

Shoresh Research Paper

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Beyond the Shortage: A Structural Perspective on Israel's Housing Market

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Abstract

Israel's housing crisis is reflected not only in a relative shortage of housing units but also in structural failures: too few small apartments are being built to match the changing composition of households, and the rental market – on which more than a third of households now rely – is based on private landlords and short-term leases. The result is instability and a heavy housing burden, comprising over 30% of household disposable income, according to the OECD definition. The findings point to a need for targeted reforms, creating a more diverse mix of dwelling sizes, developing long-term institutional rental housing, and aligning local authorities' fiscal incentives with national goals.

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1. Introduction

Israel's housing crisis has persisted for more than two decades. Although it has received extensive public attention and has been the subject of repeated government initiatives (Bank of Israel, 2023a; Azankot, 2023), housing prices have risen faster than household incomes. As a result, households' ability to purchase a home has eroded.

The problem is not limited just to high housing costs. Beneath the surface lies a deeper structural problem: a gap between what is built and households' actual needs. The fastest-growing group of households in recent years is small households – single individuals, couples, and single-parent families (Central Bureau of Statistics, 2025). Nevertheless, the share of small dwellings being built is low (Naor, 2022), while the share of households renting their dwelling has increased. Consequently, Israel's rental market relies on short contracts and private ownership, and the supply of long-term rental housing remains limited.

The partial mismatch between demand and supply in the size mix and housing characteristics has many implications. Households that rent are forced to cope with uncertainty and frequent moves, which may harm the schooling continuity and educational achievements of their children (e.g., Leventhal and Newman, 2010; Sandstrom and Huerta, 2013). Since women tend to work close to their place of residence, they face employment barriers when there is a limited supply of rental housing near employment centers, (Le Barbanchon et al., 2021). At the other end of the life cycle, many older adults remain in large, unsuitable dwellings because the market does not offer alternatives for downsizing, which also constrains the availability of larger units for larger households.

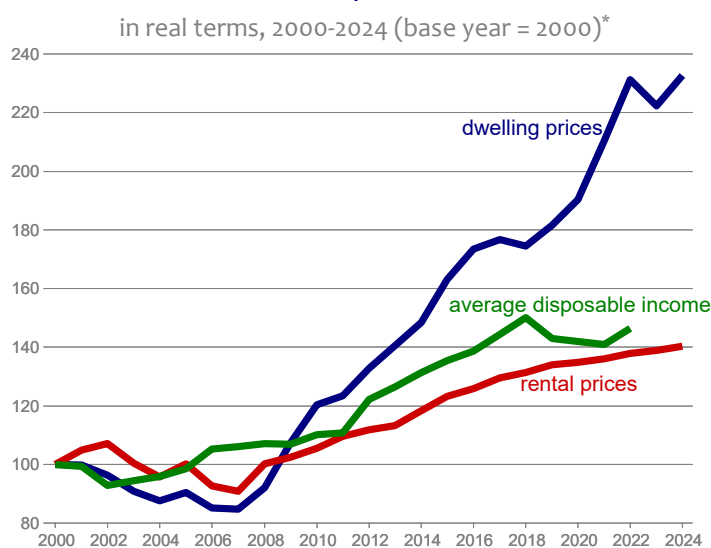
This study documents the nature and extent of mismatches in Israel's housing market, focusing on two dimensions: a shortage of small dwellings suited to the needs of the growing segment of small households; and the lack of long-term rental options, despite the expansion of the renter population. The analysis combines descriptive findings from Israeli data with an international comparison. The findings point to a need for structural reform in housing policy –

one that recognizes housing not only as a financial asset but also as vital infrastructure for human capital and sustainable growth.

2. Affordability crisis

Housing affordability describes households' ability to finance their housing needs (ownership or rent) and is measured by the share of disposable income allocated to housing expenditures. In OECD countries, a threshold of 30% of disposable income is commonly considered as a maximum reasonable housing expenditure (OECD, 2021). Figure 1 presents the real increase (i.e. inflation-adjusted) in housing prices, rent, and households' disposable income.¹ The most salient feature of Israel's housing crisis is the widening gap between housing prices and incomes. Since 2007, housing prices have been detached from the general price index. While the overall index rose at a relatively moderate pace, housing prices grew at an annual real rate of about 5.2%. Over the same period, households' real net income grew by only about 2.0% per year. This means that a growing share of income is required for housing at the expense of other consumption components.

Figure 1
Dwelling price indices compared with household disposable income



* The housing component of the index measures changes in the cost of consuming a fixed basket of housing services – both rental housing and owner-occupied dwellings. All indices are standardized so that the average value of the index in 2000 equals 100 points.

Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

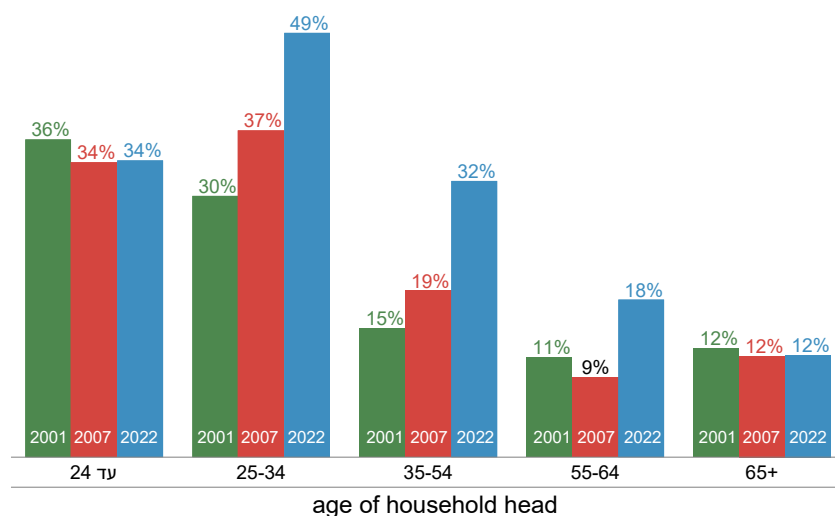
¹ The data used to calculate the housing component are based on the rent survey conducted on an ongoing basis by the Central Bureau of Statistics (CBS) and includes about 18,000 households per year. The rent component is calculated based on the change in rent paid for the same dwelling relative to the rent paid the previous month. Housing services in owner-occupied dwellings are determined only on the basis of new and renewed rental contracts (in the first month of the lease). The home price index is based on Israel Tax Authority data and is calculated using a hedonic regression that takes into account dwelling characteristics and nets out changes in quality. It cannot be ruled out that the rent index is biased downward because it is composed mostly of rents in existing contracts rather than contracts signed in the sample month, which better represent changes in prices (Raz-Dror, 2019).

