Making Housing Affordable

A new vision for housing policy

Alex Morton
Edited by Natalie Evans

Policy Exchange

Think Tank Publication of the Year 2010

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This publication was awarded Think Tank Publication of the Year 2010 by Prospect magazine

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Alex Morton was Secretary to the Conservative Party's Globalisation and Global Poverty Group Policy Group under the Rt Hon Peter Lilley MP. Following this he worked in the Civil Service Graduate Fast Stream at the Department of Health until he resigned at the end of 2009 to work on various potential public sector reforms. The proposals in this paper set out in detail one of three areas where public sector reform can dramatically reduce costs while improving social outcomes to save the government around £40 billion a year.

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Published by
Policy Exchange, Clutha House, 10 Storey's Gate, London SW1P 3AY
www.policyexchange.org.uk

ISBN: 978-1-906097-83-7

Printed by Heron, Dawson and Sawyer
Designed by SoapBox, www.soapboxcommunications.co.uk

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Acknowledgements

While the ideas in this paper are my own, thanks are owed to Tim Leunig and Professor John Hills for providing me with useful comments on this paper, and to various other people who read through and gave helpful advice on these ideas and issues.

Introduction

Making Housing Affordable outlines how to improve social outcomes (e.g. home-ownership and employment) and save £20 billion a year.

The report's basic analysis is that:
We face a housing crisis. Over the past few decades rents and house prices have risen much more rapidly in the UK than other countries, driving up government expenditure on Housing Benefit and social and affordable housing whilst driving down home-ownership. Other factors (e.g. lending) have played a part but the largest single cause is a crisis in supply. House building has more than halved in recent decades to rates that are consistently among the lowest in the developed world.

Social housing is failing its tenants. Current social housing policies are driving unaffordable levels of welfare reliance and increasing poverty for social tenants – evidenced by an 'unexplainable gap' between social tenants' much lower rates of employment when compared with similar individuals outside the sector. This is caused by the appalling incentives that social tenants face.

It proposes the following solutions:
Reduce the rate at which rents/house prices rise by increasing the numbers of new homes built. Since the evidence shows under-supply caused by the current planning system is behind rising prices it is necessary to create a 'community-controlled' planning system which moves to a more consensual model of planning, where those impacted by development (not local councils) decide on whether or not to allow developments. Financial incentives or amenities for allowing development should go directly to or directly benefit existing residents. This should substantially increase the numbers and quality of new homes built. This will in turn hold down rents, house prices, Housing Benefit, and the government's inflation measure, the CPI (should it in the future incorporate housing costs). Government action on this is essential though it should not preclude other measures.

Radically reshape the incentives social tenants face. The current 'needs-based' allocations for social housing should end and social housing should become a stepping stone into ownership for tenants who work, with the removal of the perverse incentives facing social tenants leading to a reduction in the 'unexplainable gap' in employment rates. Social tenants should be helped to own their own homes by renewing the Right to Buy and by making support between home-owners and renters more equal – so almost no social tenant pays more to own than to rent their property.

Create a new 'Path to Ownership' model of social housing and build more social homes. In the long run, if home-ownership is more affordable social housing demand will dwindle. But there is an urgent need now. The existing model of large upfront subsidy for social housing is unaffordable so a new affordable model is proposed that allows a large social house building programme immediately at almost no cost.

The reforms set out in this paper generate around £20 billion of savings a year every year beginning immediately and continuing into the future. These will come from:

- Reducing existing expenditure on social/affordable housing.
- Selling off existing stock on the open market (if expensive) or into the new Path to Ownership model (if not), while building more new social houses.
- Over time, saving money on Housing Benefits as rents rise more slowly.
- Over time, reduced welfare dependency for social tenants.

This paper does not recommend changing existing tenants' contracts or raising social rents faster than in recent years. It is an attempt to generate reforms that open up home-ownership to all those who work and want it, provide for those in need, and break out of our current housing crisis. It is the first of 3 reforms which together could save government £40 billion a year.

Executive Summary

Coalition leaders in the Third Prime Ministerial Debate[1]:

> Audience Member: "*I am married, my husband is an accountant and we have two children… we cannot afford our own family home, nor the larger deposit necessary these days. What will your party do to help families and others in terms of housing, because if a chartered accountant is priced out of the market, then what hope is there for anybody else?*"
>
> Nick Clegg: "*This is one of the things that, along with immigration, I probably hear about more than anything else as I travel around the country...*"
>
> David Cameron: "*Above all, we've also got to build more houses. I think there's no doubt in my mind that we've got to change the planning system right now.*"

The emergency budget has finally focused minds on cutting Britain's enormous deficit. The best way to reduce the deficit in both the short and long-term is to look for reasons government spending is being driven upward and change policy to reduce these pressures, rather than simply imposing cuts across the board.

Recent housing policies pushed up public expenditure and led to lower living standards. A severe shortage of the number of new homes in the private sector is causing ever higher house prices, longer social housing waiting lists, sharply rising rents and rising Housing Benefit costs. Social housing is currently exacerbating expensive problems of welfare dependency and poverty. Along with this pressure on expenditure, the numbers achieving the goal of the vast majority of people – home-ownership – is falling for the first time since modern records began in 1918.

Housing thus offers some of the greatest opportunities for changes in government policy. The new government should throw its support behind the goal of well over 80% of the population – home-ownership – and chart a bold new course that would also deliver over £100 billion worth of savings in the next five years. These savings are not achieved at the expense of long-term costs – savings continue at £15-20 billion a year into the future. These savings are also achieved while helping increase home-ownership and expand social housing supply. (For a full list of broad major costs and savings from these reforms see the summary of costs and benefits at the end of this Executive Summary.)

The reforms in this paper are a detailed exposition of one of three areas where public sector reform can dramatically reduce costs while improving social outcomes – in two further areas, (health and local government) there are a further £20 billion worth of savings a year to be made while improving social and economic outcomes.

1 All figures etc in the executive summary are from within the main document, (save these quotes which are from the BBC transcripts of the leaders' debates). Citations are attached to the figures within the main document. Unless otherwise shown, internet sources can be found in the Bibliography.

Part One: Where We Are

Housing costs are rising and this is pushing up government expenditure

- Between 1975 and 1995 average house prices in *real terms* (i.e. excluding inflation) rose 3.5%. Between 1995 and 2009 the average real terms house price rose by a historically unprecedented 120%, jumping from £72,659 to £160,000. In nominal terms, house prices have more than tripled since 1995.
- But even pre-1995 UK rises were still higher than many other countries where house prices rose on paper, but fell in real terms, leading to falling housing costs and rising living standards.
- House prices are currently more than five times average earnings across each region of the UK – and even more in expensive areas like London and the South East.
- Higher private housing costs have pushed up waiting lists for social housing. These fell slightly between 1980 and 1997 (as private housing costs rose slowly in this period), but rose rapidly from 1 million to over 1.7 million households between 1997 and 2009 (as housing costs shot up).
- Higher house prices have fed through to higher rents, as economic theory would predict (different types of housing being substitute goods). Despite the supply of rental properties rising 40%, average private rents rose 64% between 1996-7 and 2007-8 (the last year with official data). Social rents, linked to private ones, rose by 57%.
- Rising rents have caused the rising Housing Benefit bill politicians are concerned with. Housing Benefit rose by 64% from £12.2 billion in 1996/7 to £20 billion in 2009/10. The rate of increase in Housing Benefit clearly tracks rising rents.
- Proposed Housing Benefit reforms by government, while welcome in restricting excessive claims, only trim around 7% off Housing Benefit, including linking it with the CPI (a general inflationary measure), something that will be difficult to implement. Under current policy rents will rise faster than the CPI over the medium-term, putting further pressure on Housing Benefit.
- The idea that government can seriously 'push down' claimants' rents via cuts in Housing Benefit is largely false. Housing Benefit claimants made up 20-30% of private renters across the UK in the last decade – not enough to set market prices, even if it has some impact in some areas.
- The planned incorporation of housing costs into the CPI will push the CPI up. This new CPI measure incorporating housing costs will also mean the majority of the projected £6 billion of savings from linking benefits to the CPI rather than the RPI will not be realisable since most of the gap between the RPI and CPI in recent years existed as the CPI excludes housing costs and this will no longer be the case.
- The government's 'affordable housing' schemes only affect around 2.5% of all houses sold, and help 0.1% of households each year, while costing £700 million or so annually. This shows the inadequacy of current solutions.
- Rising housing costs meant that the British Attitudes Survey found that housing had the fourth highest number of people prioritising it as their first or second choice for additional government spending. For many people, getting a decent, affordable home is one of their top issues.

- But a £156 billion deficit means that the government will have to find ways to cut housing's cost to the Exchequer. Housing spending was cut sharply in the UK from 1979-1984 and in Canada in the 1990s. It is inevitable it will be sharply cut again to help reduce the deficit.
- Not only are new UK homes expensive, they are small compared with other developed countries, with 50% or so one or two bed flats. They are often poor quality, with one architectural body, CABE, finding just 20% were of a 'good' architectural standard.

Younger and low income households that were moving into ownership are now pushed out

- A range of surveys typically show that over 80% of households in the UK say they want to be owners. Studies in the UK and abroad show home-ownership raises satisfaction with a home, (more than can just be explained by income). People genuinely aspire to home-ownership.
- There is a consistent and erroneous belief that lower income households are all social tenants. But in fact in 2004-5 there were more owner-occupiers than any other group across income groups. Even in the bottom three income deciles, no more than 33% lived in social housing.
- Owner-occupiers in the bottom three deciles outnumbered social and private renters *combined* due to rising home-ownership in previous decades. This was despite annual government support for renters running at £35 billion a year, while support for owner-occupiers ran at less than £1 billion. However, due to rising prices younger and low income households are now being blocked from entering home-ownership.
- The average first time buyers' income doubled from 1997 to £40,000, rising much faster than earnings, (which rose by around 50%), as many younger and less affluent households could no longer obtain a mortgage and home of their own.
- While from 1953 to 1991 the rate of home-ownership rose from 32% to 68%, (around 9% a decade,) it only rose 3% to 71% from 1991 to 2001 and then fell from this to just 68% by 2008, the first major decline since 1918.
- Housing is the most severe area of a generational tension that David Willetts called 'the Pinch'. 90% of (typically younger) first time buyers in 2009 needed support from their family whilst the numbers of under-30s with a mortgage fell from 43% in 1997 to 29% in 2009. Just 35% of mortgages in the 2000-09 period went to first time buyers, down from 50% in the 1990s. The under-50s hold just £540 billion or just 18% of the £2.9 trillion in housing wealth in the UK.
- This trend of falling home-ownership is particularly worrying as the UK does not, as is often thought, have unusually high rates of ownership. It actually sits in the middle of the EU and other developed countries in terms of ownership rates.

The social housing sector is large, expensive and is failing its tenants

- The social housing sector had a substantial asset value of £400 billion in 2004.
- In 2008 it housed some 17% of UK households. The last EU study showed the UK's social housing sector was twice the size of the average social housing sector in the EU.

- The cost of subsidised rents and building/maintaining social homes is around £15 billion a year. Subsidising rents cost around £6.6 billion in 2004, (a figure unlikely to have risen significantly since), while constructing, maintaining and improving social properties cost around £8.6 billion in 2009. Just 3 out of 9 regions in the UK received £4.6 of the £6.6 billion rental subsidy.
- Each new social property built currently receives an upfront subsidy of around £60,000. Those who argue for cutting Housing Benefit by building new social homes ignore this cost.
- Studies show social tenants do worse in areas ranging from mental health to equality of opportunity, (one study called it one of the "*strongest and most consistent correlates of adult disadvantage*"). This is true even after adjusting for relevant factors in such studies, such as income, or parental attitudes to learning.
- Social housing appears to have a particularly negative impact on employment. While around 90% of those in private households are economically active in that they have someone in work, less than 50% of households with social tenancies do – a more than 40% gap.
- Adjusting for individual labour market disadvantages (e.g. single parent/disability status), studies show most of this gap (20-25%) still exists in employment rates between social tenants and similar individuals in private tenure.
- The majority of this 'unexplainable gap' is likely to be caused by strong and plausible incentive effects for social tenants – as discussed further below. Further evidence for this 'unexplainable gap' is that even as the economy boomed, social tenants who lost work were two and a half-times as likely to remain economically inactive as those outside the sector – despite a rising employment rate.
- The direct costs of this 'unexplainable gap' in employment can be conservatively estimated at some £7 billion a year due to around 550,000 extra households reliant on out-of-work benefits (assuming each household reliant on out-of-work benefits costs an average of around £13,000, a figure that is very cautious and excludes lost tax revenues).
- Home-ownership declining will exacerbate wealth inequality in the UK. Outright home-owners have twenty times the wealth of social tenants – largely due to their housing wealth.
- The total of all implicit and explicit costs around social housing (including welfare costs) is roughly £32 billion a year – £15 billion in building, maintaining and subsidising social tenants' rents, £10 billion in Housing Benefit, and at least £7 billion in welfare payments due to the 'unexplainable gap' in employment rates for social and private tenants.
- Ending security of tenure in social housing is a mistake. Firstly, the appalling incentives social tenants face are the root of most of their problems (see below). Ending security of tenure for new tenants in effect means social tenants who improve their circumstances may lose their home, an enormous disincentive. Secondly, any such reform will take a long time to have an effect (and when it does will only be marginal) as it will only apply to the small number of new tenants coming into the system and being reassessed at some point in the future.

- The idea that people can 'pass on' council homes is true in a limited number of cases (allowed for spouses, cohabiting partner and to a relative living with them already if they die). It would clearly be unfair to change these rules (e.g. start evicting elderly spouses).

Certain truths about social housing need to be set out

Social housing waiting lists correlate first and foremost with private housing costs

- Waiting lists primarily link to demand and house prices not supply (i.e. stock levels). Waiting lists fell between 1981 and 1997 but rose steeply between 1997 and 2009, despite the supply of properties declining more slowly in this later period (after accounting for new builds and Right to Buy).
- Post 1997 many who did not want social housing will have been forced onto the social housing waiting lists as they simply could not afford private housing costs, while between 1981-1997 lower house prices meant private housing was affordable, keeping the waiting lists down.
- Between 1997 and 2009 the numbers who left social housing to enter private housing (excluding Right to Buy) fell by *more* than the rise in waiting lists. This declining number of what are called 'private re-lets' entirely explains recent rises in waiting lists and in turn is entirely explainable by rising private housing costs.
- Waiting lists also fell slightly during the recession from 2008 to 2009, as this period also saw very substantial falls in house prices. Any increase due to rising unemployment was more than balanced by households leaving the waiting list as they hoped to move into private ownership, which was becoming cheaper.
- Thus those who blame Right to Buy ignore that the rise in waiting lists links primarily to changes in private housing costs *not* changes in council stock.

Social tenants want to be owner-occupiers

- Across a variety of polls around half of social tenants unreservedly express a preference for home-ownership rather than a social tenancy.
- The vast majority of the remainder cited feared problems with ownership rather than a positive preference for social housing, (e.g. many cited worries over the cost of repairs).
- Those who actively want to stay social tenants are a small and largely elderly minority.

Social housing is not failing due to its size, location, lack of mixed communities etc.

- Various common arguments for why social housing is failing have little evidence behind them.
- The social housing sector is not 'residual' or too small. As the UK has an internationally large social housing sector, if size is to blame for its poor outcomes it must be too big not too small.
- Mixed communities have anecdotal success but academic surveys show their current success in improving social tenants' outcomes is negligible.
- Finally, in terms of social tenants being in the wrong place, Inner London boroughs like Tower Hamlets and Hackney have large numbers of social tenants located in an area of huge employment opportunity, yet still have on average the worst social and economic outcomes in the country.

- Despite the average being pulled up by a large upper-middle class in these areas (all these regions have well above the average numbers educated to degree level or above), deprivation at the bottom of these areas is so intense it drags the average down to make these areas the most deprived parts of the UK – for example, they contain both the lowest employment rates and the highest numbers of children in workless households.
- A further solution sometimes mooted, that of relying on housing associations, will fail – social tenants' low employment rates are similar regardless of whether they are housed by housing associations or local authorities.

The real reason social housing fails is because of the incentives it creates

- The 1977 Housing Act requires all councils to prioritise allocation of social housing to households in most difficulty – often called a 'needs-based' system of allocation. The greater a tenant's 'need', largely linked to economic inactivity/welfare dependency, the higher a tenant is placed on the waiting list. This means over half of all new social tenants are economically inactive working age households reliant on benefits.
- The 'transfer applicant' system used to allow social tenants to move within the social housing sector to a new social property is also 'needs-based'. Each year around 2% of tenants are successful 'transfer applicants', meaning over the long-term most households use the transfer system (and almost all will understand how it works).
- The allocation system creates a sharp poverty trap. Both those on the waiting list for a social property and existing tenants wanting to move to another social property are penalised for becoming less dependent on the state. This problem is exacerbated as many people find it easier to move onto benefits (which may help them get the home they need) than off them (once they have it).
- Social tenants' incentives around maintaining, improving or worsening their housing situation through employment or economic inactivity are also non-existent. Tenants cannot hope to own their home or even move out to the private rented sector at present due to current sky-high prices. But they also cannot lose their home by remaining unemployed or on benefit, unlike owner-occupiers or the majority who rent.
- It is these two major incentives around housing that explain most of the 'unexplainable' gap between social tenants and those outside the social housing sector.
- This incentives based hypothesis would predict the larger the gap between the private sector and social housing costs, the greater the poverty and employment effects social housing causes, as it is where the (dis)incentive effects of social housing are strongest.
- The appalling outcomes which propel Inner London areas like Tower Hamlets or Hackney to be at or near the top of deprivation indicators confirm this. Excluding the highly educated and affluent professionals in these areas, for many welfare dependence in these areas is generally the best way to obtain a long-term decent home – as home-ownership is out of reach and the private sector costly and unstable.
- Without changing these incentives, social housing will continually act to stop inactive tenants returning to work – essential to generate savings and reduce the welfare budget.

