

Anticipated Property Tax Increases on New Construction Spur Gentrification: Evidence from New York City

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Abstract

In 2006, the New York City government decided to make property tax incentives on new construction less generous, starting in 2008. Developers responded by rushing to apply for these benefits and began building before the deadline. The magnitude of excess housing starts at the deadline suggests that a 1% increase in the future property tax increased current residential investment by 0.4%. A naive demand-supply model indicates that these new units brought to the market by the reform should lower rents in nearby incumbent units. On the contrary, I find that the rents in nearby incumbent units increased. Using the baseline land availability within a small radius around an incumbent unit as an instrument, I find that an additional new tax-exempt unit during the bunching period *increased* the incumbent unit rent by 2.3%. I find evidence consistent with the hypothesis that new residential investment made neighborhoods more desirable by attracting affluent households, facilitating the entry of businesses and consumption amenities. Overall, the results indicate that the *new* investment spurred gentrification.

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