The Alrov Affordability Index measures the average monthly repayment required on a 25-year mortgage to purchase a typical four-room apartment, assuming a 70% loan-to-value ratio, in Israel’s 12 largest cities. At the end of 2024, the average repayment was NIS 11,407 per month, about 50% of net income in the sixth income decile (Ben-Shahar and Nayer, 2025). This means that a large share of the population, including the middle class, finds it difficult to achieve homeownership.

The increasing burden of rising housing costs has changed residential patterns in Israel. The share of renters rose from 26.8% in 2007 to 32.4% in 2022.² Renting is not confined to young people at the beginning of the life cycle. More and more middle-class families – and even older households – turn to the rental market because homeownership has become harder to attain. In 2022, nearly half of households headed by people aged 25-34 lived in rental housing, compared with 30% twenty years earlier (Figure 2).

The picture comes into sharper relief when examining changes by household size. As shown in Figure 3, there is just a slight change in the share of two-person households living in rental housing over the years. But there is a much more noticeable increase in the renter share in all other household-size groups. In other words, renting extends beyond singles and young couples and is expanding to larger households as well.³

Figure 2
Share of households living in rented dwelling
by age of household head

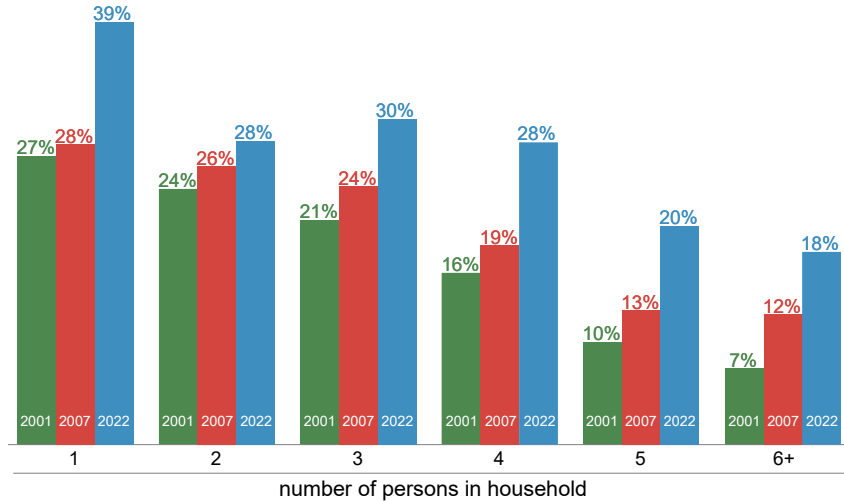


Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

² Figure A.1 in the Appendix shows the increase in the likelihood of living in rented housing relative to the likelihood in 2001.

³ In two-person households, there is a high share of older households (about 63% are over age 55 as of 2022). These households are less likely to live in rental housing, as shown in Figure 3. A breakdown of the age distribution by household size appears in the appendix.

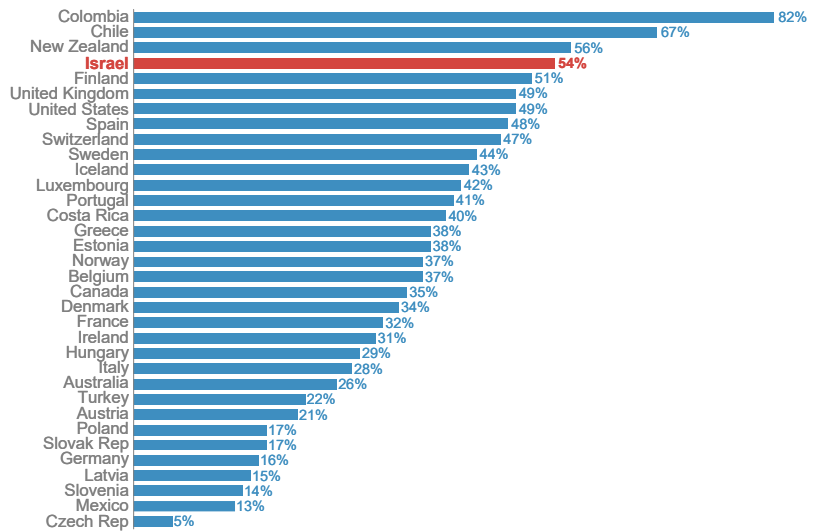
Figure 3
Share of households living in rented dwelling
by household size



Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

The rental market also does not offer an affordable solution for everyone, even though rent increased more moderately than purchase prices (as shown in Figure 1). Among low-income households, the rental burden already exceeds the OECD affordability threshold. More than half of the bottom income quintile pay more than 40% of their income on rent. This share is among the highest in OECD countries, as shown in Figure 4. In major cities such as Tel Aviv and Jerusalem, the rental burden for a four-room apartment has crossed the 30% threshold of households' average net monetary income (Central Bureau of Statistics, 2022).

Figure 4
Share of bottom quintile spending over 40% of their disposable income on dwelling rental payments, 2022



Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: OECD (2023) Affordable Housing Database

3. Demand side

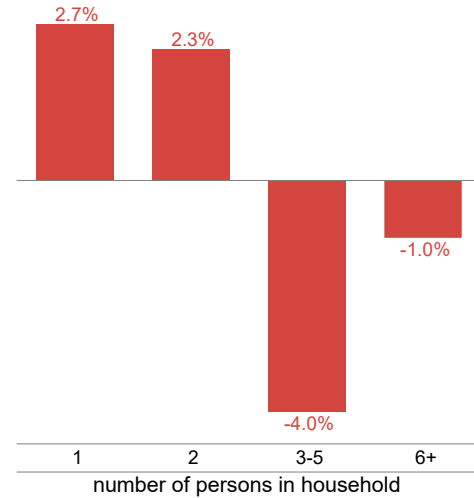
For many years, demand for residential housing in Israel has risen, primarily due to population growth. At the same time, average household size has declined. While in the 1970s the average household comprised 3.8 persons, by 2022 it had fallen to 3.2 persons due to demographic changes in the composition of the population.