- Most people polled support changing a perceived unfair social housing allocation system from the current needs-based system so that low income earners can obtain social housing. The more people know about the system and the lower their income, the more they agree with reform – with those on lower incomes or who understand the current system the best being its strongest opponents.

Some truths about private housing and home-ownership need to be set out

UK house prices rose further and for longer and have fallen less than in other nations

- While there has been a global problem of excess liquidity the UK's problems are deeper. Between 1995 and 2006 UK real terms house prices rose by 133%, the second highest among developed nations and since 2007 UK house prices have also fallen much less than other nations. Yet its mortgage debt rose only slightly more than the average during the boom.
- As a comparison, in the US, house prices doubled in nominal terms and have since fallen 30%, while in the UK nominal house prices tripled and have declined by around 10%. Even a 10-20% fall over the next few years would not bring with it housing affordability, long-term changes are needed. Real term UK house prices also rose at over twice the European average between 1971 and 2001, showing that the problem is not simply down to a recent liquidity bubble, even if such a bubble exacerbated the problem. House prices will not naturally deflate and politicians must change policies to resolve the housing crisis.

'Excessive' mortgage lending is not behind rising house prices in the UK

- As home-ownership is falling it is becoming harder to get a mortgage for a family home, not, as is often thought, easier. High house prices cause bigger loans to each household buying a new home, not vice versa. Moreover rising prices are driven by existing owners, as of those granted mortgages only 35% are now first time buyers – down from 50% in the 1990s.
- As noted above, global liquidity issues alone cannot explain the UK's long-term higher house prices and why house prices have risen more steeply than in other countries.

Immigration and demographic change are not the key factors in current housing problems

- Immigration is a real but limited factor in housing. The House of Lords investigated this issue and concluded recent immigration had only raised house prices by around 7%. Lower net migration will help but nowhere near resolve the UK's housing crisis.
- Only 7% of social housing goes to non-UK nationals – they are not 'taking over' the social housing system. It is largely established migrant communities in social housing.
- The decline in the average UK household size is slowing, while the UK's rate of population growth (excluding net immigration) is steady. Internal demographic factors are even less of a factor than immigration in driving the UK's housing problems.

The UK is not heavily over-developed and has options about its housing

- Only 10% of England, the most populated nation in the UK, is developed. 87% or so is green space. The UK has a clear choice of ever smaller and more expensive homes, or allowing slightly more development to take place over time. It should stop focusing on the amount of development and worry more about the *quality* of development.

Making new developments contain more low-cost or affordable homes does not lower prices

- It is *net* supply not the *type* of supply that matters. This is reflected in government housing data which clearly shows different parts of the housing market move together as one over time – they interrelate. Interactions between different parts of the housing market mean supplying cheap or expensive homes has the same overall effect on prices.

The real reason the private housing sector is in difficulty is that there are too few new homes

- The last decade saw just 160,000 new homes being built a year – around 45% of the 360,000 new homes built a year in the 1960s. Each decade since the 1960s has seen fewer new homes built. New UK homes are small with around 50% being flats, making the shortage in supply even greater.
- This annual reduction in new homes since the 1960s is around 80% of the entire stock of second homes held in the UK, and around half of the long-term empty homes in the UK.
- The UK has been near the bottom of the EU15 in terms of new homes per person since the 1980s, indicating that under-supply has been an issue for decades now.
- This fits with Kate Barker's work which pointed out the UK's house price rises have been higher than the international average over the last few decades – this problem goes back decades.
- There is a need for new family sized homes for those in their 20s and 30s. There is now a generation of (mostly older) home-owners now living longer in large empty homes. 7.8 million, or roughly 35% of UK households are now 'under-occupiers', living in homes with at least two spare bedrooms. Under-occupiers are overwhelmingly home-owners, (e.g. 47% of owner-occupiers are under-occupiers versus 11% of social tenants, in a much smaller sector).
- Government studies have shown the current lack of new homes is pushing up prices. The Department for Communities and Local Government's (DCLG) own research shows every reduction of 100,000 new homes per year would raise prices by 12-14% each and every decade. Kate Barker's work showed the number of new completions changing by 240,000 would raise/lower house price rises by 2.4% a year.
- Thus if supply had run at 1960s levels since 1980, around 175,000 extra dwellings would have been built a year, and real terms house prices would have risen much less than they did – from £75-80,000 to just £105-110,000. This would have brought the UK more in line with other countries – where they did build more homes.
- The UK's housing crisis and its consequences are entirely predictable as a consistent reduction in the supply of new homes will obviously have an impact on the UK's housing market.

This lack of new homes is caused by the UK's planning system

- Since the high cost of housing has such a high cost to individuals and society, we need to examine what is causing the lack of supply that the UK suffers from.

- The main reason we are building so few new homes is that not enough land is being released for home building. This is reflected in the fact that land with residential planning permission costs an astounding £1.87 million per hectare while land designated as agricultural has an average price of less than £20,000 per hectare. This means land costs around £45,000 per new dwelling – even at current very high densities.
- The price of land with planning permission is rising even faster than house prices, because the release of land for new homes is getting rarer and rarer. Previous Policy Exchange works (e.g. *Unaffordable Housing*) and Kate Barker's work also explores this point.
- Councils have been putting the brakes on new housing developments since at least the 1980s, but the problem got even worse in the last decade, largely due to bad government policies.

Recent policy and costly land created bad housing and increased opposition to new homes

- The previous government argued that making a higher proportion of new homes low-cost, affordable, high density and so on will help affordability levels. But this is based on a flawed argument around the type of housing built rather than levels of supply, as discussed earlier.
- On top of this, high land prices pushed new homes toward being poor quality as the value of the property was derived from the value of the land it sat on, (not aesthetics or design features), whilst developers know that at current prices even poor quality homes will sell at a profit.
- Thus, government policy and high land prices have meant in recent years that new developments were likely to be cheap, often flats and often poor quality.
- Polling evidence shows that local opposition is strongest to such developments and so this made development more unpopular than ever, reducing the net supply of new homes.
- People in the UK want to live in and near high quality homes with gardens, not in cramped and cheap houses and flats. 20% would oppose new homes in their area – 60% would oppose new flats. Bungalows, village homes, Victorian terraces and Modern semis are all popular homes – whereas only 2% want a flat of any kind and 0% say they would like to live in a high rise.
- Thus recent policies toward cheap and often affordable homes (and even more, flats) were strengthening opposition to development not weakening it.
- Because councils retained the powers to rule on most development proposals (except for a small minority where central government imposed new homes) over time rising opposition to development meant a reduction in housing supply and even higher house prices.
- The Council for the Protection of Rural England and DCLG have found that good quality developments can increase house prices in an area by making it more desireable
- What is needed are more better quality developments that both increase housing supply and raise house prices and the quality of life for existing residents in the areas that they are built.

Localism that does not strengthen NIMBYs and involves the community is needed

- Opposition to development *per se* is not as high as many believe. Polls show 72% agree the UK needs more homes, 55% actively support new homes in their village/suburb/town. Even in the South East, where opposition to new homes is strongest, only 30% say they generally oppose new homes in their area.
- Over 70% of people support new homes nearby if they are in keeping with the local area and if they do not lead to worse services for existing residents.
- People do however want to be involved in what new housing near them looks like – 82% believe that local people should be involved when new homes are built near them.
- Despite levels of opposition to development that are lower than often thought, simply removing recent bad policies will not change the UK's under-supply of homes. The council based planning system itself acts as a block on development. In the 80s and 90s then councils allowed more homes than at present but still nowhere near enough, and internationally speaking, allowed very few new homes.
- It is likely that the reason that councils oppose new homes more than most people do is that local government elections work to strengthen a small and determined NIMBY minority. Due to council election turnouts of around 30-35% in which local issues are often secondary to national matters, councils have strong incentives to listen to a very small but vocal NIMBY minority rather than the majority who are more relaxed about development, as these NIMBY voters are more likely to turn out and vote against councils that allow new homes.
- The current reaction to the new government's scrapping of house building targets supports this thesis, with almost all councils promising 'no new homes' in their area – something that should be ringing very loud alarm bells in government.
- True localism would by-pass NIMBYs and take more account of the majority view in most areas – which is supportive of development if concerns around the quality of new developments and local services are tackled. This would allow greater numbers of new quality homes onto the market over time, leading to more stable house prices.

Part Two: Solutions

The first point is that any proposed solutions must raise substantial sums for the Exchequer given the current financial climate. The net revenue brought in by the proposed reforms outlined below is around £20 billion a year for the next five years – over £100 billion in total. It brings in this money whilst actually stimulating employment and economic activity.

Just as importantly, these reforms set out a long-term direction for how the UK can both improve its housing situation and reduce spending. They substantially expand home-ownership, reduce social tenants' welfare dependency, and cut Housing Benefit costs. They allow a short-term rise in the numbers obtaining social housing while setting a path that should see social housing demand fall heavily over time. The reforms continue to save the Exchequer around £20 billion per year into the future, setting a permanent course for lower spending. To put this in context, this amount is more than would be saved from abolishing the Home Office and Ministry of Justice. It is a substantial prize for government and achieved while also improving social outcomes.

The government needs to turn social housing into a route into home-ownership

Changing housing allocation systems and taking control of the housing stock

- Social housing allocation and transfer application schemes must be changed so that the perverse incentives currently built into these schemes by the 1977 Housing Act are removed. This is the only way that social housing will stop operating as a limit on its tenants' aspirations.
- The government should replace the statutory requirements to allocate social housing to those in the greatest need with a requirement to give it firstly to those who are severely disabled, but then subsequently to those who wait longest or have the greatest local connections to an area. Similar changes must be made to the rules for 'transfer applicants' where tenants move within the system.
- Polls show that most individuals support changing the allocation system in this way (especially low income individuals). This change must however go hand-in-hand with reform to help vulnerable households in need of temporary support.
- To support vulnerable households whilst allowing a change in allocation systems, vulnerable tenants, (e.g. those with children), renting privately and relying on Housing Benefit should be given medium-term (e.g. three year) tenancies. In return a substantial one-off payment (e.g. £4,000) would be made to their landlords. This is substantially cheaper than providing a subsidised home for life while giving these households the immediate stability they need.
- Local authorities and housing associations created post 1997 would see their stock and debt moved into central government's hands, though they should continue to run the stock's day to day management. This is so that government can push forward with plans to offer home-ownership to these tenants directly. Housing associations as a group have failed to improve the outcomes for their tenants and cannot be relied upon to be the change that tenants need.
- Housing association debts, (estimated at around £41 billion) would be paid off with the rents from existing tenants (housing associations receive £5 billion in Housing Benefit alone). Therefore no gains from these rents are presumed to flow to the government.

A new Path to Ownership model for future tenants

- This model allows a huge expansion of social homes being built at no extra cost to the government – a boost to the economy when it most needs such support.
- In the current financial climate the government needs to move from an unaffordable model of social housing that requires heavy upfront investment – £60,000 or so per home.

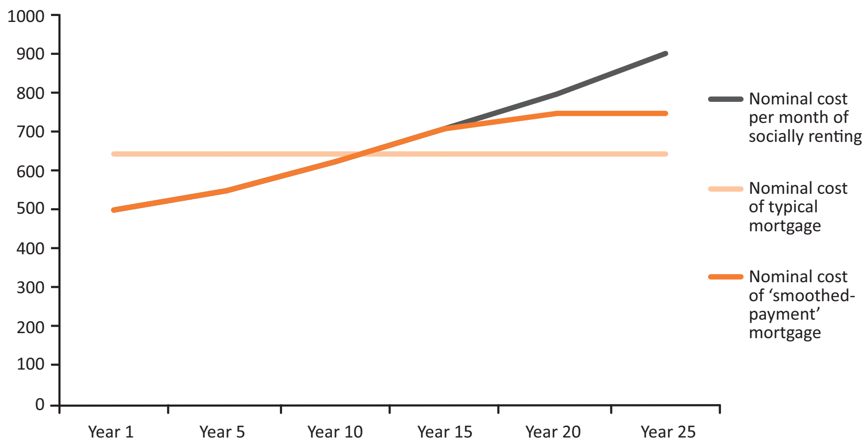
- The new Path to Ownership model removes this upfront cost. When local government builds social homes, central government issues short-term bonds to cover construction costs with the bonds refinanced on a rolling basis. This issuing of bonds is already done by some housing associations but government bonds would have much lower interest rates and fewer administration costs.
- The initial social rent on a property would cover the payment of interest on these bonds. Social rents would be held down as the interest on these bonds would be at government interest rates (usually 4% or so), and because councils could simply buy cheap land and build on it, (subject to the new planning regime discussed further down). Rents would be affordable – for instance, rents on a property in the North East costing £75,000 to build would be the same as the average current social rent.
- For Path to Ownership properties, the government would no longer gain rent from social tenants, (around £1,250 per tenancy per year net of maintenance costs). But more importantly, this scheme would remove the large upfront cost of building new social homes at a time when money is tight.
- Social rents should continue to rise at the same rate as they have done in recent years from this initial base (3.5% or so). Rising rents would both cover interest payments and generate a surplus payment over and above these interest payments. Where the tenant pays their own rent, this surplus payment should be used to pay off the principal debt owed against the property.
- Housing Benefit would cover the interest on bonds but not repayment of the principal debt. This would then create a strong incentive for social tenants to pay their rent as every rental payment made moves them automatically toward ownership. Government should consult on how to handle tenants who partially pay the rent but see this supplemented by Housing Benefit.
- As discussed later, measures to increase the supply of new homes should lower the rate of rent increases, meaning that when combined with this steady 3.5% rise in social rents for both existing and Path to Ownership models, private and social rents would converge – but crucially this would be done through holding down private rents rather than accelerating social rent rises.
- Tenants could pass on the amount they had paid off the principal debt on their home to relatives when they died, allowing them to build up wealth to pass to their family.
- If tenants' wages rise or their circumstances improve, they could chose to obtain a typical mortgage at any point, paying off the principal debt with this loan outright.
- Government would cover tenants' maintenance costs within the Path to Ownership model. Accordingly it should budget £2,000 a year for each tenancy. Once the tenant reached a stage where the share of the principal debt paid off was over 50%, this support would be proportionately scaled back as tenants moved toward 100% ownership.
- Using this new model, government should aim to build some 100,000 new social homes a year. As existing stock is vacated due to the deaths of tenants, most stock should also move into the Path to Ownership scheme, being sold off and repurchased using funds raised by issuing bonds (the same way new social housing will be funded).

- Eventually the aim should be to cover around 2 million households in this scheme, (around 10% of the households in the UK) giving costs to government of £4 billion a year to support the maintenance costs of these households.
- There should be a regional cap on the value of social properties built under this scheme, (e.g. set for the West Midlands, London) based on roughly the average or lower quartile property price in that region. Expensive social homes that are valued above this cap should also be sold off on the open market as and when they are vacated by tenants. (This may total around 32,000 properties a year – and is politically feasible due to the large scale social housing programme set out in this paper).
- This cap is necessary to allow social tenants to buy their home, to ensure interest payments on the bonds to cover construction costs are not too high, and to ensure taxpayers who cannot themselves live in these expensive areas do not resent paying for others to do so.
- In the case of London this will require a new London-wide allocation system, as some boroughs are unlikely to be able to build or retain social housing within their boundaries. Some other parts of the UK may also need councils to work together to house social tenants.
- This will not create 'ghettos' – it merely does not allow for new expensive social tenancies. The Right to Move and Right to Move and Buy set out below and creation of new social housing mean that overall these reforms are likely to reduce ghettoisation and spread tenants across areas, which coupled with changing incentives, may improve social outcomes.

Right to Buy renewed, a Right to Buy and Move, and a Right to Move for current tenants

- Firstly, raise the Right to Buy discount to more realistic levels across the UK, reversing its decline in value of recent years – (e.g. it is capped in almost all London boroughs at just £16,000 despite the phenomenal house price rises seen in recent years). This is why in recent years Right to Buy sales have declined massively to just 10,500 or so a year.
- A realistic discount (e.g. 33% in most areas) would mean tenants in some areas could purchase their home at no extra cost to staying renters. Once realistic discounts are in place then in only three parts of the UK would moving to home-ownership incur a substantially higher cost than paying social rents (in the East, South East and London).
- To further help tenants, particularly in the more expensive areas, government owned banks should create new Right to Buy 'smoothed-payment' mortgages. These would see mortgage repayments pegged to social rents, starting lower but rising with them over time, rather than traditional mortgages where housing costs rise sharply at the beginning and remain stable thereafter. These would not weaken the banks' balance sheets as they commit the same asset as security and have higher repayments (albeit over a longer timeframe) than normal mortgages. Figure 1 shows how this alters the way that repayments operate so as to prevent housing costs shooting up as a household moves into home-ownership.
- Banks would retain normal checks on tenants offered these mortgages, the only change would be on how repayment is structured.

Figure 1: Housing costs over time under three different options



- Combined with new bigger discounts this would mean almost no social tenant would pay more on a weekly or monthly basis to own their home than if they continued to rent.
- Tenants should also gain a Right to Move and Buy. This would allow tenants to transfer their existing discount to purchase another property should they wish to move into home-ownership in a property other than their current one.
- This will be particularly helpful for those in high value properties who will be able to move into ownership in another property even if they can't afford their current home.
- Further, as part of these reforms to the Right to Move, a previous Policy Exchange proposal that allows tenants to exchange their property for one of equivalent value elsewhere could be implemented, improving tenants' welfare without the possible negatives (costs and increasing waiting list numbers) as these are tackled by other changes outlined in this paper.
- Allowing greater mobility increases the numbers of tenants buying their property. Obviously if a tenant picks a new home they like, they are more likely to want to own it.

