In calculating the rent price index, RI categorises average rent prices and the number of registered leases by size of property (number of rooms), neighbourhood, and region. To enhance the quality of the index, leases for flats of unknown size, leases more than 60 days old, and leases for subsidised rental housing are excluded. The difference in the number of leases can be significant, as can be seen in Chart 2.

Box III-1

The Icelandic rental market

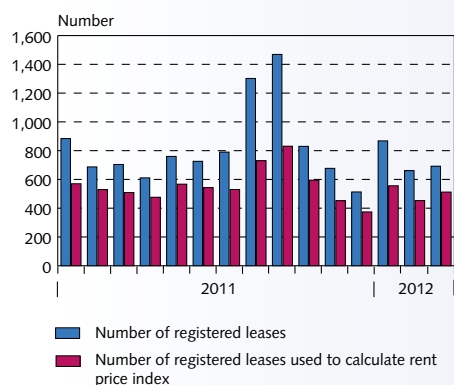
Chart 1
Registers Iceland rent price index
January 2011 - March 2012



Source: Registers Iceland.

Chart 2
Number of registered residential
leases nationwide

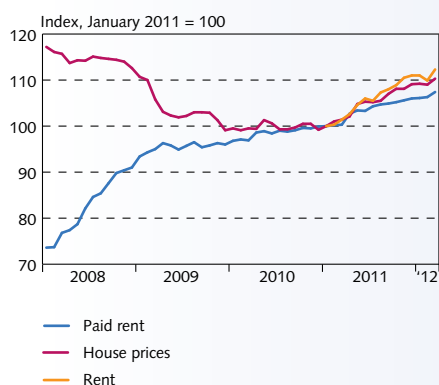
January 2011 - March 2012



Source: Registers Iceland.

Chart 3
Rent, house prices, and paid rent
in nominal terms

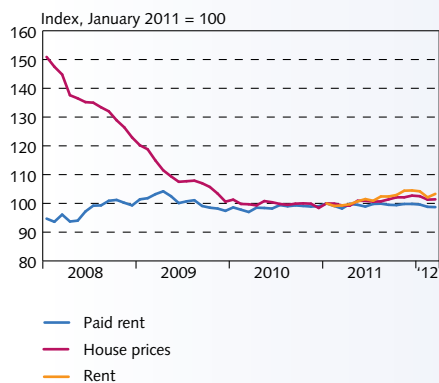
January 2008 - March 2012



Sources: Registers Iceland, Statistics Iceland.

Chart 4
Rent, house prices, and paid rent in real terms

January 2008 - March 2012



Sources: Registers Iceland, Statistics Iceland.

To enhance the quality of the paid rent index, SI plans to gain access to RI data but will continue to gather data from Reykjavík Social Housing, as those leases do not require registration.

Shortcomings in the RI rent price index

Registration of leases is not required by Icelandic law; therefore, it is likely that some rental contracts are not registered. This is probably more often the case with higher-priced properties, as high-income tenants are not eligible for rent subsidy allowances and therefore have little incentive to register their leases.¹ By the same token, leases for the least expensive flats are unlikely to be registered, as no subsidies are paid for single rooms, reducing the incentive to register these leases as well. Leases for six months or less are also ineligible for rent subsidies and may also be underrepresented in registration data.

Developments in house prices and rent

It is interesting to compare developments in house prices and rent. Because RI rent price index data extend back only to the beginning of 2011, the paid rent index from Statistics Iceland is used for earlier periods. Chart 3 shows developments from the beginning of 2008, with nominal prices falling by over 15% from their January 2008 peak until they hit bottom in December 2009. Paid rent rose by about 30% over the same period, however. The year-on-year change in the RI rent price index was 10.7% in March 2012, whereas SI's paid rent index and house price index rose by 7% and 8.7%, respectively, over the same period. Chart 4 shows that real house prices fell by about a third from January 2008 onwards. The real price of paid rent has remained relatively stable since January 2008, with the RI rent price index rising about 4% in excess of inflation between March 2011 and March 2012.

Price-to-rent ratio

The publication of data on average rent price and number of registered leases by property size (number of rooms), neighbourhood, and region provides a good overview of the rental market. This information can also help prospective buyers faced with deciding whether to buy or rent, as the price-to-rent ratio gives an indication of which option is more economical. It is often argued that if the price-to-rent ratio is under 15, it is more profitable to buy than to rent. If the ratio is between 16 and 20, it is better to buy if the intention is to hold the property and better to rent if the intended holding period is short. If the ratio is higher than 20, it is considered more profitable to rent than to buy.² Table 1 shows the price-to-rent ratio by neighbourhood and region in 2011. It is under 15 in all cases, indicating that it is more economical to buy a flat than to rent. The price-to-rent ratio is often considerably higher in Europe and the US than in Iceland, due to differences in factors such as interest rates, credit system, statutory rent control (which is non-existent in Iceland), and variations in rent by location.

1. Monthly rent subsidy allowances are reduced by 1% of annual income in excess of 2 m.kr. This refers to combined total income of all individuals with a legal domicile or residential address at the rental property in question. See also the Act on Rent Subsidy Allowances: <http://althingi.is/lagas/nuna/1997138.html>. (in Icelandic).
2. See, for example, <http://www.investopedia.com/terms/p/price-to-rent-ratio.asp#axzz1peJ2rnr4>.

Table 1 Price-to-rent ratio in 2011, by neighbourhood and region

Reykjavík west of Kringlumýrarbraut and Seltjarnarnes	13.4
Reykjavík between Kringlumýrarbraut and Reykjanesbraut	12.8
Kópavogur	13.4
Garðabær, Hafnarfjörður, and Álftanes	13.3
Grafarvogur, Grafarholt, Árbær, Norðlingaholt, and Úlfarsárdalur	12.5
Breiðholt	11.4
Kjalarnes and Mosfellsbær	13.5
Suðurnes peninsula	11.8
West Iceland	12.5
West Fjords	8.9
North Iceland	11.4
East Iceland	9.6
South Iceland	10.9

Source: Registers Iceland.