The decline in average household size stemmed from an increase in the share of small households (singles and couples) among all households, as reflected in Figure 5. Whereas small households made up 41.4%

of all households at the beginning of the 2000s, over two decades their share rose to 46.4%, alongside a reduction in the share of larger households, especially those with 3-5 persons.

The growth trend in the share of small households differs across population groups. In 2022, the share of small households in the non-Arab population (Jews and others) was 51%, compared with only 22% in the Arab population. However, over the last twenty years, the growth rate in the number of small households in the Arab population was three times that recorded among the rest of the population (Central Bureau of Statistics, 2025). Demographic changes such as a rise in age at marriage and in divorce rates are expected to continue increasing the share of small households in this population group.⁴

Figure 5
Change in the share of differently sized households*
out of total households, by number of persons, 2022 relative to 2001



* percentage point change

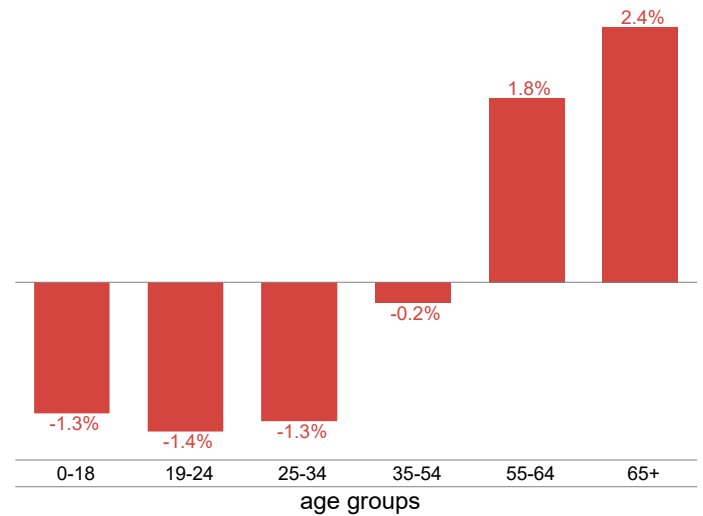
Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

⁴ The median age at marriage among Muslims (who constitute 83% of Israel's Arab citizens) increased over the past two decades from 25.7 to 27.2; the divorce rate over the same period among Muslim men aged 15-49 rose from 6.1 in 1996 to 9.3 in 2023.

One of the drivers of the decline in household size is population aging. This is reflected in the increasing share of older adults, who are at a life stage in which children have already left home. Figure 6 shows the change in Israel's age distribution between 2001 and 2022, illustrating a relative increase in the share of those aged 55 and over alongside a decline in the share of younger people up to age 34. This trend is also reflected in the absolute data: the share of those aged 55 and over rose from 16.4% in 2001 to 20.8% in 2022. At these ages, living in small households is particularly common. Only about 24% of those aged 35-54 live in small households, compared with 59% among those aged 55-64 and about 90% among those aged 65 and over.

Alongside population aging, changes in family composition also contribute to the decline in household size. Figure 7 presents the change in the distribution of the population aged 18 and over by marital status between 2001 and 2022. During this period, the share of married individuals fell from 63.5% to 59.6%. At the same time, the share of never-married individuals rose by about 3.6 percentage points and the share of divorced individuals rose by about 2.5 percentage points.

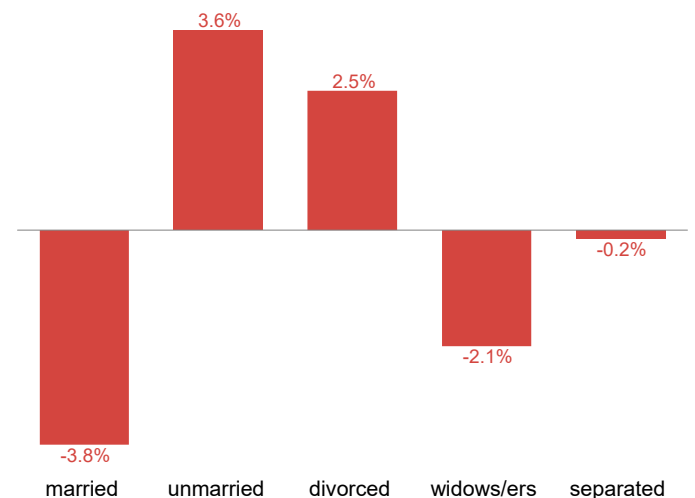
Figure 6
Change in distribution of age groups*
change in the share of each age group in total population, 2022 relative to 2001



* percentage point change

Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

Figure 7
Change in household shares, by household status*
out of 18+ population, 2022 relative to 2001



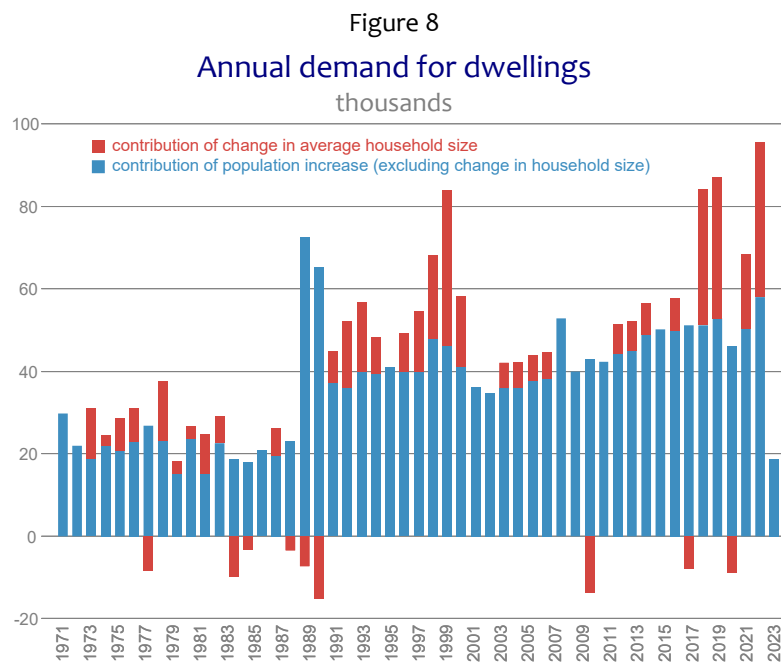
* percentage point change

Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

These trends reflect an ongoing social change that has led to an increase in the share of households consisting of single individuals and couples without children.