Gains in terms of asset sales from existing social housing stock

- As set out before, as existing tenants die, current social housing stock would be sold off and either repurchased and put onto the Path to Ownership model, or if valued above the regional maximum allowed for social properties, be sold off on the open market.
- Around 2% of social stock (roughly 80,000 properties) is released each year due to the deaths of tenants. Around 32,000 more expensive homes a year may exit the sector, but due to the earlier goal of an extra 100,000 new social homes being built a year, this should not be a problem.
- The levels of stock transferred under the new Right to Buy and Right to Move and Buy should be substantial as tenants can move into ownership without seeing any increase in housing costs, and there will also be a package of measures to support low income owners (see further below).

- In the first ten years around 146,000 homes per year are assumed to be bought by tenants, (with more in the early part of this period than the later part of this period). This is not that much higher than the first decade of Right to Buy sales (106,000 or so a year) despite the ease with which working tenants will be able to buy and the support available.
- Every 1% of stock transferred without a discount raises £4 billion, while every 1% of stock transferred with the tenants having a discount would raise £2.64 billion.
- £8 billion a year would be raised from stock sales from when tenants die. A further £15 billion in the first year and £10 billion in the next four years is projected from sales to existing tenants (after subtracting discounts). Even if sales to tenants are slower than this they would still make a very substantial contribution to reducing the deficit over the next five years. Current sales receipts from Right to Buy are likely to be around just £1 billion a year without these changes.
- Within a couple of decades these sales would transfer around 84% of the existing stock out of the current system, either to those who currently rent it, into the Path to Ownership model, or, in the case of a small number of expensive properties, out of the system entirely. Despite this transfer, with stable house prices due to other policy changes and the Path to Ownership model allowing a substantial increase in the number of new social homes, waiting lists should shrink substantially in this period.

How these measures are likely to raise social tenants' employment rates

- Fundamentally reshaping the incentives that social tenants face through changing the allocation system and helping them own their home at no extra cost should raise social tenants' employment rate from its current and appallingly low rate of less than 50% to perhaps 70% or so over a decade, eliminating most of the 'unexplainable gap' between social tenants and other households. This 70% would still leave social tenants' employment rates substantially below other tenures' nearly 90% rate.
- A 20% rise in the numbers of social housing households with employment over a ten year period means 550,000 fewer workless social households by 2020. Each extra 55,000 households moving into employment each year saves an extra £700 million, so by 2020 this saves £7 billion in welfare costs every year.
- In addition, these reforms should ensure that wider welfare-to-work reforms are a success, allowing at least another 300,000 or so social households see at least one member return to work. No savings are envisaged from the success of wider welfare reforms when we assess the costs/benefits of this paper, but without this or similar social housing reform, wider welfare-to-work success for social tenants is likely to remain elusive.

Demolishing the worst estates (where no one will want to buy)

- To demonstrate social cohesion and progressive values, the government should earmark £2 billion a year towards a scheme that demolishes the worst estates and rehouses those living there, (estates and new homes selected by tenants themselves, rather than chosen by central government, though only more deprived estates should be eligible). The aim should be to demolish and replace the worst 5-10% of estates over the next ten years as part of these reforms while this land, with development rights, should then be auctioned off to developers.

The government must also provide more support to low income owner-occupiers

- Of the 50% or so of social tenants wanting to stay in social housing, this was usually due to fears about ownership, not a positive feeling towards remaining social tenants. This is exacerbated by the way government support is heavily tilted toward support for renters, with billions spent on schemes supporting renters whereas almost nothing is spent supporting home-owners (despite the fact that low income home-owners outnumber low income renters).
- Reform therefore would not 'privilege' home-ownership but reflect a more 'tenure-neutral' system of support.
- Interest free loans should be offered to unemployed home-owners needing short-term support for mortgage payments. This is vital given that in any one year around one in six low income households sees a large fluctuation in income. These loans should be easy to claim and cover both mortgage interest and repayments, expanding and simplifying existing schemes.
- Government should help low income borrowers with good credit/rent paying history by providing zero interest loans for deposits and with government only requiring a 70% repayment of the money lent over a ten year period. Similarly generous loans for repairs and renovations would help reduce one of the main barriers that social tenants often identify to moving into home-ownership.
- With lending capped at £15,000 for deposits or repairs, these schemes would initially cost £3.2 billion a year to help at least 100,000 households, falling to £2.1 billion a year over time.
- Finally, low income households should be offered new, 'smoothed-payment' mortgages, just as social tenants should be. These would see repayments start off lower, and rise gradually over time rather than a one-off rise right at the start. This would not cost the government or banks any extra, just change the way that the mortgage was paid off.
- Such mortgages would be targeted on low income households with good credit history and would have to ensure the loan-to-value ratio declined each year, even if it fell slightly more slowly than under traditional mortgages.

A central goal of government should be home-ownership affordable to all who want it

- The underpinning of government housing policy should be the long-term and flagship housing target that by 2030 a person working full time on the minimum wage should be able to afford an average UK lower quartile property. This will allow all households that want to achieve home-ownership to do so, heavily cutting demand for social housing schemes.
- A secondary goal is rough annual house price stability over the coming two decades. This will ensure that this longer term target is hit.
- Responsibility for these goals would rest with the Housing Minister, who should write an annual open letter to the Prime Minister to explain the steps they are taking to ensure price stability and progress toward the 2030 goal.
- To defuse sensitive issues, this letter should also contain a clear assessment of how immigration will affect UK housing demand and how the government felt monetary policy was impacting on asset prices (including house prices).
- The coalition government has announced that the CPI, (the government's main inflation measure) will in future include housing costs. Thus the

recommendations above fit with the new government's determination to not allow another housing bubble to emerge.

- Hitting this target will also ensure lower rents – it will keep housing costs low for all private households. As is explored later, this will reduce pressure on government spending.

More homes through real localism – 'community-controlled' planning and direct democracy

- The government should scrap all density and affordable housing targets and aspirations. This is likely to lead to both more homes in general and more high quality developments. This allows everyone in the UK to 'trade-up' to better housing as each household moving to a nicer home vacates their existing one. Areas can allow cheap homes if they wish – but this decision should be entirely down to local residents and government should not pressure them into doing so.
- By making new homes fit with what existing residents in an area want, rather than what government dictates, this removes one barrier to expanding the numbers of new homes.
- Planned changes to ensure councils receive extra funding for new homes via matched Council Tax receipts are welcome. But government also needs to urgently review how often the figures that determine funding levels for many services are produced and see if this needs changing, and investigate this and other ways to measure population shifts (e.g. through monitoring households moving into and out of an area).
- The new government also needs to go further in a radical decentralisation of planning. For reasons explored earlier, decentralising planning to councils under the current system is very likely to strengthen the powers of a vocal NIMBY minority and restrain the limited numbers of homes being built. Planned changes are simply not big enough.
- Any continuation of the near-anaemic number of new homes being built would increase house prices and so reduce home-ownership, raise rents, push up Housing Benefits, raise the (new) CPI and so other benefits and push up social housing waiting lists even more.
- The government should instigate a radical shift and move to a system of 'community-controlled' planning. This would mean those home-owners 'directly impacted' by a housing development being balloted over any development proposal registered with the local council, and the development proceeding unless 50% of those balloted reject it.
- By development this means either the construction of new homes, changing buildings or the designated purpose of land or buildings – anything that impacts on the UK's housing stock.
- Unless 50%+ of those residents 'directly impacted' by a proposed development vote against it, the development would automatically be approved. The costs of administering this would be small – for every 1,000 households balloted, this should only cost around £1,000-£2,000, and this could easily be paid for by developers.
- What exactly 'directly impacted' should mean should be consulted on and set out in government guidance, but proximity, size of development and visual impact are likely to be key.

- Developers should be free to offer financial incentives to households being balloted over any planned development to ensure that their proposals went through. The aim should be that some of the increase in land values from granting planning permission should return to the community.
- Offers could be generous as the value of an average hectare of land rises from £20,000 to £1.87 million when planning designation goes from farming to residential. Though this gap would fall as more land was released, even if it fell by half this would still allow for serious incentives.
- Developers should also be free to offer amenities as an inducement to local residents in return for allowing development – e.g. paying for a new playing field for a school, or park, in return for allowing the building of new homes or redevelopment of an old industrial estate.
- Finally, to increase the supply of housing stock still further, VAT on renovations and extensions should be reduced. Each extension increases the total supply of housing space in the UK. Often it means a family remain in their expanded home rather than upgrading to a bigger house, leaving that bigger house free for another family.

This new planning system should result in better quality homes

- With this system developers would have to take on board local concerns about the quality of new homes seriously – they would have to propose homes that local people approve of.
- This means that development should become more of a 'win-win'. New homes can actually raise existing households' house prices and create a better quality of life for those who live near them, as studies of large high-quality developments in areas like Poundbury in Dorset or the Docklands have shown.
- For those who worry this new system will lead to too high population density and so an unliveable UK – Surrey has one of the highest 'shire' densities in the UK, while Kensington and Chelsea has the highest density in the UK, and both are seen as pretty desirable. But high density would be high quality.
- This system would also encourage brownfield developments, where almost no one is 'directly impacted' and where homes are likely to improve the feel of an area, so that development permission would be easier to obtain. On brownfield sites where no one was 'directly impacted' and no ballot was necessary then councils could halt development if they could publicly justify 'exceptional' reasons why development should not be allowed, but development on brownfield sites should overall become very much easier and simpler to obtain.

Safeguards to ensure areas are not overdeveloped and urbanised

- Areas of Outstanding Natural Beauty and National Parks should see their current stricter planning rules remain in place to retain their existing (low) population densities.
- To prevent development occurring in less populated areas such as woodland or meadows, (where no one lives close-by but which are valued by locals and should remain unspoilt,) each local authority should be able to designate up to 75% of its existing undeveloped land as 'off-limits' to developers. This would still allow for a huge increase in the numbers of new homes and well over a doubling of the land currently developed in the UK whilst protecting the character of rural areas.

- Large high-rise flats should also have different rules in place, potentially with councils being involved, as they often generate a visual impact for miles around.

How will councils build new social homes under this planning system?

- If councils want to build social homes, they could grant themselves planning permission as long as they won the support of those 'directly impacted' – with the funding for these new homes coming from central government issuing bonds – as set out earlier.
- Councils could allow mixed private/social developments and use some of the funding raised to financially incentivise the building of new homes. However, they would no longer be able to force developers to include social housing within their developments.

Increasing the numbers of new homes will hold down rents, Housing Benefit and the CPI

- Just as the low supply of new homes has fed through to increase rents and Housing Benefits in recent years, building more new homes would not just make home-ownership affordable, it would also hold down rents and Housing Benefits, as well as the CPI and so other benefits.
- Stable private rents would increase living standards for the 14% of the population that currently rent at a time when many people will inevitably feel worse off.
- But more stable private rents will also save substantial sums for government. If private rents rise at 1% a year rather than rising at their recent historic rate (around 5% a year), this would save £4.7 billion in Housing Benefits a year within ten years. (This saving is on top of £1 billion worth of government savings from feasible reforms that are already announced.)
- Government plans to link rises in Housing Benefit to the CPI instead of rents will simply push housing costs onto those on low incomes if rents continue to rise at their recent rates. Rising housing costs are the main reason for spiralling Housing Benefit and thus it is only lower housing costs that can cut Housing Benefit.
- The government also intends to save £6 billion worth of savings from linking benefits to the CPI not the RPI while also incorporating housing costs into the CPI. These savings rely on a CPI of 2% a year. Yet the main difference between the RPI and CPI is that the RPI includes housing costs. Given the RPI rose at 3% or above in five of the past ten years, the new CPI will not fall to 2% if housing costs continue to spiral. Further, without slowing rising housing costs then changing the CPI, the Bank of England's target indicator, will also make 'official' inflation higher – leading to higher interest rates and potentially damaging the economy.

Wider positive impacts on ownership, equality, poverty, transport and economics

Ownership, inequality and poverty

- Under these reforms the home-ownership rate should rise to around 80% or so within a decade and keep rising – in line with 20th century trends and reversing the decline of the past decade.

- Increased home-ownership would lead to a substantial narrowing of the current 20:1 ratio of wealth between those who own their homes and social tenants. If the average social household ends up owning a property worth just £100,000 this ratio would fall to 4:1.
- Increased housing affordability would also remove many of the negative effects of the pinch on income and wealth that younger households are currently feeling, reducing generational inequality in a way that should be acceptable to the older generations.
- Poverty should decline due to these reforms. If the employment rate for social tenants rose by 550,000 and just half of these households were those with children that moved out of poverty, this would lift around 300,000 out of poverty – nearly equal to the entire reduction in child poverty between 1996/7 and 2007/8.

Transport and economics

- There would be an improvement in transport flows in and around London, as the changes set out cause a demographic shift in expensive parts of Inner London, where social housing would slowly be phased out and young working individuals would move in, reducing commuting demand and redistributing travel patterns – easing problems on particular bottlenecks.
- This is essential given the tight budget transport will have in the coming years and how close to capacity much of London and the South East public transport system is. In the 2000s transport demand hugely outpaced growth and this is likely to continue.
- More broadly, these reforms would help rebalance the economy toward construction and away from speculation in property rather than productive investment. They should also help increase employment – crucial when government is relying on the private sector to create millions of new jobs in the next few years.
- They would also raise £100 billion that would otherwise need to be cut from other areas and instead allow for large numbers of new homes over the next few years – effectively creating a large economic stimulus rather than a large cut in demand.

Without these radical changes current negative trends in housing and pressures on government expenditure will only get worse in the next decade or so. House prices may fall in the next couple of years but will not become affordable for the vast majority unless policy changes. Government must avoid the temptation to 'salami-slice' its way out of the current crisis rather than implementing necessary structural reforms. The reforms in this paper are a detailed exposition of one of the areas where public sector reform can dramatically reduce costs while leading to more desirable outcomes. Savings of a further £20 billion a year are possible from structural reforms in two other areas.

Basic Description of Costs and Savings

These figures assume roughly 2.5% inflation and rise with it, so they are 'real terms' savings. These are all very much ball park figures. Savings use the Hills Report's valuation of social housing assets at £400 billion which may be an underestimate.

Table 1: Costs and savings to government from implementing the reforms proposed in this report

	Year 1	Year 2	Year 3	Year 4	Year 5	Years 6-10	Years 11-20
Savings (£ billion)							
(a) Sales receipts from Right to Buy and Right to Move and Buy (above present predicted sales)	14.8	10.4	10.1	9.9	9.7	5.4* falls to 4.9	0.5* falls to 0.2
(b) Selling off deceased tenants social housing stock	8	7.8	7.7	7.5	7.4	7.2 falls to 6.6	6.5 falls to 5.3
(c) Reduced construction/maintenance costs of social and affordable housing	7.8	7.8	7.8	7.8	7.8	7.8	7.8
(d) Reduction in welfare dependency if social housing 'employment penalty' is eliminated	0.7	1.4	2.1	2.8	3.5	4.2 rises to 7	7
(e) Rents rising more slowly meaning private renters' Housing Benefit rises more slowly	0.4	0.7	1.1	1.5	2	2.5 rises to 4.7	5.3 rises to 12.9
(f) Reduction in retired social tenants housing costs	-	-	-	-	-	-	0 rises to 0.5
Costs (£ billion)							
(g) Low interest loans to low income home-owners for deposits/repairs	3	2.9	2.7	2.7	2.6	2.5 falls to 2	1.9
(h) Demolition of the worst social housing estates	2	2	2	2	2	2	-
(i) Reducing VAT on repairs and renovations	1	1	1	1	1	1	1
(j) Maintenance for 'Path to Ownership' tenants	1	1.3	1.6	1.9	2.2	2.5 rising to 4	4
(k) Paying for longer term Housing Benefit contracts	1	1	1	1	1	1	1
(l) Lost rental revenue from working social tenants	0.3	0.6	0.9	1.1	1.3	1.6	1.6
(m) Mortgage support for low income households	0.2	0.2	0.2	0.2	0.2	0.2	0.2
Rough Annual Net Gain to Exchequer (£ billion)	**23.2**	**19.1**	**19.4**	**19.6**	**20.1**	**16.3* rises to 19.7**	**15.9* rises to 22.5**

* In reality there will be a more tapered decline in stock sales and hence totals, but there are likely to be two 'drop' points where revenue does fall substantially around these years, even if the decline is in fact spread more over the preceding and subsequent year.

NOTE: This table excludes the projected £6 billion savings from uprating benefits with the CPI in future. Much of this £6 billion in projected savings will only be realised if housing costs rise only slowly – which requires changes to the planning system in order to be achieved.

Savings

(a) Sales receipts from Right to Buy and Right to Move and Buy (above present predicted sales)

The projected sales receipts from these two schemes are given below:

Table 2: Revenue from sales of social housing over twenty year period (revenue figures are £ billions to nearest decimal)

	Year 1	Year 2	Year 3	Year 4	Year 5	Years 6-10	Years 11 -20
Right to Buy/Move and Buy sales involving tenants, number and (%)	240,000 (6)	175,000 (4.4)	175,000 (4.4)	175,000 (4.4)	175,000 (4.4)	105,000 (2.7)	30,000 (0.7)
Revenue raised by these sales	**15.8**	**11.4**	**11.1**	**10.9**	**10.7**	**6.4 falls to 5.9**	**1.5 falls to 1.2**

The revenue is stock value, (£4 billion per 1% according to the Hills report), multiplied sales subtracting an average discount of 33%. £1 billion is subtracted from revenue each year to represent Right to Buy sales likely to occur even without these reforms. Stable house prices combined with moderate inflation reduce projected revenues in real terms by 2% a year. The reasons behind the estimates of Right to Buy and Right to Move and Buy sales involving working tenants, (which are very rough ballpark estimates,) are set out in Part 2 (4) of this paper.

(b) Selling off deceased tenants social housing stock

John Hills valued each 1% of the social housing stock as worth £4 billion. 2% of stock each year is released as tenants die, around 80,000 properties. If this is sold off, with the most expensive properties sold on the open market and the rest into the Path to Ownership model, (they are re-bought by government, which pays for this by issuing bonds against them), this raises £8 billion a year. Roughly stable house prices and moderate inflation reduce projected revenues in real terms by 2% a year. This flow is constant over the next few decades as older households are unlikely to buy their home and stay social tenants until they die, meaning Right to Buy/ Right to Move and Buy sales will not reduce this flow of properties for sale.

(c) Reduced construction/maintenance costs of social and affordable housing

The last year where figures are available saw government spend around £9.3 billion on housing. This can now be reduced very sharply to £1.5 billion a year as the 'decent homes' programme is almost finished, affordable housing will no longer be funded by central government, and future construction costs for almost all social housing will be covered by the issuing of government bonds. In addition maintenance costs for social tenants will fall as the existing stock and tenant numbers reduce and new tenants come under the Path to Ownership scheme (see (j) below).

(d) Reduction in welfare dependency if social housing 'employment penalty' is eliminated

The current gap in employment between social housing tenants and others is 40%, with around 20-25% of this 40% gap down to 'unexplainable' factors. Since this paper argues it is the incentives these households face that cause this gap, changing social households' incentives should remove much of this social housing 'employment penalty' (perhaps 20% of this 25%). Removing 20% of working age social households from welfare dependency saves roughly £7 billion a year in welfare. This is assumed to be done over a ten year period, with savings generated over time in proportion to the amount of individuals returning to employment. To be cautious, savings exclude any tax gains from households returning to work. This is explored more in Parts 1 (3) and 1 (4).

(e) Rents rising more slowly means private renters' Housing Benefit rises more slowly

If private rents and so Housing Benefits being paid to private tenants rise at the reasonably stable rate of 1% compared with recent annual rises of around 5% this gives the savings outlined in this table. This saving assumes a 10% reduction from the current £10 billion on Housing Benefit for private tenants to £9 billion due to planned reforms around capping excess claims, but for reasons explored in this paper does not assume further savings are possible from linking Housing Benefit rises to the CPI. Thus savings are calculated from the gap created by this £9 billion rising at these two different speeds of 1% and 5% a year. These savings assume the numbers of Housing Benefit claimants in private housing stays the same.

(f) Reduction in retired social tenants housing costs

Almost all social tenants need Housing Benefit when retired to pay their rent. If households own their home, this cost is not incurred. 2.75 million working age social tenant households exist, and the average cost of a social tenancy was £69 a week in 2008. This gives a figure of £10 billion for all households per year when these retire. Assuming each household requires rent for twelve years on average gives a figure of £120 billion. Spread over perhaps forty years as households retire gives £3 billion a year. If two-thirds of these households move into owner-occupation this saves £2 billion a year. These gains begin fifteen years after reforms begin and rise by £0.1 billion a year toward this £2 billion figure, reaching £0.5 billion after five years.

Costs

(g) Low interest loans to low income home-owners for deposits/repairs

Both schemes are based on lending up to £15,000 to over 100,000 households per year. The original cost is capped at £1.5 billion for each scheme. 70% of average loan is paid back at 0% interest over a ten year period, (e.g. if £15,000 is borrowed repayments are £1,050 per year.) Assuming 2.5% inflation a 70% repayment of the initial loan over ten years returns around 62% of the initial value. As money coming in over time can become funds going out, after ten years the annual cost per scheme falls from £1.5 to around £0.94 billion. This means some of the cost each year becomes covered by previously lent money returning. The cost of the two schemes therefore would fall to an annual cost of £1.9 billion, and then continue at this cost indefinitely.

(h) Demolition of the worst estates

For the next ten years £2 billion should be set aside to help pay for demolition of the worst estates. £1 billion would be for working tenants in these areas wanting to use the Right to Move and Buy. Another £1 billion a year would compensate those who might have bought in these estates. Other social tenants should be moved into the Path to Ownership model in nearby properties or to existing properties under their current terms. Land from these estates would be sold to developers with planning permission to develop and with these funds returned to government in order to help pay for this scheme. Given the sale of these estates to developers no reduction in asset sales is projected from these sales as due to the problems on these estates the alternative values of properties is very low and almost no tenants would want to buy homes there.

(i) Reducing VAT on repairs and renovations

£1 billion was the official estimated cost in 1998 of abolishing VAT on repairs and renovations altogether. This is costed at £1 billion if VAT is still charged above a set level (e.g. £15,000 per house) so that more expensive extensions still pay some VAT.

(j) Paying for 'Path to Ownership' social housing maintenance

The government will no longer collect rent from new Path to Ownership social tenants but will still support their maintenance. This is likely to cost around £2,000 per tenancy a year. As the numbers in the new Path to Ownership model start at zero and then rise, so do costs, from £1 billion in the first year to £4 billion a year by 2020. This allows 2 million households' maintenance and repairs to be completely supported from 2020. As tenants in the Path to Ownership model move toward owning their home, this support will be withdrawn in proportion to the share of the property they own until it reaches zero. Past 2020, it is assumed that new tenants coming into the scheme should be balanced by those moving toward paying the full cost of their maintenance, so no increase above this £4 billion a year is predicted post 2020. As home-ownership becomes affordable over time and social housing waiting lists fall it may be possible to reduce this spending post 2020, but to err on the side of caution this is not assumed.

(k) Paying for longer term Housing Benefit contracts

As the allocation system for social housing will no longer be 'needs-based' then to ensure medium-term stability for vulnerable households, (e.g. those with children,) such households renting privately and using Housing Benefit will be given medium-term contracts in the private sector. To do this a lump sum payment of some £4,000 would be made to landlords in return for a longer contract (e.g. 3 years). This would provide the stability that such vulnerable households need without distorting the allocation of social housing. If each year around 250,000 contracts are created with lump sum payments of £4,000 each this costs £1 billion per year.

(l) Lost revenue from working social tenants

Around 33% of roughly 1.3 million social tenants pay their rent (rather than rely on Housing Benefit). This revenue would be lost as existing working tenants under typical existing contracts move into home-ownership. The average rent is £3,510, but annual service costs are £2,232 in 2008/9, so the average net gain per social tenant paying rents is just £1,280 or so. Multiplying this figure by 1.3 million gives £1.6 billion. This would be lost as working social tenants moved to own their property over time rather than all at once, and so mounts over time.

(m) Mortgage support for low income households

This consists of temporary interest free-loans for households in difficulty, with a maximum cap of £10,000 per household. If in any one year 1 million households, over 5% of all home-owners, took this up in at the maximum rate of £10,000, the cost of this would be the government interest on the loans during these six months. This is just £200 million (1 million households borrowing £10,000 at 4% annual interest (government borrowing rates) for six months gives £10 billion x 2%). The basic amount lent to government would then be recouped by adding the sum borrowed to the mortgage costs of the household borrowing and the funds transferring back to government. Should the house be repossessed the government will receive its money from the sale of the property.

Part One
Where We Are

1

Housing Expenditure Must Fall Sharply

The government will have to cut housing spend to reduce the deficit

There is no use coming up with any policy that increases housing spending given a government deficit of around £156 billion in 2009/10,[2] and a national debt heading towards £1.4 trillion.[3]

Previous rapid deficit reduction in Canada in the 1990s and the UK in the early 1980s required a substantial fall in housing spend. In Canada's case it simply abolished national housing budgets, devolving it along with other welfare programmes to the provinces, in return for a lump sum payment called the Canada Health and Social Transfer Programme. This lump sum payment fell by roughly 15% and unsurprisingly the provinces cut housing rather than education or social services. An assessment in 2007 found Canada spent $65 per year on social housing per head of population, effectively maintaining a small stock of existing properties. We spend roughly three and a half times that.[4]

Meanwhile housing was the largest part of the cuts made in the first Thatcher term. The Thatcher government's expenditure plans from 1980/1 to 1983/4 envisaged 75% of the real term *reductions* in department spending (over and above departmental freezes) coming from the Housing Budget.[5] This sharp reduction was duly enacted, with housing spending falling in real terms by around 55% between 1979/80 and 1983/84.[6]

Given the current situation and from examining successful reductions in government expenditure in similar circumstances, it is clear housing policy as a whole will have to substantially contribute to the very sharp fiscal tightening that is necessary over the next five years.

2 *Public Sector Finances, April 2010*, Office for National Statistics (ONS), 2010

3 *Budget 2010*, HMT, 2010

4 *National Housing Day 2007-Policy Background*, Wellesley Institute, 2007

5 *Enquiry into Implications of the Government's Expenditure Plans 1980-81 to 1983-84 for the Housing Policies of the Department of the Environment,* The Stationery Office 1980

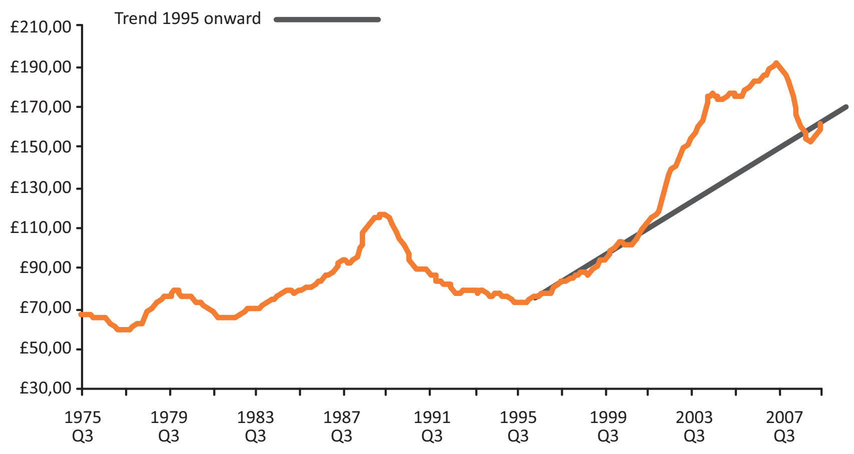
6 A D H Crook *"Privatisation of housing and the impact of the Conservative Government's initiatives on low-cost homeownership and private renting between 1979 and 1984 in England and Wales: 1. The privatisation policies",* Environment and Planning A, vol 18, pp 639-659, 1986

2
Unaffordable Housing is an Ongoing Crisis

House prices are still at record highs

The problem is that this time any cuts will come at a time when the cost of housing is a major issue for many households. Figures from Nationwide show house prices in nominal terms more than *tripled* between the end of 1995 and 2010.[7] Even more historically astounding, between 1995 and 2009 average house prices rose in real terms by 120% (e.g. even after accounting for the post 2007 crash), from £72,659 to £160,000.[8] Before 1995 house prices generally only rose in nominal terms (e.g. house prices had risen each year, but less than inflation). Thus between 1975 and 1995 average house prices in real terms rose 3.5%.[9] The only other rise in real term house prices post World War II was a 30% rise in the late 1980s housing boom, which unwound in the early 1990s recession. It should be noted that as discussed later the work of Kate Barker found even this small rise was higher than in many countries, (meaning house prices fell in real terms in these nations, though they rose in nominal terms due to inflation). Figure 2 shows how steep and unprecedented the rise in real term house prices since the mid-1990s has been.

Figure 2: Real term average house prices (prices adjusted for RPI inflation) 1975-2009[10]



7 *Nationwide, average UK house prices since 1952*, Nationwide, available on their website

8 *Nationwide, average UK house prices adjusted for inflation*, Nationwide, available on their website

9 *Nationwide, average UK house prices adjusted for inflation*, ibid

10 *Nationwide, average UK house prices adjusted for inflation, base year 2009 Q3*, ibid

Median house prices rose from 3.5 times the median wage in 1997 to 6.27 times the median wage in 2009, even after the recent crash.[11] They are therefore still almost twice as expensive in terms of income/prices as they were in 1997. The cost of housing is a national crisis. The ratio of median house prices in the 'cheaper' North East and North West stands at 5 times average earnings, while in the West and East Midlands the ratio is around 5 and a half times average earnings, compared with over seven times average earnings in some areas.[12] Unaffordability is not confined to the middle of the market. Lower quartile house prices, (i.e. prices halfway between the bottom and average price) were six times higher than lower quartile earnings in 2009,[13] making home-ownership very expensive for low income households.

While the share of income that is taken up as repayments for first time buyers is slightly under their average since the mid-1980s – at 18.4%,[14] this is largely because the average first time buyers' income has doubled to £40,000, up from £20,000 in 1997.[15] Had this risen in line with inflation, the average first time buyer's income would be £25,000.[16] In other words, low income households are simply dropping out of the market. In addition, the average deposit is now 27.7% rather than 10.2% in 1995,[17] while borrowers are benefiting from a 0.5% Bank of England base rate last seen in the Napoleonic wars. These factors mean that first time buyers' housing costs are 'affordable' only because those buying are affluent and doing so on very favourable terms. Mass home-ownership is simply unsustainable at today's high prices.

Higher house prices have reversed rising levels of home-ownership

These sharply rising prices since the mid-90s have reversed almost a century of rising home-ownership. Between 1953 and 1991 the proportion of home-owners in the UK rose from 32% to 67.6%, an average of around 9% a decade. Had this continued the rate of home-ownership would have risen to be close to 85% in 2011. But home-ownership only rose by 2.8% between 1991 and 2001, and fell between 2001 and 2008 as a proportion of all households by 2.1% – the first such fall since 1918. Table 3 sets out how housing tenure has changed over time.

Table 3: % of households in each housing tenure 1918-2008[18]

Date	Owner occupation	*Change*	Social rented	Private rented
1918	23.0	-	1.0	76.0
1939	32.0	*+9*	10.0	58.0
1953	32.0	-	18.0	50.0
1961	43.0	*+11*	23.0	34.0
1971	51.0	*+8*	29.0	20.0
1981	57.2	*+6.2*	31.7	11.1
1991	67.6	*+10.4*	23.0	9.4
2001	70.4	*+2.8*	19.5	10.1
2008	68.3	*-2.1*	17.7	13.9

11 *Table 577; ratio of median house prices to median earnings*, Department of Communities and Local Government (DCLG), available on their website

12 *Table 577; ratio of median house prices to median earnings*, ibid

13 *Table 575; ratio lower quartile house prices to lower quartile earnings*, DCLG, available on their website

14 *Table 539; repayments as a % of income and deposit as a % of purchase price, by type of buyer, UK*, DCLG, available on their website

15 *Table 513; Simple average house prices, mortgage advances and incomes of borrowers, by new/other dwellings, type of buyer and region*, UK, DCLG, available on their website

16 *Consumer Price Indices CPI and CPI12*, ONS, available on their website

17 *Table 539; repayments as a % of income and deposit as a % of purchase price, by type of buyer, UK*, ibid

18 *From Table 801; Household characteristics, tenure trend, from 1918*, DCLG, available on their website

Further evidence house prices are too high for first time buyers is that in the 2000-09 period first time buyers made up just 35% of new mortgages, even lower than in the 1990-99 period, when they made up around 50%.[19] First time buyers – the young and those on low incomes are simply being pushed out of the market.

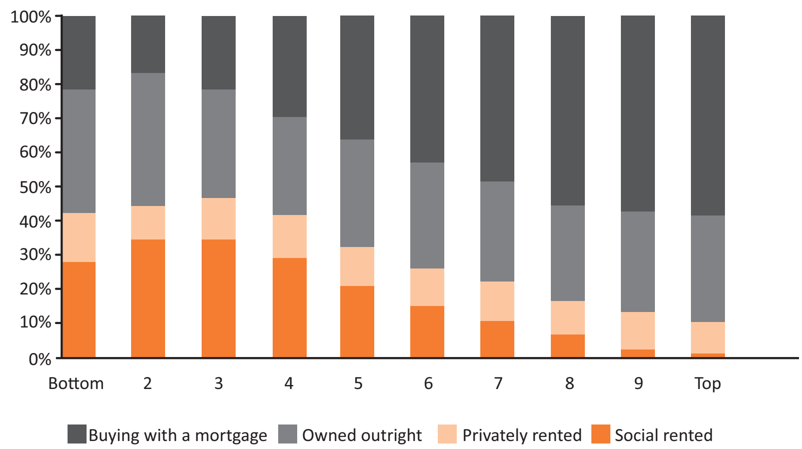
So many young people now live at home it even has a modern acronym to describe it as a lifestyle trend – "KIPPERS" – "Kids In Parents Pockets Eroding Retirement Savings". More scientifically, the ONS noted that the proportion of young people under 30 with a mortgage fell sharply from 43% in 1997 to 29% in 2009%.[20] And by late 2009 a staggering 80% of first time buyers under 30 needed help from their parents.[21] This is having an impact on family life – with 21% of people saying they are currently delaying having a family because they simply cannot afford a home.[22]

There has been a great deal of concern about what David Willett's has identified as 'the Pinch', where younger households are increasingly seeing their disposable income stagnate while older households are becoming increasingly wealthy. Housing is the largest component of this Pinch – with the baby-boomers sitting on large levels of housing wealth, while their children increasingly cannot afford to own. Under 50s hold just £540 billion or just 18% of the £2.9 trillion in housing wealth in the UK, making the divide in housing a key issue in this generational split.[23]

Home-ownership for low income households is higher than thought

The rise of home-ownership was simultaneously both one of the most egalitarian and conservative trends of the 20th century – if one of the least celebrated. There is a consistent and erroneous belief that lower income households are all social tenants. But in fact in 2004/5 there were more owner-occupiers than any other group across income groups. Even in the bottom three income deciles, no more than 33% lived in social housing, with around 20% in these groups having a mortgage and many others being outright owners.