The decline in average household size contributed significantly to rising housing demand. Figure 8 presents the annual demand for housing units, broken down into two components: demand arising from population growth and additional demand resulting from the decline in the average household size. As shown, the contribution of population growth is relatively stable over the years (aside from

the large increase in 1989-90 following the wave of immigration from the Soviet Union). In contrast, the contribution of the decline in household size is more volatile, though it has been substantial in several of the years. By way of illustration, had the average household size in 2022 remained at 3.8 persons, similar to its level in the 1970s, the number of households in Israel would have totaled approximately 2.5 million. In practice, the number is about 2.9 million. Thus, the decline in household size created cumulative demand for nearly 400,000 dwellings, about 17% of total housing starts since the 1970s. The decline in household size occurred alongside substantial population growth in Israel, as noted above – from 3.3 million residents at the end of 1973 to about 9.6 million at the end of 2023. This growth stemmed both from natural increase and from immigration, mainly the arrival of about one million immigrants from the former Soviet Union in the early 1990s. However, the number of households grew at an even higher rate: while the population grew by about 290% between 1973 and 2023, the number of households grew by about



Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

350% over the same period. The gap between these growth rates highlights the contribution of changes in household structure as an independent factor expanding demand for housing.

In addition to demographic variables, demand for housing is also affected by financial and institutional conditions, foremost among them the interest rate environment and the fiscal system. The low real interest rate made mortgages cheaper, encouraged purchases of owner-occupied housing, and steered investors toward housing as a substitute for financial investments (Genesove, 2021). This was compounded by tax distortions: while capital gains in the capital market are taxed at rates of 10%-25%, rental income is exempt from tax up to a ceiling of NIS 5,654 per month (NIS 67,848 per year). This gap creates a structural distortion that favors investment in residential dwellings over investment in other financial instruments. This dynamic was further strengthened by regulatory changes. The wave of investor purchases in 2021 ahead of the increase in the purchase tax illustrates how strongly tax policy shapes demand patterns (Ministry of Finance, 2021b). Another example of the impact of tax policy on investors' activity in the housing market emerges from Ater et al. (2021). The study found that measures intended to reduce the attractiveness of investing in dwellings – such as raising the purchase tax for investors, abolishing the capital-gains tax exemption, and providing temporary incentives to sell dwellings – led to an increase in sales of investment dwellings.

The combination of low real interest rates and tax benefits for private investors attracted many investors to the housing market over the past decade. Their purchases added pressure on prices, sometimes even crowding out first-time homebuyers – especially young households from the middle class (Ministry of Finance, 2021a).

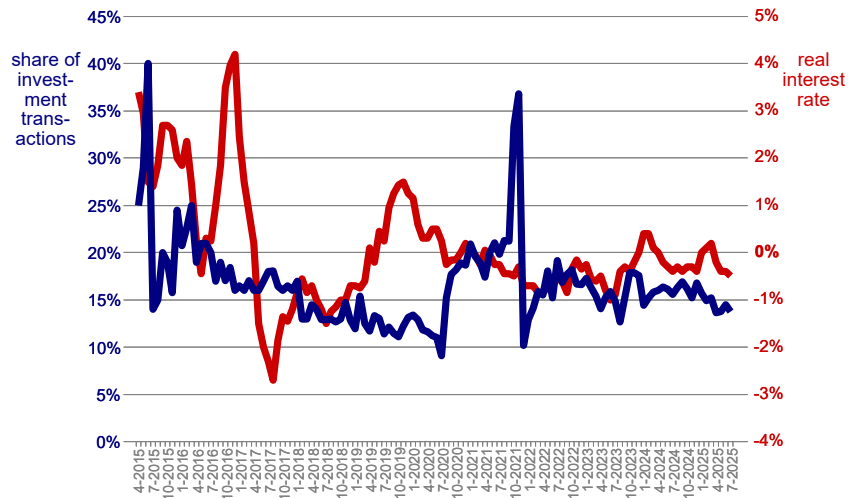
Figure 9 depicts the share of investor purchases alongside the expected real interest rate. Extraordinary purchase fluctuations were recorded around tax changes, especially the purchase tax, underscoring the impact of fiscal policy alongside monetary conditions. The combination of the two created sharp fluctuations in demand for investment in housing.

Income levels also affect patterns of housing demand. An increase in income per capita increases households' ability to purchase a dwelling, both for residence and as an investment. It also allows families to move from crowded living arrangements to independent housing, or young tenants to leave shared apartments and move into single-occupancy units.⁵ Central Bureau of Statistics data (2025) point to a potential for additional housing demand from households that include more than one family: in 2023 there were about 33,600 households in which more than one family lived; in addition, about 47,000 households consisted of non-family groups, which may also point to latent demand associated with improvements in living standards.

It is interesting to note that about 19% of households living in rental housing in 2022 also owned a dwelling. Within this group, about 11.2% of all renters also made mortgage repayments on the dwelling they owned, even though they did not live in it (Central Bureau of Statistics, 2022). This phenomenon illustrates the influence of incentives and social norms to “enter the market” even when the dwelling does not meet actual housing needs.

In summary, the set of forces – demographic growth, declining household size, an accommodative monetary environment, tax distortions, and rising income – all pushed the demand side upward.

Figure 9
Real interest rate and share of investment transactions out of total monthly dwelling sales, 2015-2025*



* The expected real interest rate is the Bank of Israel interest rate net of inflation expectations, as implied by the yield spread between inflation-indexed government bonds and nominal shekel government bonds in the capital market. The rate of change in home prices is the annual percentage change in the owner-occupied dwelling price index.

Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Finance Ministry and the Bank of Israel

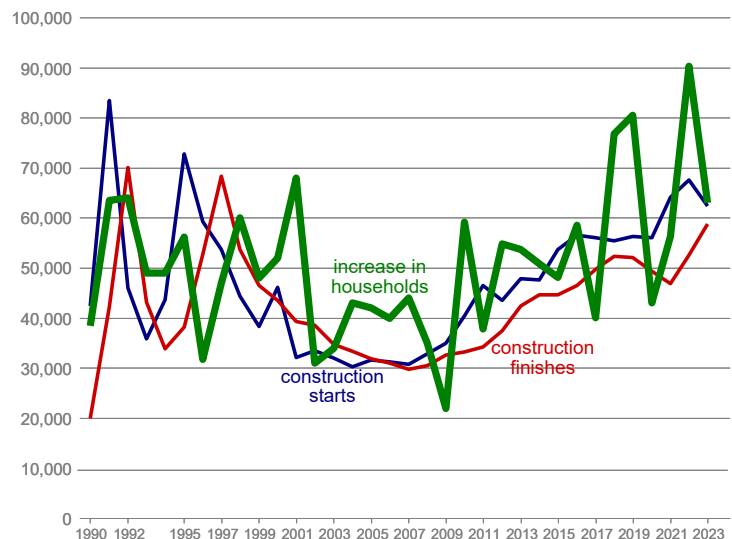
⁵ Genesove (2021) estimates that each 1% increase in GDP per capita translates into additional demand of about 25,000 dwellings.

4. Supply side

While demand pressures contributed to the worsening affordability crisis, its intensity cannot be understood without also looking at the supply side. The supply of new dwellings has failed to keep pace with growth in the population and the number of households, and certainly has not adjusted to the changing composition of demand.

Figure 10 presents the change in the supply of new dwellings through the number of housing starts and the number of completed dwellings. In a long-term perspective, aside from a temporary step-up in the 1990s to absorb the immigration wave from the former Soviet Union, there appears to be no essential change in the number of dwellings added to the housing supply each year. In the late 1990s, with the completion of absorption of the large immigration wave, housing starts began a prolonged decline that lasted about a decade. In 2007 the trend reversed and the number of housing starts began to rise. However, since that period, completions have remained below starts – evidence of longer construction completion times.

Figure 10
Annual supply and demand for dwellings
1990-2023



Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

5. Failures in the housing market

Land planning and marketing

Land planning and marketing in Israel are characterized by high centralization alongside institutional fragmentation. Israel's land market is dominated by the Israel Land Authority (ILA), which holds most of the land reserves, but planning processes involve many bodies – government

ministries, local and district committees, and infrastructure agencies – resulting in delays and lack of coordination.⁶ For land that is not designated for residential use to be converted to residential zoning, a lengthy planning process is required, which can take seven to ten years or even more (Naor, 2022).

To shorten planning procedures, the National Committee for Planning and Building of Preferred Housing Complexes (VATMAL) was established in 2014. Indeed, 90% of the dwellings planned under this framework were approved within the standard time, compared with less than 50% in the regular planning process (State Comptroller's office, 2023). However, VATMAL has been criticized for harming planning quality and the balance of local interests.

Even after statutory approval, land is marketed mainly by the Israel Land Authority through tenders, a process that advances slowly and depends on the completion of infrastructure by local authorities. The result is that about half of the planned dwellings do not progress at all to the stage of applying for building permits (Bank of Israel, 2024; State Comptroller's office, 2023).

Permits and licensing

Licensing procedures in Israel are complex, and the multiplicity of bodies involved creates uncertainty and lengthy delays. According to the State Comptroller's office (2021a), the average time to obtain a building permit through the regular track was about 319 days, and in cases involving planning reliefs for developers – a more complex process – it lengthened to about 407 days. In complex projects such as urban renewal, the process is even longer: three to four years in demolition-and-reconstruction (pinui-binui) projects or structural strengthening (Bank of Israel, 2023b).

Beyond regulatory complexity, local authorities have little incentive to expedite residential projects, since residential development yields relatively low property-tax revenues compared with

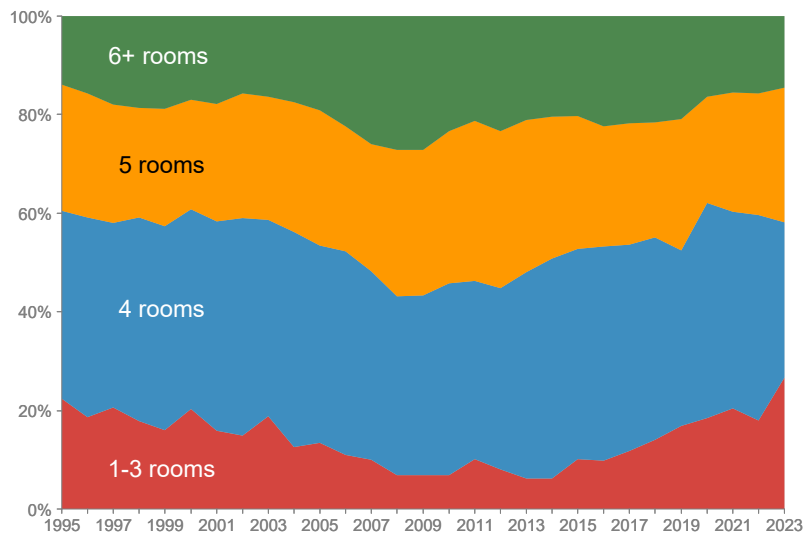
⁶ The State of Israel directly owns about 70% of the land and another roughly 10% through the Development Authority. In addition, the Israel Land Authority (ILA) also manages land owned by the Jewish National Fund (JNF). In total, the ILA manages about 90% of the land.

commercial uses. To overcome this barrier, “roof agreements” (Heskemei Gag) have been used since 2013, under which the government finances infrastructure and public buildings and the municipality commits to advancing building permits at an accelerated pace (Decision 768). Despite some localized successes, the State Comptroller’s office (2021b) found significant gaps between marketing targets and implementation, especially in the case of land for commercial uses: by 2021, only about 7% of the land designated for these uses had actually been marketed. This situation deepens municipalities’ dependence on budget transfers on the one hand and limits the development of employment opportunities for residents on the other.

Mismatch in the housing-size mix

Even when new dwellings are built, their size distribution does not match actual demand patterns. A housing preferences survey (Naor et al., 2023) found that about two thirds of respondents in small households residing in an apartment of 80 square meters or more expressed willingness to live in a smaller unit. Large apartments dominate new projects, while small households (1-2 persons) account for about 45% of all households. Figure 11 shows the decline in the share of small apartments out of total housing starts in 2004-2014. In subsequent years, their share began to rise, mainly due to the construction of small apartments in Tel Aviv, but even after this trend change, the share of new small apartments remained below 20% of total housing starts.