Figure 3: Housing tenure by income decile[24]



19 *Table 513; Simple average house prices, mortgage advances and incomes of borrowers, by new/other dwellings, type of* buyer and region, UK, ibid

20 *Fall in the proportion of young homeowners; news release*, ONS, 2009

21 *Tightening in lending criteria abates*, Council of Mortgage Lenders (CML) press release, 2009

22 *Young adults delaying getting married and starting a family due to affordable housing drought; Press release 22 March 2010*, YouGov; Poll for Housing Federation, available on their website

23 David Willetts, *How Rich Are the Baby Boomers and How Poor Are Their Children* (presentation), LSE, available at their website

24 *The Hills Report into Social Housing*, Centre for the Analysis of Social Exclusion/DCLG, 2007

While social tenants are poorer than average – nearly half are 'low income' (below 60% of the median income after housing costs),[25] the poorest are not all social tenants. Yet this positive tendency toward rising home-ownership across society is now at risk from spiralling house prices.

The overwhelming majority of people still want to own their own homes

Despite rising prices in 2007 one survey found 84% of households saying they would like to own their own home 'in the next ten years'.[26] It was even higher for the 25-65s, standing at 87%. This did not vary hugely across the UK regions. The recession has had only a minor impact on the desire of most people to own their home. A 2010 poll for YouGov found that around only 21% of those they surveyed were neither owners or were not planning to buy, with only around 13% of ABC1's putting themselves in this category.[27] This indicates desire for home-ownership in the short-term may have fallen slightly to 79%,[28] – mirroring a similar decline in the aftermath of the 1990s recession – though the percentage wanting to buy quickly rose back to the mid-80s after this.

This evidence of a slight dip in the numbers wanting to own contrasts with 2010 government polling that found 82% of all adults saw owning as the ideal tenure even in the aftermath of the recent housing slump. It also found 75% of those 25-34 year olds who expected to rent in three years time said they would rather own but couldn't afford to do so – showing there is an increasing gap between aspiration and reality for many households.[29]

Owner-occupiers are the happiest of all tenures with their housing

One major reason people want to own their homes is the satisfaction this brings as individuals gain an asset for their families, can decorate and renovate their home as they see fit, and generally feel they have a stake in society. According to the seminal 2007 government-commissioned but independent Hills report into social housing just 3% of owner-occupiers were dissatisfied with their accommodation versus 16% of social tenants. Private renters' satisfaction was in-between. Scottish government research on satisfaction levels shows a similar pattern with just 1% of owner-occupiers not satisfied with their housing (versus 77% very satisfied).

Table 4: Scottish government findings for satisfaction with housing in different tenures[30]

	Owner-occupiers	Social renters	Private renters	Total
	%	%	%	%
Very satisfied	77	44	41	66
Fairly satisfied	21	42	54	29
Not very satisfied	1	10	5	4
Not at all satisfied	0	4	1	1
Base: All respondants (n=1,211)	508	356	314	1,211

25 *The Hills Report into Social Housing*, ibid

26 *Improving Attitudes to Home Ownership*, Council of Mortgage Lenders, 2007

27 *Buying a Property [New Homes Marketing Board]*, YouGov, available on their website

28 *Improving Attitudes to Home Ownership*, ibid

29 *Public Attitudes to Housing 2010*, DCLG, 2010

30 *Housing Aspirations*, Scottish Government Social Research Publications, 2007

Cross-country studies confirm home-owners are happier than other tenure types. Elsinga and Hoekstra found that in seven out of eight countries, owner-occupiers were happier than renters.[31] A study by Diaz-Serrano similarly found that tenure status is critical in determining housing satisfaction across 12 EU countries and home-ownership is the key to housing satisfaction.[32]

It is a myth that the UK has unusually high home-ownership rates

It is clear that the government should support home-ownership. Unfortunately, largely based on comparing the UK with a couple of Northern European nations, there is a widely held view that declining home-ownership is unimportant because it is thought we have unusually high home-ownership rates already. Indeed, some politicians occasionally argue we need to become 'more like Europe' – meaning that we should see more renting rather than owning their home.

Yet a look at the statistics shows that home-ownership is not peculiarly British, but is desired across developed nations. The last set of major statistics compiled for the EU showed the UK was already in the middle of the EU for home-ownership rates, coming 11th out of the 20 EU Member States with comparable figures.[33] Many other countries now have higher rates than the UK. This study also found the rate of home-ownership across the EU rose from 53% to 68% between 1980 and 2000 (using countries that have comparable figures from 1980/2000), showing that as incomes rise home-ownership is desired across developed countries.

Another study of 19 developed countries including nations outside of Europe, (such as the USA and Australia), by Scanlon and Whitehead put the UK as part of a "*Mid-level Owner-occupation*" set of countries.[34]

Social tenants want to be owner-occupiers not social tenants

Politicians need to reconnect with the electorate. And on housing, they should realise that the desire for home-ownership is not going away. Social tenants, like most people, aspire to own in many cases – as one social tenant stated about their tenure to government researchers – "it is just life, it is just another of life's disappointments".[35]

In surveys on tenure preference around half of all social tenants state they want to be owner-occupiers without qualification. The Hills report noted the British Social Attitudes Survey found 45% and 46% of council/housing association tenants respectively stated an outright preference for owner-occupation. Separately, the Council for Mortgage Lenders found that around 8% of the entire population indicated council or housing association tenure would be their preferred occupancy in ten years time, (around half of all the 17% of households in social housing – assuming only a small number want to move into social housing).[36] This gives around half of all social tenants as being firmly in favour of becoming home-owners. Research for the Notting Hill Housing Trust found even in the South East and London 63% of tenants were planning or wanted to buy – against just 26% who had no aspirations to buy.[37]

Supporting this aspiration is popular. There is wide support for helping social tenants into home-ownership – a 2008 Mori poll showed 72% agreed that more

31 M. Elsinga, & J. Hoekstra, *Homeownership and housing satisfaction.* Journal of Housing and the Built Environment, Volume 20, pp401–424, 2005

32 L. Diaz-Serrano, *Housing Satisfaction, Homeownership and Housing Mobility: A Panel Data Analysis for Twelve EU Countries*, Paper for the Institute for the Study of Labour (Germany), 2006

33 *Housing statistics in the EU,* National Board of Housing, Building and Planning, Sweden. Figure 2002 or 2000 if unavailable. Excludes Malta and Luxembourg and countries not proving data. (2004)

34 Scanlon and Whitehead, *International Trends in Housing Tenure and Mortgage Finance*, LSE/CML, 2004

35 *Housing Aspirations*, ibid

36 *Improving Attitudes to Home Ownership*, Council of Mortgage Lenders (CML), 2007

37 *Assets and Opportunities,* Notting Hill Housing Trust, 2007

should be done to give social tenants opportunities to become home-owners,[38] while the huge success of Right to Buy in the 80s and 90s shows that many tenants respond well to measures that help them into ownership.

However, not only do around half of social tenants usually say they want to be owners, those who do not usually cite problems with them being owner-occupiers (e.g. cost of repairs or the impossibility of owning due to high prices), *not* a positive preference for social renting.

> "Not only do around half of social tenants usually say they want to be owners, those who do not usually cite problems with them being owner-occupiers, *not* a positive preference for social renting"

Scottish government research found the top three reasons for wanting to stay social tenants were house prices being to high/income too low (41%), cost of private repairs and maintenance were too high (18%), and concerns about security of tenure (11%).[39] The Notting Hill Housing Trust found that 30% of those who said they did not want to own their current property were put off by the cost of doing so.[40] A survey by the DCLG showed 38% of social tenants thought that the best thing about social housing was they were not responsible for repairs and upkeep, unlike home-owners.[41] Social ownership is often viewed as a safe, but not desirable, tenure, even if tenants do not say that they would like to move into home-ownership.

Support for low income home-owners is very limited compared with renters

Despite the fact that there are more low income home-owners than renters, and most people, including social tenants, want to become home-owners, low income owners receive little help. Assistance has declined in recent years and now only around £400 million is spent on schemes to help (low income) home-owners. The *(Income) Support for Mortgage Interest* ((I)SMI) scheme and the new Homeowner Mortgage Support Scheme (HMSS) pay interest for those who lose work but have a mortgage. In 1995 ISMI cost around £1 billion and roughly 500,000 households claimed it, but by 2007 just 100,100 low income households at roughly £47 per week and 120,000 pensioner households at £20 a week claimed it, a cost of around £245-£345 million.[42] It is likely this fall reflects various facts. Firstly, government limited the help available to each household in 1995. Secondly, interest rates fell while house prices rose, (meaning less help was needed to pay interest and more to repay the principal repayments – which ISMI did not cover). Finally, the ending of MIRAS as a route to 'talk to' home-owners would have lowered awareness of this scheme. Meanwhile the HMSS helped just a total of 15 households in 2009.[43]

Private sector home improvement grants to help low income households with repairs and maintenance have also been steadily reduced over the past two decades (of course renters, (social or private) do not pay maintenance and repair costs). They declined throughout the 1990s, falling in England from £316 million in 1990 to £172 million in 1998,[44] and central government scrapped in 1996. Data is no longer being centrally collected, as many councils no longer offer such assistance. It is likely this current spend is less than the £172 million recorded in 1998.

38 *Ipsos MORI housing survey shows support for Housing Minister proposals on social housing*, Ipsos-Mori, available on their website

39 *Housing Aspirations,* ibid

40 *Assets and Opportunities,* ibid

41 *Attitudes to housing, Findings from IPSOS-Mori Public Affairs Monitor Omnibus*, DCLG, 2009

42 *Means-tested benefits: help with mortgage costs*, Standard Note: SN/SP/737, House of Commons, 2008

43 *Action by government and lenders keeping families in their homes,* DCLG press release, 2009

44 R. Burrows, J. Ford, and S. Wilcox, *Half the Poor: Policy Responses to the growth of low-income home-ownership*, (pp11-21) Housing Finance Review 2000/1, Joseph Rowntree Foundation, 2000

Given a rough likely spend of around £400-£500 million supporting owner-occupiers, we can contrast this with the total spent on social housing and Housing Benefits for private renters. This spending totals over £35 billion – in Housing Benefits, subsidised rents for social tenants, and spending on building or maintaining social housing. Overall, renters, receive a combined total of around 70-80 times as much support as home-owners, despite low income renters being fewer in number than low income home-owners.

Social housing waiting lists rise due to higher house prices *more than* falling stock levels

Despite what many on the left argue, it is the general housing affordability crisis *not* the Right to Buy that is behind rising social housing waiting lists. Waiting lists track house prices, not stock levels – because they are primarily demand-led, not supply-led – as Table 5 shows.

Table 5: How the factors of supply and demand impact on social housing waiting lists

Period	Supply factor: Changes in supply			Demand factor: Rise in real house prices[45]	Approx. rise in waiting lists
	Right to Buy [46, 47]	New homes[48]	Net change		
1981–1997	-100,000	+36,000	-74,000	+ 8%	-200,000
1997–2009	-46,000	+18,000	-28,000	+ 108%	+770,000

Overall stock declined by a net total of 74,000 homes a year from 1981-97, but just 28,000 a year from 1997-2009. But between 1981 and 1997, waiting lists fell from 1.2 million[49] to 1 million,[50] but then rose significantly to 1.77 million by 2009.[51] The reason for this is real house prices rose between 1981 and 1997 from £74,646 to £80,569, just 8%, while between 1997 and 2009 they exploded, rising from £80,569 to £167,165, a rise of 108%. The fact that the reduction in net stock declined to around a third of what it had been was outweighed in this later period by spiralling housing costs.

Further evidence that waiting lists are determined by house prices *not* stock levels is that the rise in the waiting list since 1997 is entirely explained by a fall in the number of 'net re-lets' when social properties become vacant and are re-let. This fall was caused by a sharp decline in the numbers of private re-lets, when tenants leave the social housing sector for private housing and their property can be re-let to new claimants (i.e. excluding Right to Buy where the tenant exits the sector but takes a property with them). Total net re-lets fell steadily from 332,000 to 208,000 between 1997-8 and 2006-7, entirely due to a fall in levels of private re-lets.[52] Had the number of re-lets caused by tenants leaving to enter a different property in the private sector remained the same, there would have been at least 939,000 additional re-lets in this period – so that *waiting lists since 1997 would have fallen*, just as they did in the 1981-97 period. As private housing costs spiralled tenants were trapped in the social housing sector – and thus private re-lets dried up.

45 *Nationwide, average UK house prices adjusted for inflation*, ibid

46 1981-97 figure from *The Right to Buy,* Research Paper 99/36, House of Commons, 1999

47 1997-2009 figure *Table 678;Total Social Housing sales to sitting tenants*, DCLG, available on their website

48 From *Table 244; House Building, permanent dwellings completed*, DCLG, available on their website

49 *Housing in Britain, the post war experience*, John Short, p69

50 *Table 600; rents, lettings and tenancies, numbers of households on local authorities waiting lists,* DCLG, available on their website

51 *Table 600; rents, lettings and tenancies, numbers of households on local authorities waiting lists,* ibid

52 *Analysing key trends in the supply and distribution of social housing lettings,* Housing Corporation, 2008

All this is easy to understand once it is grasped that social tenants want social housing as a second choice. In other words, the current 'need' for social housing is not really a need for more social housing at all, but a need for new private housing. Demand for more private housing creates price rises in private housing, and this causes a growth in social housing waiting lists by pushing people into their second choice – social housing.

Only this understanding that social housing waiting lists are above all linked to private housing costs explains why the waiting list for social housing actually *fell* marginally between 2008 and 2009 from 1.769 to 1.763 million – in the middle of the UK's deepest recession since the 1930s.[53] As housing affordability marginally improved some could leave the waiting list and buy their own home, and more thought they would be able to do so in future. This more than cancelled out an increase in those wanting to move into social housing due to the recession – confounding those who, (such as the Local Government Association) argued that the recession would cause spiralling waiting lists.[54]

A clear choice in the medium-term between escalating spending and more (private) homes

Once we understand in the long run, allowing more homes will not only increase home-ownership in line with people's goals, it will also reduce demand for social homes, we see that solving one problem – stabilising house prices and supporting home-ownership will solve another – eliminating social housing waiting lists over time. The alternative to this is further pressure for greater government spending on housing – already high on voters' priorities.

In 2008 the British Attitudes Survey found 4.9% of the population said housing should be the number one priority for any additional government spending. This was the fourth highest priority, behind health, education and policing ahead of defence, transport, roads, social security, international development and support for industry. When people were asked what their second highest priority was, 8.9% said housing, again making housing the fourth highest priority for any additional spending, behind health, education and policing.[55]

Rising house prices are pushing up rents and eroding living standards

Rising house prices are not just driving demand for social housing. They are also contributing to higher rents, eroding living standards for a substantial part of the population. Higher house prices inevitably lead to rising rents. After all, as they are substitute goods, rents and home-ownership have roughly equivalent costs over time. Although this relationship is far from perfect, it is largely true in the long run. If home-ownership becomes more costly, more will try to rent, pushing up rents, and if home-ownership becomes cheaper, more will buy, pushing down rents. Similarly if house prices rise, and the cost of purchasing a house to rent out increases, rents will rise, and if house prices decline, so will the cost of a property to rent.

And so it has been the case – rents have risen sharply in recent years, just like houses prices. Between 1997 and 2009 general prices rose by 35%.[56] This was substantially below wages, as median wages rose by 52% during this period,

53 *Table 600; rents, lettings and tenancies, numbers of households on local authorities waiting lists,* ibid

54 *5 million people waiting for social housing by 2010*, LGA press release, 2008

55 *British Social Attitudes Survey 2008,* National Centre for Social Research, 2009, Colchester, Essex, available online at UK Data Archive

56 *Bank of England Inflation Calculator,* bank of England, http://www.bankofengland.co.uk /education/inflation/calculator/fl ash/index.htm

meaning living standards rose by around 1.5% a year.[57] But during this period average private rents rose 64% or so, from £341 a week in 1997-8 to £558 a week in 2007-8,[58] – notably ahead of wages. Thus, those privately renting have seen a substantial part of any increase in wages taken up by rising rents. Rising rents also increase the difficulty of saving a deposit for most households by cutting down their discretionary income.

The very high rise in rents occurred despite a sharp rise in the total numbers of dwellings being rented – from 10.1 to 13.9%.[59] The fact that rents did not rise as fast as house prices is almost certainly linked to the increased supply of rental properties – the much maligned 'buy to let' sector. Should this increase in the number of 'buy to let' properties slow, rents are likely to rise even faster than they have done in the past decade or so.

Meanwhile, since social rents are set with reference to private rents, so they too rose very rapidly in the past decade – rents rose by 57% for Registered Social Landlords between 1997 and 2009.[60] Any attempt to hold down social rent increases substantially below private rent rises would increase further the cost of maintaining the social housing sector while simultaneously increasing the desirability of these cheap rents – increasing demand for social housing and pushing up waiting lists. Ultimately, problems in all parts of the UK housing market are all broadly linked together – different faces of the same housing crisis.

Rising private rents are driving rising Housing Benefit expenditure

Rising rents increases both private housing costs, and, through Housing Benefit, government expenditure. Housing Benefits have risen from £12.2 billion in 1996-7 to an estimated £20 billion in 2009-10, a rise of 64%.[61] As Housing Benefit can be charged up to the average rent of an area, it would be expected that the costs of Housing Benefit would rise in line with private rents. So it is unsurprising that a 64% rise in private rents (and 57% rise in social rents) over the 1996-7 to 2007-8 period has been accompanied by a similar 64% rise in Housing Benefit over the 1996-7 to 2008-9 period. Though the figures for private rents cover eleven not twelve years, the fundamental relationship is clear – Housing Benefit costs rise in line with rents.