Figure 11
Construction starts by number of rooms in dwelling
1995-2023



Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

On the supply side, there are clear incentives to prefer building large apartments. Developers tend to prefer more affluent buyers. In addition, local authorities sometimes impose planning constraints.⁷ The result is that the size mix of new apartments primarily reflects existing planning norms rather than households' changing needs. This creates an ongoing shortage of small, affordable apartments despite the continuous rise in the share of small households in the population.

Urban renewal – limited realization

Urban renewal is viewed as a central component of housing policy in Israel. But in practice, its contribution to resolving the affordability crisis is limited. Demolition-and-reconstruction (pinui-binui) projects and TAMA 38 are concentrated almost exclusively in high-demand areas in the center of the country, where land and property values are high enough to justify the project's economic cost.⁸ By contrast, in peripheral municipalities where land prices are low, projects are hardly advanced at all (Government Authority for Urban Renewal, 2025).

As a result, urban renewal not only fails to provide a solution to the shortage of affordable housing, it may even deepen regional disparities: property values rise in high-demand areas while the quality and value of housing in the periphery continue to deteriorate. Instead of producing a broad and tailored variety of housing solutions, the existing mechanism reproduces center-oriented

⁷ For example, Shlomit Tzur (TheMarker, 11 April 2025) quotes the architect Royzin: “Despite the existing need, many municipalities do not encourage small apartments, thereby pushing out of the city people who do not need large apartments. Those people also occupy apartments that are double the size they need. Ra’anana, for example, is a municipality that encourages large apartments because it defines itself as a city for families. But once there are no small apartments, for instance when a couple divorces, both spouses are forced to occupy two large apartments, which are taken out of the stock of apartments that families really need. In practice, many people live in apartments that do not suit them.” Hila Yanai-Levinson (Globes, 5 April 2025): “Many local authorities are not interested in small apartments, out of concern that they will attract weaker populations or students” (in an interview with Nir Muallem, head of the Urban and Regional Center at the Faculty of Architecture and Town Planning at the Technion).

⁸ Pinui-Binui (demolition-and-reconstruction) is an urban renewal project that involves demolishing old buildings and constructing new ones at higher density, while providing new apartments to existing residents and financing the project through surplus building rights. TAMA 38 is a National Outline Plan for strengthening buildings against earthquakes, which allows for additional building rights or demolition and reconstruction, and has been implemented primarily at the level of individual buildings.

development patterns and reinforces the mismatch between housing supply and the population's changing demographic needs.

In summation, these supply-side failures mean that even record levels of housing starts are not translated into improved affordability. The bottlenecks are not only related to the number of units built, but also to the institutional arrangements that determine where, at what pace, and what types of dwellings are constructed. Without reforms in land marketing, planning procedures, and the unit-size mix, the gap between supply and demand will persist regardless of aggregate construction figures.

6. The rental market

Israel's rental market has become a central component of housing in recent years, with more than a third of households now living in rental housing. However, the quality of the market's response remains low: short contracts, an almost exclusive reliance on private landlords, and low yields that do not attract institutional players (because housing prices rose much faster than rents). The result is a market structure that does not provide long-term security, creates instability, and exacerbates the affordability crisis.

The vast majority of rental units in Israel are held by private landlords (about 89%), while the public and institutional sectors together account for less than 5% of the market.⁹ This means the market is fragmented, without large players that can offer long-term leases, stable management services, or internal oversight of quality and maintenance. Most leases are signed for one year only. In practice, the duration of residence in a rented apartment tends to be longer – about 3 to 4 years on average – but these are estimates based on data from companies and private entities, since Israel lacks an official, up-to-date system that measures actual tenancy duration. This gap between the formal contract length and the real length of residence creates ongoing dependence on lease renewals and increases uncertainty for renters.

⁹ The remaining renters rent from other parties such as student dormitories or yeshivot, the government, a local authority, a kibbutz, or a cooperative moshav.

The weakness of Israel's rental market is also evident in the price-to-rent index, which measures the ratio between a dwelling's price and annual rental income. In 2007-2024, the index increased in Israel by a factor of 2.02, compared with an average of 1.21 in OECD countries (OECD, 2025a). The gap is particularly pronounced compared with countries in which the rental market is more institutional and stable, such as Germany (1.45) and Switzerland (1.46). The sharp increase indicates that housing prices in Israel have detached from rental income, so investing in housing pays mainly as a capital investment rather than as a source of ongoing yield. This creates an apparent contradiction: rents in Israel rose steadily, yet the index points to relatively low returns. The contradiction is explained by the fact that housing purchase prices rose much faster than rents. While rent is constrained by households' ability to pay, purchase prices are also influenced by tax benefits, credit conditions, and expectations of capital appreciation.

Supporters of investor activity sometimes argue that it improves the market because it increases the supply of rental housing. In practice, Israel's tax system encourages small investors but scarcely promotes institutional development of long-term rental housing. Investor purchases often compete directly with first-time buyers over small and medium-size apartments in central locations, raising prices without improving stability or accessibility for renters (Ministry of Finance, 2021a). In recent years there have been attempts to develop an institutional rental sector through REITs¹⁰ and private developers, but even today the scale remains limited. Financial statements as of 31.12.2024 show that the yield on income-producing real estate is about 2.5%. The rise in interest rates in recent years casts doubt on their viability, despite tax benefits and land discounts they receive.

The mismatch is clear: more households in Israel rely on the rental market than ever before, yet the institutional framework overseeing it remains weak. In contrast to Israel, some countries have multi-year or unlimited rental contracts, along with protections against eviction and

¹⁰ A Real Estate Investment Trusts (REIT) is an investment instrument intended for investment in income-producing real estate, and their securities are traded on the stock exchange. On the Tel Aviv Stock Exchange, two funds operating in the residential sector are listed for trading (Megurit and Azorim Living). The funds operate by purchasing clusters of apartments or by developing buildings intended for rental.

mechanisms that enable institutions to supervise maintenance quality and service (OECD, 2021; 2025b). Rather than mitigating the affordability crisis, Israel's existing structure exacerbates it and creates a high rental burden, residential instability, and limited security. Without reforms that align incentives and protections, the rental market will not be able to fulfill its vital role as infrastructure for long-term housing stability.

An attempt to encourage an increase in the supply of long-term rental housing was made in 2013 with the establishment of the government company "Dira LeHaskir" ("Apartment for Rent"), whose goal was to increase the supply of rental dwellings by marketing land to developers who commit to build for long-term rental (after 10 years, the developer may sell the units). In practice, the company did not succeed in significantly increasing the supply of dwellings.