Of this £20 billion only the Housing Benefit for local authorities' tenants does not leave government. As discussed later on, around £10 billion of the £20 billion spend goes on private rents – straight out of the public sector to the private sector and of the remaining £10 billion, given that at last count 1.62 local authority tenants and 1.48 housing association tenants claimed Housing Benefit,[62] and assuming roughly similar rents, these proportions mean another £5 billion goes to housing associations. So only around £5 billion of this Housing Benefit is retained in government, the other £15 billion entirely leaves the government's hands.

This growing expenditure on Housing Benefit is the inevitable result of spiralling housing costs – not from, as some think, individual claimants' or landlords' greed. Government has proposed some welcome changes to reduce Housing Benefit, with proposed caps on weekly claims (e.g. a maximum of £400 a week for four bed homes) and changes so that housing benefits are set at the

57 *Patterns of pay; Results of the Annual Survey of Hours and Earnings*, ONS, available on their website

58 *Table 731; rents, lettings and tenancies: private rents and tenancies*, DCLG, available on their website

59 *From Table 801; Household characteristics, tenure trend, from 1918*, DCLG, available on their website

60 *Table 704; RSL rents, by district, from 1997*, DCLG, available at their website

61 *Table 114; The UK Housing Review 2009/10,* Chartered Institute of Housing, editor Steve Wilcox, 2010

62 *Table 118; The UK Housing Review 2009/10*, ibid

30th percentile in an area rather than at the median to restrict excessive claims (especially in expensive areas), but these are only one-off savings. They will produce a one-off shift in savings that pushes claimants out of the very expensive areas in the UK, and cuts the claims allowed in any particular area. This is likely to result in savings without too much hardship.

However, this done, the government plans to raise Housing Benefit in future in line with the CPI (Consumer Price Index, a measure of general inflation). Yet if rents rise at their recent 5% or so a year, government will not be able to raise the new caps in line with 2-3% CPI increases. Linking Housing Benefit to CPI will not drive down rents – because they are not being driven up by Housing Benefit – rents are rising due to a shortage of property. As only around 20-30% of renters claim Housing Benefit across the UK,[63] the idea that it will be possible to drive down claimants' rents by cutting Housing Benefit is false. The planned indexation is based on the idea Housing Benefit is rising due to landlords 'profiteering'. But Housing Benefit claims are simply rising in line with rising rents – caused in turn by the UK's housing crisis. If the government goes ahead with this plan it is likely to run into difficulties. It may well increase the numbers in temporary accommodation (eating into planned savings), while the remaining Housing Benefit claimants have to divert considerable sums of their low income into topping up rental payments.

Planned changes to the CPI will reduce much of the recent planned savings in welfare

In addition, the new government has announced plans to make two changes involving the CPI. Firstly, they have stated that they wish for the CPI to be used when annually uprating benefits, rather than the Retail Price Index (RPI), (a different measure of inflation). This is projected to save some £6 billion a year by 2015, as from 2011 benefits rise around 1.5% less each year, based on a rough annual CPI of 2% and RPI at around 3.5%.[64] Secondly, George Osborne has indicated to Mervyn King that the government wants to incorporate housing costs into the CPI, (which is the Bank of England's target indicator for inflation).[65]

The problem with doing both of these is the very reason that the CPI and the RPI have diverged in recent years is that the RPI incorporates housing costs. Government publishes ongoing figures that show the reasons why the RPI and CPI rates differ and these show that housing costs are the overwhelming reason. Table 6 sets out two typical six month periods and the causes behind the differences in the two rates.

Table 6: Gap between the RPI and CPI inflation rates and reasons behind this[66]

Date	% difference between the RPI and CPI rates	Difference due to housing costs	Difference due to other factors
July-Dec 2007	-2.13	-1.96	-0.19
July-Dec 2009	+2.17	+2.61	-0.44

63 *Table 718; Average Housing Benefit support*, ibid

64 *Budget 2010*, HMT, 2010

65 *Letter from George Osborne, Chancellor of the Exchequer, to Mervyn King, Governor of the Bank of England*, 18th May, available at the Treasury website

66 *Consumer Price Indices June 2010*, ONS, June 2010

Thus, if the CPI incorporates housing costs it will move broadly in line with the RPI over the next few years. This means the majority of the £6 billion savings pencilled in from switching indexes for benefits will not be realised as the projected gap between the two measures will close. In the medium-term, switching will only reduce welfare costs in one of two ways. Firstly, this will reduce costs if housing costs are not incorporated properly into the CPI, (storing up an asset bubble for later). Secondly, whichever measure is used, government addresses the drivers of rising housing costs and so holds down inflation. It is clear which one the government should choose.

“There has been a great deal of agonising about ‘hobbit home’ Britain and the lack of space (and gardens) new homes provide”

On top of all these problems the quality of new-build homes in the UK is deteriorating

The UK’s increasingly expensive homes are not increasingly better quality – rather they are becoming both more expensive and less appealing. There has been a great deal of agonising about ‘hobbit home’ Britain and the lack of space (and gardens) new homes provide. In 2002, Bradford and Bingley released a report showing newly built homes in France and Germany were over 100m^2 – larger than the existing homes, whilst the UK’s new houses, at 76m^2 on average, were the same size as existing homes. Japan and Holland, countries with similar pressures on land as the UK, built substantially larger houses – Japan’s at 92m^2 and Holland’s at 115m^2.[67]

Table 7: New dwellings completed in financial year by type of dwelling (as a %)[69]

Financial year	Houses		Flats	
	1-2 bedrooms	3+ bedrooms	1-2 bedrooms	3+ bedrooms
2000/1	16	64	18	2
2007/8	8	44	47	1

Since then there has been an acceleration of the trend for new dwellings to be flats, as Table 7 shows. This is despite people’s strong preference for houses with gardens, with one poll showing just 2% said their preferred home was a flat (a statistical 0% said it was a high rise).[68]

The design quality of the UK’s new homes is also often poor. The Commission for Architecture and the Built Environment (CABE) performed a ‘housing audit’ on new houses using the government’s Building for Life criteria. This found just under one in five developments were of a good standard, and almost three in ten were so bad their local planning authority should have rejected them. The CABE reported, “The audit shows family housing with no play areas, windows looking out on blank walls, poorly lit areas, confusing sites with no focal point, and broad expanses of tarmac.”[70] It is certainly not an increase in new homes’ average size and quality that is driving their prices upward.

67 *Better Homes and Neighbourhoods*, Royal Institute of British Architects, 2007

68 *Bungalow’s are people’s choice in England,* MORI 2002, available on their website

69 *Recent developments in the UK Housing Market,* ONS, August 2009

70 *Regional Housing Audits*, Commission for Architecture and the Built Environment, 2007

'Affordable housing' schemes are a small proportion of homes and not a viable solution

A major part of the current response to the problem of rising house prices is 'affordable housing' – part of the housing stock made more affordable via government subsidy. Government subsidy to the main new low-cost home-ownership schemes (NewBuild and OpenMarket HomeBuy) was £34,623 and £26,762 per unit on average (respectively).[71] In 2008-9, 24,680 low-cost home-ownership houses were constructed.[72] Multiplying these figures with the average subsidy (approximately £30,000) gives an annual rough cost for affordable housing at £700 million.

This supply of 25,000 homes must be put in context against a total of 940,000 mortgage transactions (excluding remortgages) in 2007-8,[73] and around 22 million households within the UK.[74] Thus in one year, the proportion of affordable housing transactions was 2.5% of all property transactions and around 0.1% of households. The solution to high house prices cannot be something that only affects 0.1% of households. To expand them to the necessary scale (even if we wanted to) is simply impossible given financial constraints over the next decade or so.

71 *House of Commons Written Answers, 20th April 2007, Column 793*, Hansard,

72 *Table 1000; Additional affordable homes provided by type of scheme,* DCLG, available on their website

73 *Mortgage Product Sales Data Trends Report September 2008,* Financial Services Authority, 2008

74 *Table 104; Dwelling stock by tenure, historical series*, ibid

3
A Failing Social Housing Sector

The social housing sector is currently in even more difficulty than the private housing sector. Not only is social housing not what its tenants want, it is acting as a barrier to reducing poverty for its tenants. This failure is deep rooted in existing policy mistakes.

The social housing sector is large not 'residual' as is often argued

While there has been a decline in the rate of new homes being added to the rented social sector, in 2008 social homes made up a substantial 17% of all households in the UK – 3.87 million households out of around 22 million.[75] Internationally compared, in 2004 the average EU social housing stock made up just 10.1% of homes, less than half the UK's 2004 rate of 20.8%.[76]

The social housing sector's assets (housing association and local authorities) were conservatively estimated as being worth £400 billion in 2004 by the Hills Report.[77] To put this in context, this is around half of the current national debt. The main change in the sector in recent years has been that while in 1997 registered social landlords rented to 935,000 households, and local authorities rented to 3.4 million, then by 2007 stock transfer meant 1.98 million households rented from local authorities and 1.88 million from registered social landlords.[78] While the social housing sector is still large, it has declined slowly in recent years due to Right to Buy. This has not been replaced, the main reason being that it costs a great deal to build new social homes. The current model of subsidising new social housing upfront means each new social property costs £62,000 in government subsidy – a huge cost at the present time.[79]

The cost of social housing is around £15 billion a year in direct housing costs

The social housing sector is still a large cost to the Exchequer. The building of new government housing and improvements to existing stock totalled £9.3 billion according to the Treasury in 2009.[80] If around £700 million is for affordable housing this means around £8.6 billion was spent building and renewing social housing.

Social rents per household have risen from £58 a week in 2004 to an average of £73.5 a week in 2009 for tenants of Registered Social Landlords, and from £49.1 a week to £61.5 a week for tenants of Local Authorities[81] (3.6 and 4.2% a year respectively). Government subsidised social rents to below market rates by £6.6

75 *Table 104; Dwelling stock by tenure, historical series,* ibid

76 *Regular National Report on Housing Developments in European Countries,* The Housing Unit, the Irish Government, 2004

77 *The Hills Report into Social Housing*, ibid

78 *Table 104; Dwelling stock by tenure, historical series*, ibid

79 *House of Commons Written Answers, 20th April 2007, Column 793,* Hansard,

80 *Public Expenditure, Statistical Analyses*, HMT, 2009

81 *Table 703; Registered social landlord rents by region, and Table 701: Local Authority Average Weekly Rents by Region*, DCLG, available on their website

billion in 2004 (i.e. this is how much it cost to set social rents at a lower level than the market rent for each property). This was concentrated in 3 UK regions, with all six other regions obtaining less than £2 billion in subsidy. As social rents largely tracked private rents since 2004, any changes in the level of £6.6 billion of subsidy are likely to be small (both will have risen at roughly the same rate). This subsidy given to social tenants will however still be concentrated in particular areas, with the social tenants in six regions of the UK that received limited subsidy in 2004 still receiving limited subsidy in 2010.

Table 8: Rental subsidies to social housing tenants[82]

Region(s)	Total subsidy for all these regions in 2004	Weekly subsidy per household in 2004
London	£3 billion	£70-80
East and South East	£1.6 billion	£25-45
North-East, North-West, South-West, East Midlands, West Midlands, Yorks and Humberside	£2 billion	£10-20

Often the subsidies social tenants receive are incorrectly judged as being higher than they actually are, as the average private rent at £595 a month is a lot more than the average social rent at around £296.[83] This ignores the fact social renters' properties are less valuable than private renters' propertes. In fact, in most regions of the UK social tenants' subsidy is noticeable but not huge.

Households moving into and living in social housing have poor social outcomes

The economic status of those moving into social housing is poor. The economically inactive of working age (those job-seeking while on benefits, those not seeking work and those unable to work due to sickness or disability) make up around 55% of all those moving into a social tenancy.

Table 9: Economic status of households moving into/within social housing sector[84]

	Total	Total %
Working full-time *(30+ hours a week)*	52,394	23.8
Working part-time *(less than 30 hours a week)*	18,852	8.6
Govt training/New Deal	526	0.2
Jobseeking	33,949	15.4
Retired	24,558	11.2
Home/not seeking work (mainly single parents)*	54,712	24.8
Student	3,114	1.4
Unable to work due to sickness or disability	28,574	13.0
Other adult (over 16)	3,545	1.6
TOTAL	**220,224**	**100**
Not available	*30,098*	

* Single parents made up 23.5% of new tenants in 2007/8 according to DCLG[85]

82 *The Hills Report into Social Housing*, ibid

83 *Chart 732; Rents, lettings and tenancies, average rents for free market private, council, and housing association tenants*, DCLG, available on their website

84 *Table 752; General needs social lettings 2007/8 England, economic status of household reference person*, DCLG, available on their website

85 *Table 750; General needs letting by RSL and LA landlords, household type*, DCLG, available on their website

Social tenants not only enter social housing with poor employment rates, but continue with them. 31% of social tenants are in retired households, 33% of social households have at least one member of the household in work while 35% of households are unemployed or otherwise economically inactive.[86] This gives an employment rate for social households of around 46% – meaning over 50% of social tenants of working age are living in households where no one works. A key justification for the sub-market rents of social housing is that this would encourage social tenants to move into employment as they would keep more of their wages, but this is clearly not working.

The gap in employment between social tenants and private households is vast. For private households 11.63 million out of 13.02 million households of working age (excluding those taking early retirement) are economically active.[87] This gives an employment rate of 89% for those in private housing, (excluding early retirees). This contrasts with the employment rate of around 46% for social tenants – a basic gap in employment rates of over 40%.

Basic adjustments for disadvantage fail to remove most of this gap

But what really demonstrates the failure of social housing is not that social tenants have poorer employment (or other social) outcomes than private tenants, but that their social and economic outcomes are *much worse than similar groups outside of social housing*. For example the rate of employment for lone parents is 64%, but for lone parents that are social tenants it is 34%. For unqualified individuals it is 70%, but for unqualified social tenants it is 43%.

Table 10: Employment rates for individuals within different tenures and groups[88]

Individual is…	Disabled	Lone parent	An unqualified worker
in social housing	40%	35%	43%
not in social housing	80%	64%	70%

Attempts to further account for the fact that social tenants may suffer multiple disadvantages again slightly reduce but leave most of this gap. As Figure 4 shows, social tenants with two market disadvantages (e.g. they are both unqualified and a single parent) have an employment rate of 30%, whilst across all tenures individuals with two market disadvantages have an employment rate of around 50%. Figure 4 taken from the Hills report shows a typical gap of around 20% in employment rates between social tenants and the average for 'all tenures'. In fact, the gap between private and social tenants will be closer to 25%, as the roughly 20% of households in social housing will substantially drag down the 'average' employment rate for 'all' tenants as social tenants have a much lower employment rate than private tenants.

This roughly 20-25% 'unexplainable gap' in employment rates between social tenants and privately housed households is often dismissed by defenders of social housing. After all, theoretically, as social housings' subsidised rents allow tenants to

86 *Table 803; Economic status of household by reference person*, DCLG, available on their website

87 *English Housing Survey 2008-9*, DCLG, 2010

88 *The Hills Report into Social Housing*, ibid

keep more of their earnings as disposable income it should act to raise the level of employment for social tenants, (helping to justify the subsidy of tenants' rents). Yet this is clearly not the case. As the Hills Reports noted, the evidence showed social housing appeared to lower employment rates for its tenants rather than have the expected positive effect of raising employment for its tenants. It stated "there are several potential explanations, either for such an effect being masked, or for there actually being a negative employment effect of social housing *per se*"[89].

Figure 4: % Employment rates for those with multiple disadvantages across different tenures[90]

However, some other defenders of social housing claim that social tenants are likely to suffer the worst disadvantage possible in each group (the most 'intense' disadvantage) and have hidden problems (e.g. depression) not picked up such analysis – and this explains the 'unexplainable gap'. There is certainly truth in this. But, defenders of social housing who make arguments about 'intensity of disadvantage' overlook the fact that while social housing is likely to house individuals with the most dehabiliating disadvantages, social tenants face substantial incentives to exaggerate dependencies and bars to employment, and this is a countervailing pressure that is likely to increase their recorded problems. To subscribe to the view that the 'unexplainable gap' is down to 'hidden factors' means believing less than one in two social tenants is capable of even part time employment.

Defenders of social housing also ignore countervailing points that this gap does not take account of. For instance, even excluding affluent early retirees, private households not in employment are more likely to be students, rather than in poverty or welfare reliant. For instance in January-March 2010, 2.3 million of the 8.1 million classed as economically inactive were students.[91] Students, who are largely housed privately, are not reliant on welfare in the way most economically inactive social tenants are. Thus broad comparisons between social tenants and private households/individuals' employment rates flatters the negative effects of social housing on employment because they compare dissimilar economically inactive but non-welfare reliant households/individuals in private tenure with economically inactive and welfare-reliant social tenant households and individuals.

89 *The Hills Report into Social Housing*, ibid

90 *The Hills Report into Social Housing*, ibid

91 *Labour Market Statistics May 2010*, Office for National Statistics, May 2010

Further strong evidence to back the view that social housing has a substantial negative impact on employment *per se* over and above the characteristics of its tenants is demonstrated by the fact that between 1994-2004 the proportion of social tenants in work who lost their job and remained unemployed was almost two and a half times the proportion of those across all tenures who lost their job and remained unemployed.[92] These individuals cannot be unemployable as they were indeed in work at some point – but when they lost their work they remained unemployed at a much higher rate than other individuals.

The welfare costs of lower employment caused by social housing are substantial

If we take forward the view that social tenants have around a 20% or so lower employment rate compared to similar private tenants this has a substantial cost in terms of welfare. There are around 2.75 million social tenant households of working age.[93] If their employment rate is 20% lower than private tenants, this means an extra 550,000 social households who are dependent on welfare.