7. Policy

The persistence of Israel's housing crisis, despite high levels of construction, indicates that the problem is not only quantitative but also structural. This study's findings point to two key failures: (a) an ongoing shortage of small apartments suited to the growing share of small households, and (b) the absence of an institutional framework that would enable the rental market to serve as a stable long-term solution. The objective of the policy recommendations below is to improve the fit between housing supply and the population's needs.

Unit mix

The data show that new construction projects mainly include large apartments, while about 45% of households in Israel consist of 1-2 persons. In lieu of change, developers maximize profitability through large and expensive units, exacerbating the shortage of small, affordable apartments. Since residential construction in any case requires statutory and planning approvals by the authorities, this is not about increasing government involvement but rather about a

redirection of existing tools. In other words, building approvals can be conditioned on a more diverse unit mix better matched to the demographic composition of households.

The need is not merely technical but structural: a variety of dwelling sizes enables better matching to the population's changing needs and reduces long-term distortions. Israel's Planning Administration has already proposed such a mechanism (Planning Administration, 2022). Studies indicate that small apartments are vital for diverse populations – young adults, couples at the start of their path, small families, and older couples whose children have left home (Naor et al., 2022). In the absence of small apartments, these households are pushed into larger and more expensive units that are not suited to their needs.

Beyond the social dimension, small apartments can serve as a policy tool for improving market efficiency: they contribute to lowering rents in city centers, increase density in high-demand areas, and create a more diverse stock (Na'eh et al., 2025). Thus, they are not only a response for specific groups but a central component of housing policy that seeks to align supply with changing demographic patterns.

The rental market

This study's findings indicate that the rise in Israel's renter share has made the rental market a major component of the housing market. And yet, the market relies almost entirely on private landlords (about 89%) and short-term contracts. This structure creates instability, vulnerability to rent increases, and frequent moves. The needed regulation is not rent control – a tool that has proven problematic in many countries – but rather an institutional framework that incentivizes large landlords and sets standards for long-term leases.

International comparisons show that such solutions are feasible and beneficial. Countries such as Germany and the Netherlands operate institutional rental markets with multi-year contracts, basic protections for tenants, and incentives for institutional investors that enable renting to serve as a stable long-term solution (OECD, 2021; Kholodilin, 2020). Another prominent

example is the United Kingdom, where a Build-to-Rent (BTR) sector has developed over the past decade, focusing on long-term rental owned by companies and funds.

The British experience illustrates that through tailored regulation, tax incentives, and designated land, long-term leases can be turned into a lucrative institutional investment channel. Since 2012, the UK has adopted a series of systemic measures to promote institutional-owned long-term rental housing. A government unit was established to coordinate between the government, local authorities and investors. At the same time, a fund was launched to finance loans to institutional entrepreneurs for the construction of long-term rental projects, and state guarantees were given for institutional loans. These measures, combined with targeted tax incentives, including purchase tax relief, deduction of financing and maintenance expenses, and deferral of capital gains tax, created a stable regulatory and financial framework that enabled rapid growth of the sector (MHCLG, 2018; Homes England, 2018). According to a report by Blue Castle Capital (2025), published by an investment firm with a business interest, BTR's investments have grown to tens of billions of pounds while developing residential complexes managed by professional bodies. Although the report reflects an industry perspective, it illustrates how, through tailored regulation and tax incentives, leasing can be turned into a profitable institutional investment channel, thereby increasing tenant stability and reducing dependence on small investors.

The budgetary cost differences between encouraging home purchase and encouraging long-term rental are particularly striking. Between 2015 and 2021, the cost of subsidized purchase programs, such as “Price for Buyer” (Mechir LaMishtaken), amounted to about NIS 10.9 billion – mostly as revenue forgone by the state from land sales (Azankot, 2023). This is a one-time benefit for first-time winners, many of whom belonged to middle-to-upper income deciles, so the contribution to reducing affordability gaps was limited and even regressive (Bank of Israel, 2023c).

By contrast, encouraging long-term rental requires far fewer fiscal resources – mainly targeted tax exemptions or land discounts – yet it creates an ongoing stock of units that can serve changing tenants over time. Unlike purchase programs, which increase demand and intensify

pressure on prices, developing an institutional rental sector adds stable supply and contributes to housing security.

In Israel there are early signs of such activity (REITs and institutional initiatives), but their scope is limited and does not change the market's structure. Adopting similar principles – such as reduced taxation on rental income for companies that hold assets for at least 15 years and dedicated loans, adapted to local market conditions – may enable a gradual transition to a more institutional and stable rental market.

8. Conclusion

The picture that emerges from the data is that Israel's housing crisis stems both from an overall shortage of housing units and from structural mismatches in supply. Two phenomena stand out: a persistent shortage of small apartments in the face of growth in small households, and a rental market that relies almost entirely on private landlords and short-term contracts, despite the continual rise in the renter share. Although housing starts increased over the past decade, they did not catch up with the shift in the composition of demand, resulting in erosion of housing affordability – both for ownership and for renting.

The price-to-rent index illustrates the severity of the gap: in Israel, this ratio increased in 2007-2024 by a factor of 2.02 compared with 1.21 on average in the OECD – a figure that points to especially low returns from renting and a market that does not attract institutional players. The tax system likewise favors private landlords over institutional ones, through rent-tax exemptions. The result is a short-term, unstable rental market that cannot serve as a reliable alternative to homeownership.

In a country where about 87% of the population lives in cities, these mismatches become an urban problem and a structural constraint on growth. As emphasized by the OECD (2025c), urban-adapted housing is a condition for the functioning of education, employment, and family systems. In Israel, the lack of small apartments and of an institutional rental market undermines

the ability of the urban space to provide diverse and accessible solutions, thereby weakening the engines of human capital and growth.

The conclusion is clear: alongside expanding construction, institutional reforms are required. A mandatory, better-adapted unit mix, the development of long-term rental housing, and the modification of local and national incentives are prerequisites for improving affordability and for establishing housing as a basis for economic and social stability.