The exact cost of each is hard to exactly calculate, but given that the lowest typical benefit, Jobseekers' Allowance (JSA), is £65 a week, and those on benefits in social housing will on average receive Housing Benefit of around £65-70 a week, and on top of that Council Tax benefit worth around £20 a week if they are receiving Council Tax benefit to cover a £1,000 Council Tax bill. This adds up to a weekly total of £150 a week for someone living alone on JSA and receiving housing and Council Tax benefit. This works out at around £7,800 a year.[94]

Of course, the actual level for almost all households on benefits is likely to be much higher than this, as incapacity benefit is around £25 a week higher than JSA, (£1,300 a year), many workless households have children, and therefore receive additional amounts (e.g. £56 per child per week for those on JSA, or £3,000 extra a year). Further, while few households receive less than £65 a week in Housing Benefit rent, many receive much more, (e.g. in London the average social tenant receives almost £30 a week more, £1,500 or so a year)." A reasonable estimate might be that the total cost to the Exchequer of each workless household on benefits is around £13,000 or so. This excludes benefits like Child Benefit that would be available regardless of employment status as well as any extra tax revenue these households would contribute. However, 550,000 x £13,000 gives the cost of extra welfare dependency due to social tenants' lower employment rates at around £7 billion a year – a very substantial sum. Note that this is a very cautious estimate that excludes any taxes on income and assumes an average of two adults or one adult and one child per economically inactive household.

Any reduction in welfare costs for social housing tenants outlined in this paper are thus not based on the naïve believe that social tenants' employment rates can rise from 50% to 90%, in line with privately renting/owner-occupier households. Existing social tenants do face and will continue to face greater difficulties in finding work. The most disadvantaged will often live in social housing. Yet the proportion of the gap in employment rates between social tenants and other tenures that should be able to be removed is substantial, perhaps around half. As we will examine further later, social housing is acting as a very serious poverty trap and it is this that explains the 'unexplainable' poor outcomes of social tenants. The alternative is to believe that an employment rate of 45% or so for social

92 *The Hills Report into Social Housing*, ibid

93 Subtract earlier figures for retired households from total number of social households

94 Reference for JSA rates, dependent children, and incapacity benefit from: *Social Security Benefit Up-rating*, DWP, 2010, available on their website.

tenants is morally and financially acceptable, and that 55% of social tenants will never be able to work. If the new government concludes this it will fail to improve the lives of social tenants and cut welfare dependency for these households.

Finally it is worth emphasising again that this is a conservative estimate on the low scale – £13,000 per welfare dependent household is likely to be an underestimate, while this excludes any increase in income tax and national insurance from such households moving into work.

Social housing increases child poverty, mental health issues, and inequality of opportunity and wealth

Social housings' failure is much wider than just low employment rates. Child poverty across the UK is twice as high for social tenants compared with other tenure types, (58% to 31%), strongly related to the poor employment rates of social tenants we saw.[95] 79% of children in a workless single parent family and 88% of children in a workless couple live in poverty.[96] Social tenants also have larger families, further increasing the numbers of children in poverty. In 2003/4 children in social housing made up 25% of all children, whilst social households only made up 18% of households.[97] The Joseph Rowntree Foundation found that 50% of children in families of four or more children are poor compared with only 23% in one-child families. Children in families with three or more constitute 42% of all poor children.[98] (This tendency for larger families is a key reason welfare costs caused by social tenants' low employment rates may be higher than estimated above).

"On top of the inequality of opportunity and poverty that arises from tenants' poor employment rates, social housing contributes to wealth inequality – an even greater problem in the UK than income inequality"

Though the effects are getting worse, social housing has always damaged equality of opportunity. Studies show those born in 1958 and 1970 who grew up partially or exclusively in social housing have done significantly worse than otherwise identical individuals, (adjusting for factors ranging from income to parental attitude to learning and so on,) across a host of factors: young parenthood, lack of qualifications, poor employment, unemployment, depression and social dysfunction, lower income, relying on benefits, early parenthood, homelessness and poor housing in general. The effects of social housing are also generally getting worse over time.[99] One study finds that for a child born in 1970, having a childhood spent largely or exclusively in social housing *doubled* the chances of women being unemployed at age 30. To quote one studies' abstract (my emphasis) "Academic test scores and *parental housing tenure* stand out as two of the strongest and most consistent correlates of adult disadvantage."[100]

On top of the inequality of opportunity and poverty that arises from tenants' poor employment rates, social housing contributes to wealth inequality – an even greater problem in the UK than income inequality. A report for the Government Equalities Office found that the median net wealth for social tenants in the UK was just £18,000. The total for those who owned their home outright was

95 *Poverty figures for London 2007/8*, GLA publication, 2009

96 *Child poverty in London: Income and labour market indicators*, GLA, 2006

97 *Households Below Average Income* 2003/4, DWP, 2005

98 *Child Poverty in Large Families*, Rowntree Foundation, 2006

99 *See The Public Value of Social Housing, a longitudinal analysis of the relationship between housing and life chances*, The Smith Institute, 2008, and Sigle-Rushton, *Intergenerational and life course transmission of social exclusion in the 1970 British Cohort Study*, LSE, 2004

100 *Intergenerational and life course transmission of social exclusion in the 1970 British Cohort Study* ibid

£411,000 with housing making up £210,000 – more than half. Because they were paying off equity, even mortgagors had an average property wealth alone of around £123,000.[101] As the report stated "*As the new figures for wealth distribution we present here show, inequality in housing wealth represent one of the starkest inequalities in Britain*." Greater home-ownership would thus have a substantial impact on reducing inequality in the UK.

On top of these 'hard' economic indicators, even softer quality of life indicators like depression and general health and well being are substantially worse for social tenants, even after adjusting for issues such as disadvantage and incapacity benefits.[102]

Social housing tenants largely rely on Housing Benefit to pay their rent

Further evidence of the dependency caused by social housing under the existing system comes from the fact that even in 2007, before the recession began, 63% of social housing tenants in housing associations were reliant on Housing Benefit to pay their (already subsidised) rent.[103] The last available figure from the same source for local authority tenants was 68%, giving a rough average of 66% for all social tenants. In 2007 just 20% of households who rented privately received Housing Benefit, down from 31% in 1996,[104] (though the numbers privately renting on Housing Benefit will have risen in the recession, this is likely to fall back again as it did during the previous boom).

If roughly two thirds of social tenants relied on Housing Benefit in 2007, the last year with all relevant figures available, this would mean approximately 2.5 million out of a total of 3.87 million social tenants relied on Housing Benefit. With an average social rent of £68 a week or £3,536 a year,[105] Housing Benefit for those in social housing cost around £8.9 billion in 2007. Since in 2007/8 Housing Benefit cost £15.7 billion,[106] this means that year roughly £6.8 billion went on Housing Benefit for private renters, (including those in temporary accommodation). Housing Benefit has since risen to around £20 billion in 2009/10. Since the majority of this rise will have gone to private renters in the recession (as social tenants' welfare dependency was so high it is unlikely to rise as steeply, and each new private Housing Benefit claim will generally be more costly than each new social Housing Benefit claim), we can plausibly assume the £20 billion spend currently splits roughly equally between social and private tenants – £10 billion to each. Thus social tenants cost £10 billion in Housing Benefit in 2009/10, with half leaving government to go to housing associations. This is a substantial cost to government.

Additionally, there is the cost of future Housing Benefit payments to cover the rent of retired social tenants. Almost all the 2.75 million working age households in social housing will look to the State to provide for them in retirement. As the average social tenancies' rent was £68 a week by 2008 or £3,640 a year, this gives us a figure of £10 billion a year for all these households claiming in a particular year. Assuming that each household will require rent for an average of twelve years gives us a figure of £120 billion – and spread out perhaps over 40 years or so as tenants retire over time, this gives a likely cost of around £3 billion a year in the future.

101 *An Anatomy of Economic Inequality in the UK*, Government Equalities Office, 2010

102 S Macintyre et al, *Do housing tenure and car access predict health because they are simply markers of income or self esteem?* Journal of Epidemiol Community Health, Volume 10 (pp657-64), 1998 and S Macintyre et al, *Housing tenure and car access: further exploration of the nature of their relations with health in a UK setting*, Journal of Epidemiol Community Health, Volume 55 (pp330-331), 2001

103 *Table 718; Average Housing Benefit support*, DCLG, available on their website

104 *Table 718; Average Housing Benefit support*, ibid

105 *Table 718; Average Housing Benefit support*, ibid

106 *Table 3; Benefit expenditure, Great Britain, 1991/2 to 2009/10*, (nominal terms), DWP, available at their website

Social housing policy is an expensive subsidy for failure at £32 billion a year

Adding up the immediate costs of government support for the failing social housing system comes to around £32 billion a year. Building and maintaining social housing (£8.6 billion), subsidising rents (£6.6 billion), Housing Benefit for social renters (£10 billion), and additional welfare costs due to social tenants' low employment rates (£7 billion). This £32 billion is supporting a system that most in it want to leave and increases poverty whilst widening inequalities of opportunity and wealth. Urgent reform is necessary – once we understand why social housing is failing its tenants so badly.

Ending security of tenure would be a mistake

There have recently been suggestions that government should end security of tenure for new tenants. The idea that this will be a solution (or even come close) to the problems in social housing is a mistake. Since most tenants who are occupying bigger homes than they need are elderly couples or individuals whose family have left, reducing this total of elderly over-occupiers via this change for new tenants would take decades to feed through into supply.

For younger tenants, since it would be a review every few years, this would also fail to tackle the real issue at the root of their problems – the incentives facing social tenants who are trapped in their sector by high private housing costs. To further distort these incentives by telling social tenants who return to work or move to a better job that they will have to give up their home is to further compound existing problems. The government should quietly drop this idea once the official consultation is completed.

In terms of those who pass on their homes to their children, the rules governing this are actually quite strict. The idea is that this prevents a tenant's spouse, long-term partner, or children who have moved in to support parents as carers from being evicted the moment that the original tenant dies. To change this to require such individuals to vacate their home once the original tenant dies would be difficult to implement in a sensitive way, so this paper proposes to leave the existing rules as they are. In any case, only one such 'transfer' is allowed, preventing unscrupulous families manipulating these rules so that they can keep passing their social tenancy on through their family.

4
Why Social Housing is Failing

Current proposed solutions are often based on weak evidence

Despite weak supporting evidence, certain misconceptions are deeply ingrained in the thinking around this area. These need to be tackled head on.

1. Government-created 'mixed communities' do not solve the problems of social housing

The first argument is that social housing's problems are down to 'area effects' of clustering social tenants together. Therefore we can solve social housing tenants' problems and low employment rates by building or creating mixed communities which disperse social tenants. But while on an anecdotal level this has had some moderate successes, as a large scale solution it has not. Government mixed communities are often just parallel communities side by side. A major study of various planned mixed communities found only 4% would ask a tenant from another tenure for help finding a job.[107] Another separate study found that social households focused upon their estate in their social interaction in a way home-owners did not, limiting cross-tenure social interaction and positive benefits from this.[108]

Employment in these mixed communities is not particularly higher. An LSE study of mixed tenure areas found in Edinburgh "despite significant tenure diversification in Niddrie in Edinburgh … joblessness amongst social sector tenants is, if anything, higher". Examining a series of other studies it concluded, "available evidence suggests effects are not strong, and there are some negative effects. The evidence does not justify promotion of mixed tenure and tenure mixing".[109] The DWP has itself stated in a report on worklessness amongst social tenants that "A key conclusion which emerges from the research is that area effects are an insignificant part of the explanation for the high rates of worklessness found amongst social tenants."[110] In other words, the theory that the area and surroundings facing tenants was important is simply not true. But the DCLG and other stakeholders have continued to promote this as a solution.

Further, tenants in these government created mixed communities often suffered low levels of satisfaction. One survey across ten mixed estates found satisfaction with the estates was *lower* for *all* tenure types than the national average. This was particularly surprising for social housing residents, who on the mixed estates had a net satisfaction of +50 compared with a national average of +57 – itself the lowest of any group of tenants.[111]

Unlike home-ownership, most people don't care about living in mixed communities. One poll found 25% thought a mixed community a 'good' thing, a

107 B. Jupp, *Living Together, Community Life on Mixed Tenure Estates*, Demos, 2000

108 R. Atkinson and K. Kintrea, *Reconnecting Excluded Communities: The neighbourhood impacts of owner occupation*, Scottish homes research report, 1998

109 R. Tunstall, *The promotion of mixed tenure: in search of the evidence base*, paper presented at the Housing Studies Association Conference, York, Spring 2002

110 *Social Housing and Worklessness: Qualitative research findings*, DWP, 2008

111 *Living Together, Community Life on Mixed Tenure Estates*, ibid

further 25% thought it was a 'bad' thing, while the remaining 50% were ambivalent.[112] The educated and affluent were the most in favour of it. Prioritising it over home-ownership is to ignore what low income households want.

This argument gains strength as it is often used as a stick with which to beat Right to Buy. It is often argued that prior to the 1980s, social housing estates were 'mixed' but that better off tenants then bought their properties and moved out, and thus the Right to Buy destroyed 'mixed communities'. This view is not backed by the evidence. Firstly, the more affluent tenants who bought under Right to Buy were disproportionately located in the suburban housing estates, meaning real mixing was limited, as the Hills Report details.[113] Affluent tenants were substantially segregated in geographical terms even before Right to Buy came into operation. Secondly, tenants who bought homes did not suddenly vanish. They remained in their home and community. The Right to Buy did not destroy communities – indeed, by offering a discount to tenants in their existing homes, it allowed more affluent tenants to stay in their home rather than have to move out of their area if they wanted to move into home-ownership.

2. The location or mobility of tenants cannot be what is impeding employment

An argument related to 'mixed communities' is that social tenants do poorly because they are located in 'the wrong areas'. In 2001 the Inner London boroughs of Islington, Tower Hamlets, Hackney and Southwark had the four highest concentrations of social households in the UK. These areas are located next door to the City, and the social housing tenants in these areas have much greater employment opportunities than almost anyone else in the UK. If the location of social housing away from jobs, (and by extension lack of mobility within the social housing sector), is the key problem facing social tenants, these areas would contain 'successful' social housing sectors with high levels of employment for their tenants. With that in mind, Table 11 shows figures for each borough's total numbers in social housing, their employment rates and the numbers of jobs within each borough and neighbouring City of London.

Table 11: Social housing and employment figures for certain Inner London boroughs

	% of households in social housing in the borough[114]	2008 borough employment rate as a %[115]	Numbers of jobs in borough & City of London, & ratio of jobs to workless adults in borough[116]
Tower Hamlets	52	53	469,000 (14:1)
Hackney	50	59	386,000 (15:1)
Islington	49	66	450,000 (14:1)
Southwark	53	65	454,000 (14:1)

As can be seen the mere proximity of jobs, many low skill or entry level, does nothing to lift employment rates that are amongst the worst in the country. These areas are polarised between very affluent private housing and some of the poorest people in the UK, largely locked into social housing. The boroughs of Islington, Hackney and Tower Hamlets were ranked in the top ten most deprived districts of

112 *Living Together, Community Life on Mixed Tenure Estates*, ibid

113 *The Hills Report into Social Housing*, ibid

114 *Table KS18 Tenure, Key Statistics for Local Authorities in England and Wales, Census 2001*, ONS, available on their website.

115 *Focus on London 2008*, GLA, 2008

116 *Commuting in London*, GLA publication, 2007

England in 2004 and 2007 Government Indices of Deprivation in terms of the average rank scored. Hackney and Tower Hamlets came in the top 3 for deprivation both times.[117] This is despite the fact these Inner London areas contain very large numbers of affluent professionals (e.g. Islington in 2001 had the 10th highest number of people educated to degree level or above across all 376 local authorities in the UK, Southwark came 16th, Hackney 20th, Tower Hamlets 30th). The fact these areas contain a large and affluent upper-middle class makes the fact that these areas score as close to being the most deprived parts of the UK on average even worse.

In 2008 Hackney and Tower Hamlets, with almost half of their housing as social homes and favourable locations next to the City had two of the top three lowest employment rates in the whole of Great Britain.[118] Social tenants' location in Central London is, if anything increasing their deprivation as shown by a quote from a Greater London Authority publication, "of 376 local authority areas in England and Wales, the London boroughs of Tower Hamlets (46%), Islington (45%) and Hackney (41%) have the highest percentage of "children in benefits families".[119] Families living in social housing in Inner London are surrounded by available jobs but have no one earning a wage. It is worth again emphasising that the average results for these boroughs, the worst in the UK, are achieved despite a large affluent upper-middle class population in these areas.

Social housing is failing *everywhere*. But Inner London shows that location and by extension lack of mobility within social housing is not to blame for social tenants' poor outcomes. If tenants don't take jobs nearby even where they exist, moving tenants within the social housing sector cannot solve social tenants' poor employment rates. (This excludes where tenants are allowed extra mobility *in order* to take work. But this works through changing tenants' *incentives*, not just greater mobility in itself).

3. We cannot build our way out of current problems

A third argument is that we should build our way out of the problems of social housing. Some people argue if more lived in social housing or waiting lists were smaller, its problems wouldn't exist. But our social housing sector is much larger than most countries and it is still failing. It is difficult to see why if having a social housing sector twice as big as the EU average doesn't work, making it three times larger than the average would solve its problems. It seems true social tenants' disadvantage has worsened in recent years, but this is not related to the size of the sector.

4. Giving greater power to housing associations or 'local solutions' will fail

One view is that local government can simply be relied upon to resolve the problems of social housing – or that housing associations will be able to do this. Relying on this would be a mistake. Housing association tenants have low employment rates and are largely welfare dependent, like local government tenants. Housing associations are only feasible due to support from government (e.g. £8.4 billion to build new homes between 2008-11).[120] This is on top of most benefiting from a charitable status which helps reduce their tax liability.