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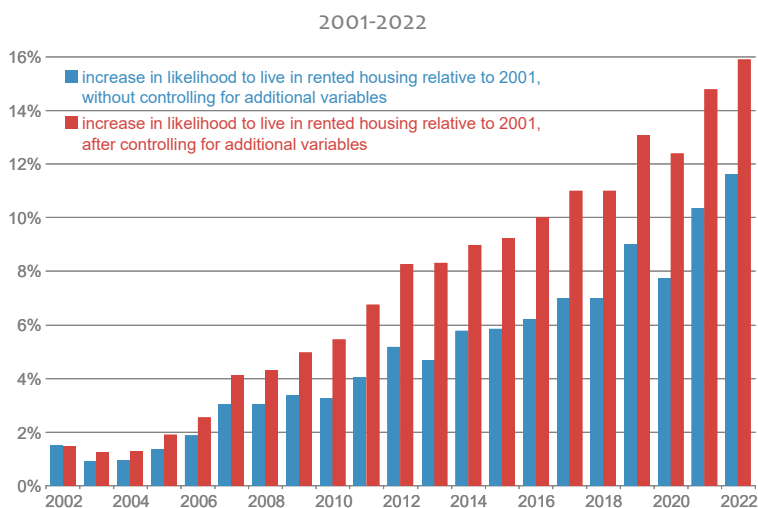
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Appendix: A multivariate analysis of the probability of living in rental housing

To better understand changes in residential patterns in Israel, a multivariate analysis using linear regressions was conducted to isolate the relationship between the probability of living in rental housing and each demographic variable, while controlling for other variables, over the years 2001-2022. The analysis isolates the contribution of the household head's age, household size, and income to the likelihood of living in rental housing. The results indicate a persistent increase in the probability of living in rental housing even after controlling for these variables, as well as sharp gaps across age groups and family composition. The analysis uses household expenditure survey data for 2001-2022 and includes 210,444 households living either in owner-occupied dwellings or renting from a private landlord.

Figures A.2 and A.3 show the change in the probability of living in rental housing by the household head's age and number of persons, relative to one-person households headed by someone aged 25-34 in 2001: the probability of living in rental housing declines with the household head's age (after controlling for the other variables), and single-person households have the highest probability of living in rental housing.

Figure A.1
Increase in likelihood to live in rented housing relative to likelihood in 2001*



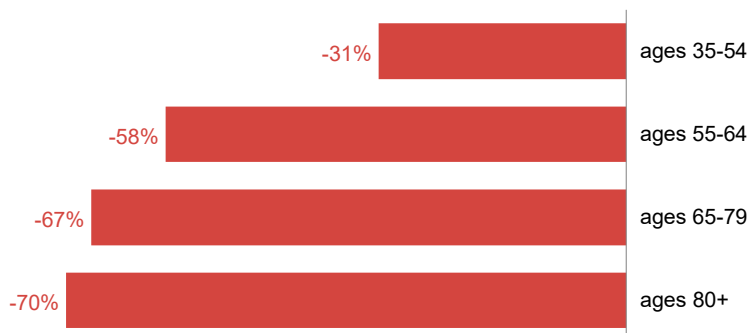
* These are results of a multivariate analysis, controlling for income, household size, and the age of the head of household, relative to a baseline of a single-person household aged 25-34 in 2001. Most coefficients are statistically significant at the 1% level, except for the coefficients for 2002-2004, which are statistically significant at the 10% level.

Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

Figure A.2

Change in likelihood to live in rented housing

by age of household head*



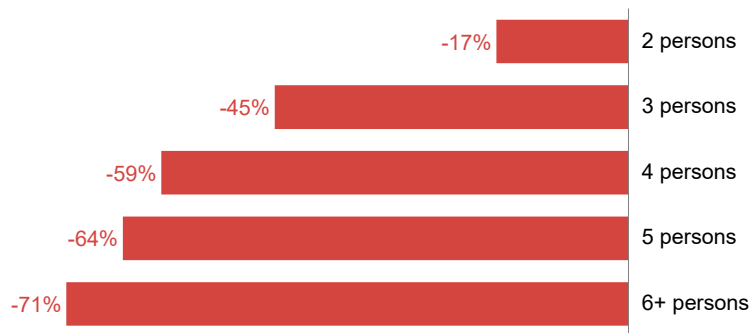
* These are results of a multivariate analysis, controlling for income, household size, and the age of the head of household, relative to a baseline consists of households in which the head of household is aged 25-34. All coefficients are statistically significant at the 1% level.

Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

Figure A.3

Change in likelihood to live in rented housing

by number of persons in household*



* These are results of a multivariate analysis, controlling for income, household size, and the age of the head of household, relative to a baseline of a single-person household. All coefficients are statistically significant at the 1% level.

Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics

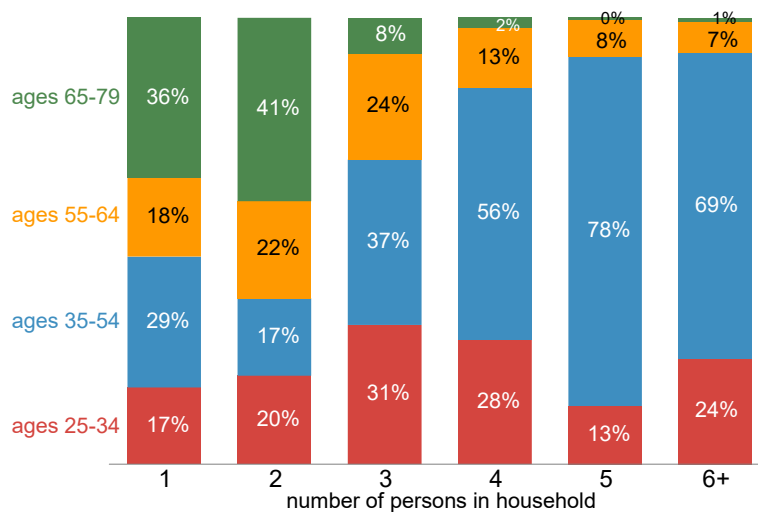
From Figure A.4, which presents the age distribution in 2021 by the number of persons in the household, it emerges that among two-person households there is a particularly high share of those aged 55 and over, who were less affected by rising prices (apparently because most were homeowners prior to the price increases), and the lowest share of young adults and working-age groups (24-54), who were significantly affected by the price increases.

The findings in this appendix reinforce the need for housing policy that is tailored to the changing composition of households: singles and young couples face sharper affordability difficulties, while older couples are less exposed to rising prices.

Figure A.4

Age distribution of household heads

by household size in 2001



Source: Yael Mishly, Shoresh Institution for Socioeconomic Research
Data: Central Bureau of Statistics