117 *The English Indices of deprivation 2004 and The English Indices of deprivation 2007*, DCLG, available on their website

118 *Focus on London 2008*, ibid

119 *Child Poverty in London, Income and Labour Market Findings*, GLA, 2006

120 *Funding Affordable Housing – New Options for Housing Associations*, PWC, 2008

For many indicators there are not separate statistics captured on local authority and housing association residents (partly as social tenants often are confused as to which they are – itself indicating that while the labels change, the difficulties faced do not). However, on the key point of employment as we saw on earlier pages, there is no real difference between social tenants in housing associations and those in local authorities – the gap is roughly the same. This failure of social tenants to work is behind most other social problems and the driver of poverty and welfare reliance – and it applies to all social tenants. Relying on 'local solutions' will fail as if social housing is generally failing everywhere and regardless of whether tenants are in local authority or housing associations, then there must be a common cause for this failure. And this common cause is in fact the incentives that all social tenants face.

The especially poor outcomes of social tenants are related to the incentives they face

The reason for the gap in employment rates between social housing tenants and similar individuals outside of the social housing sector is primarily related to the incentives social tenants face. Social tenants face the typical poverty trap all low income households face but are also trapped in a housing system that penalises work and rewards welfare dependency.

Social housing will always require rationing due to sub-market rents

The biggest reason social housing is currently flawed is its allocation system. Social housing will always require rationing as the creation of sub-market rents creates demand in excess of supply. Rationing therefore requires a way of allocating social housing to those waiting for a social tenancy. The problem is that the current way of allocating social housing is a disaster.

Social housing in the last few decades has been allocated 'by need'

At the beginning and continuing well into the 20th century social housing was cheaper than the equivalent quality private rented accommodation, though more expensive than most (poorer quality) private accommodation. Generally, ability to pay rents was required through payment in advance, and prospective tenants were expected to show evidence of a job. Councils largely ensured that both the most affluent and least affluent were not given council homes (though tenants could see incomes rise without being penalised). The idea behind this was that council housing would be a 'reward' for the respectable working classes – a classical liberal concept of helping people to help themselves.[121] Finally, 'local connections' counted for a great deal when most councils allocated their stock of social housing.

This idea that council housing should be a 'reward' to the local and respectable working class lost ground across the political spectrum from the 1960s onward. The emphasis on 'local connections' and 'deserving rights' bypassed both the very

121 See, for example, *Working Class Housing in England between the Wars*, Olechnowicz, 1997

poorest and new migrants, and jarred with the new 'rights-based' language being taken up by many on the left. The Conservative party increasingly saw government support for home-ownership as a preferable incentive and, as this was more popular for those who could afford it, came to view council housing as a 'second best' compared with encouraging people to own.

The 1977 Housing (Homeless Persons) Act gave a legal underpinning to this shift away from social housing as a 'reward' and placed a statutory duty on councils to house those who could not house themselves. This required that priority should be given to those who were homeless or could become homeless, with further priority given to those who were sick, pregnant or had children, or were caring for someone who was sick. In practice, this meant those on benefits, or who looked like they might not be able to pay future private rents and thus faced homelessness, were prioritised over those who were working and looked like they could pay. This became called the 'needs-based' system – because it is based on the prioritisation of the needy, (or those who might in future become needy), over others – reversing the original idea behind social housing.

> "Requiring councils to prioritise those in need was done with good intentions. But its impact has been disastrous. In the real world, it has acted as an extremely sharp poverty trap"

Since the 1977 Housing Act, various other Housing Acts have tinkered with the statutory requirements on social housing. But none have reversed the essential enshrining of a legal requirement to allocate social housing to those in greatest need. Housing associations (excluding a few that have been in existence for decades) now largely use the same statutory framework when allocating their own housing as the government, meaning the whole social housing sector is using this needs-based framework instigated by the 1977 Housing Act.

This allocation of social housing 'by need' creates and sustains dependency

Requiring councils to prioritise those in need was done with good intentions. But its impact has been disastrous. In the real world, it has acted as an extremely sharp poverty trap. Welfare dependency is rewarded while independence from the state is penalised. Applicants' need is calculated through a 'points-based' system. For example, Islington Council will award an extra 20 points to a household if: "The applicant's household includes someone with a need for settled accommodation on welfare or medical grounds who cannot reasonably be expected to find accommodation for themselves in the near future".[122]

Bristol Council like most councils places those above low income workers where "An applicant and/or member of his/her household has a physical or mental health problem that is in part related to their current housing and could be helped by rehousing to a different type of accommodation or area." Or where "S/he or a member of his/her household needs to move to a particular locality in the City of Bristol, where failure to meet that need would cause hardship to themselves or to others."[123] In practice this means councils give priority to those who are disabled (usually incapacity benefit claimants), those with dependents

122 *Islington Allocation Policy 2005*, Islington Council, 2005

123 *Bristol City Council HomeChoice Council Housing Allocation Scheme*, Bristol City Council, 2009

(often single parents), and those who can legitimately claim difficulty in housing themselves (often those reliant on out-of-work benefits).

Thus, the reason that 55% of new social tenants live in economically inactive working age households is that the system pushes these households to the front of the queue. By contrast, those who work but are on low incomes are pushed to the back of the queue. A starker version of the welfare trap in action could not be imagined.

The attractions of a needs-based system are clear – it helps the vulnerable. But the allocation systems penalises low income workers who want social housing. Households where someone earns are likely to be scored lower than those that are reliant on benefit, (particularly incapacity benefit and single parent benefit). Put bluntly, if as a waiting applicant you move to incapacity benefit (for example), you will be able to get to the front of the queue for a social home. For many, particularly for those with few skills to start with, difficult backgrounds and/or low self-esteem, once they have been put onto benefits it is often hard for them to make a change and come off and back into work. A poverty trap has been sprung.

Further, tenants' future incentive to come off benefits is severely weakened as the prioritisation of the most needy is not just applied when people enter the system, but for tenants wanting to move within the system. For almost all councils, when tenants want to move house they reapply to the council to get a new home as 'transfer applicants' and go back on the waiting list. In 2006-7 71,000 such 'transfer applicant' households, (around 2% of all tenants) were rehoused.[124] Again, the system used to decide a tenants' place in the queue is 'needs-based' – so in practice the more reliant you are on benefits the more you are put to the front of the queue. The dependency that social housing creates is thus not just a 'one-off' but an ongoing problem.

Tenants know this is how the system works and will punish them if they need to 'trade up' within the system but become independent of the State. The more that you move off benefits as a household, the less likely you are to be able to be put to the front of the queue. For families who have children but could never afford private housing the best way to get a bigger home is to increase dependency, rather than reduce it – with dire consequences in terms of child poverty.

In addition, the incentive of improving/losing your own home no longer exists

In addition to the flawed allocation system, the second major problem with social housing is that the incentives and penalties that come with private housing don't apply to social housing tenants. Whilst many people aspire, over time, to move to a nicer house, (and if they work hard they may be able to), this aspiration doesn't exist for council tenants. Hard work cannot get a social tenant to a nicer home in the same way it does for private owners or renters.

Right to Buy did at least offer some tenants the possibility of purchasing their home and carrying out any desired home improvements on it. But the numbers have steadily dropped off as house prices rose while discounts for tenants were increasingly capped at low levels, (e.g. in the most extreme example, London, discounts are almost all set at a maximum of £16,000)[125] making

124 *Analysing Key Trends in the Supply and Distribution of Social Housing Lettings*, ibid

125 *Your right to buy your home*, DCLG, 2009

home-ownership for social tenants through Right to Buy increasingly unrealistic. Average annual Right to Buy sales in 2006-7, 2007-8 and 2008-9 were just 10,500 a year.[126] Until recently there was also the option of leaving the sector if tenants got a good enough job, allowing them to buy privately (or aspire to do so in the medium-term). But again rising rents and house prices have cut off this option. This closing off of options for social tenants is shown by the fact that the net private re-lets, (the number of social tenants leaving the sector and moving into private accommodation, meaning that their property could be re-let to new tenants,) dropped by over 100,000 a year from 1997-8 to 2006-7, as discussed earlier.

But while social tenants can not improve their housing situation through hard work, unlike private tenants, social tenants can also only rarely lose their home. If they lose their job and don't find another, they will not lose their house and their landlord will not kick them out. If they have more children it doesn't matter because they are more likely to be moved to a bigger house. This is not to say that tenants should be 'punished' but just to point out that social tenants both lack positive and negative incentives around housing and it is this, combined with bad allocation policies, that explains much of the 'unexplainable gap' in employment rates between social tenants and similar individuals outside the sector.

Housing is one of the key aspirations and determinants of quality of life. To face a situation where hard work cannot get you a better house or let you buy your home, but where you are often penalised for your efforts, (whilst increasing your dependence on the State helps you move to a better social property) is ludicrous. But this is the system social tenants are in – on top of what are often effectively 60-70%+ 'participation tax rates' for low income workers due to the interaction of the tax and benefit system. Given all these perverse incentives what is surprising is not how *few* social tenants work but how *many* do.

Social housing in affluent areas distorts incentives the most and has the worst effects

Under the analysis above, which places the incentives that social households face at the root of their problems, the more social housing is located in more affluent areas, the greater the poverty it will cause, (all other things being equal). If an area is becoming gentrified the worse thing to do in terms of creating future poverty is to increase the social housing element in an area.

For this will not stop private house prices and rental costs rising as wealthy households move into an area – what happens is private and social housing costs will diverge. As low income households face rising private housing costs, increasingly the only way to get a (decent) home is to become a social tenant and move within this system. The problem is that more and more of your local community will be trying to do the same as higher housing costs push them out of private housing. So to obtain a social property you need to move up the allocation system. This then leads to a vicious circle, where as the area becomes more expensive, then in order to obtain social housing then the incentive toward state dependence caused by social housing increases, and poverty rises further and further.

126 *Table 643; Social Housing Sales: Financial data on local authority homes sold through right to buy, by region*, DCLG, available at their website

This is confirmed when we look at Inner London, so exceptionally deprived in terms of low employment rates, child poverty etc. despite tenants there being surrounded by job opportunities. For it is in Inner London boroughs that the gap between private housing costs and social housing costs is most pronounced. The average property price in Tower Hamlets, for instance, is £342,000, thirty-four times what a full time minimum wage job pays.[127] Welfare dependence in such areas acts as a way of obtaining, keeping, and moving within social housing – which given sky high private housing costs, the instability of private renting, and the fact many landlords will not rent to Housing Benefit claimants, is the only way that many can obtain a decent and secure home. This also helps explain why Inner London with its huge social housing sector has the worst levels of 'children-in-benefits' families in the country. In Inner London, the best way to get a permanent and stable family home is to move onto benefits and then try to work your way up the social housing system. This also helps explain why it is in London, where the additional poverty trap effects of social housing are strongest, that welfare-to-work has failed the most. As the most recent Mayor's Economic Development Strategy bluntly puts it "London's labour market performance, measured by the employment rate, is one of the worst in the UK…Welfare to Work programmes have tended to be less successful in London than nationally".[128]

This is one reason why prioritising government created 'mixed communities' above other goals is dangerous. For in Inner London, where the goal of 'mixed communities' through large scale social housing projects has been realised, this is not causing higher employment and lower poverty, but *reducing* employment and thereby *increasing* poverty.

Social housing acts as a block to welfare-to-work success in general

Social housing acts as a block to welfare-to-work programmes in general. The current total on out-of-work benefits numbered around 5.1 million in the fourth quarter of 2007 – barely down from 1999, when it was been 5.4 million. In eight years of economic boom, the total drop was just 300,000. Of this, 150,000 was due to the fall in 'widow's benefit', paid to women of working age whose husband has died – a fall mainly linked to longevity.[129] Even a booming economy was not absorbing these long-term welfare dependent individuals.

Social tenants are particularly trapped on out-of-work benefits, as we have explored. The skewed incentives of social housing must be reduced if welfare reform is to fully succeed. This requires an overhaul of social housing so that it helps, not hinders, individuals back into employment. Without tackling a system that still houses almost one in five people in the UK, and impacts on another 1.8 million households on the waiting list, welfare-to-work reforms will struggle to succeed.

People believe that the current social housing allocation system is unfair

Despite the party political consensus on social housing allocation, most people do not currently believe that our current system of social housing allocation is fair, as shown by polling work done by the DCLG.[130]

127 *Land Registry House Price Index; March 2010*, Land Registry, 2010

128 *The Mayor's Economic Development Strategy for Greater London*, GLA, 2009

129 Figures from this paragraph from the *Work and Pensions Longitudinal Study*, DWP, available at their website, variables entered being dates (Q4 1999 and 2007), and totals on out-of-work benefits

130 *Attitudes to housing, Findings from IPSOS-Mori Public Affairs Monitor Omnibus*, DCLG, 2009

Of the general public 32% of people thought that the way social housing was allocated was not fair, while only 23% thought it was fair, a net balance of -9. But the more an individual knew about social housing allocation the more likely they were to say it was unfair. Of those individuals who knew 'a lot' about how social housing was allocated, 32% said they strongly disagreed it was fair, and another 32% said they disagreed it was fair, making this almost two thirds of respondents. Just 23% said it was fair, with only 4% strongly agreeing it was fair, (below those who did not express an opinion,). The group most positive about social housing allocation was the group which knew nothing about it, (though even in this group slightly more viewed it as unfair than fair).

Moreover, of those polled, 48% agreed that more low income working households should be allocated social housing over those with the greatest need. Only 19% disagreed, a net agreement of +29%. What is most startling is the strongest agreement was those who earned less than £9,500, or less than the minimum wage – who gave a net agreement of +39%. The more affluent households agreed, but agree less strongly.

More also agreed than disagreed with the statement that those who have lived in an area for a long time should be prioritised over those who have worse circumstances. 48% agreed, 30% disagreed – a net agreement of +18%. Low income individuals again were the most likely to agree with this, though in every income group more agreed than disagreed with this statement. Disagreement with the existing system is also shown by a 2008 Mori poll where the length of time on a waiting list was identified as the most important factor by the largest number of people when allocating social housing.[131]

The Hills Report also noted that many stakeholders in the sector also agreed that the existing way of allocating social housing was not working: "People argued that it is important to get allocations policy right… social housing cannot just be for the most vulnerable and needy".[132]

Social housing is a second best to rising home-ownership

Despite the many problems explored above, social housing has a role to play in the future of housing policy. But rising home-ownership should still be the focus of government, both because it is less expensive for government and as it is what the public want. However, rising home-ownership will only return if government policy addresses the reasons behind sharply rising house prices – to which issue we now turn.

131 *Ipsos MORI housing survey shows support for Housing Minister proposals on social housing*, Ipsos-Mori, available on their website

132 *The Hills Report into Social Housing,* ibid

5

Why Housing Costs and House Prices are Rising

Earlier in this paper it was outlined how rents are linked to house prices. The recent rapid rise in rents in recent years is ultimately caused by higher house prices. Therefore while this section focuses on house prices rather than rents when discussing housing costs rising in recent years, this is also shorthand for higher rents. If the causes behind rising house prices are tackled, this will also reduce rent increases down to a more manageable level.

Before discussing the causes of the UK's rising house prices it is important to explore two points. Firstly, the UK's house price rises in recent years were far higher than in other countries and the fall in prices smaller. Secondly, it is important to briefly explore those reasons which are often put forward to explain the UK's house price rises, but have limited evidence behind them.

UK house prices rose faster and for longer and have fallen less than in other nations

The UK's house price rises in recent years were exceptionally high. Between 1995 and 2006 house prices in the UK rose by 133% in real terms, ahead of everywhere in the developed world except Ireland.[133] This high growth was despite the fact we have had higher interest rates than many developed nations – making mortgages more expensive. But not only did our house prices rise further, house price falls in the UK since 2007 have been smaller than other countries – for example, Standard and Poor's house price indexes of 10 and 20 US cities dropped 30% between their peak and January 2010, after a period when they slightly more than doubled in nominal terms since the mid-1990s,[134] compared with a fall of just 12% in the UK,[135] after our tripling of house prices. Indeed, in 2009 UK house prices rose – in the middle of the biggest recession since World War 2. We have not just been part of a general international bubble.

The UK's above average rise is part of a long-term pattern. The Barker Review of Housing Supply found the UK's real term house prices rose at 2.7% per year between 1971-2001 – over twice as high as the European average of just 1.1%.[136] While housing unaffordability in the UK has reached a critical point in recent years, it is a problem that has been growing for some time. Even if in the next few years house prices fell by 10% or even 20%, they will still be at record highs and unaffordable for the vast majority. Moreover, short-term decline is likely to

133 K-H. Kim & B. Renaud, *The Global House Price Boom and its Unwinding,* Housing Studies, Volume 24, (pp 7-24), 2009

134 *S&P/Case-Shiller 20-city index*, Standard and Poor's, available on their website

135 *UK House prices since 1952,* ibid

136 Kate Barker, *Review of Housing Supply, HMT, 2004*

be followed by a resumption of what has been a relentless long-term rise. Politicians must not mistake any 'correction' over the next few years for the idea house prices will resolve themselves out as an issue.

Net immigration has had an impact on housing demand – but this has been modest

Some argue that the main reason house prices have risen so fast is the level of net migration into the UK. Net migration added 147,000 a year to the UK population between 2001-2008.[137] The government's own figures show this means an extra 82,500 households per year.[138] This has obviously had an impact on house prices. However, it is less than is often supposed. The House of Lords Report *The Economic Impact of Immigration* estimated the impact of current immigration on house prices, and found house prices at their peak would likely have been around 7% lower but for recent migration.[139] A drop of 7% from the 2007 house price peak would not have made houses affordable, and though it would have meant homes costing around £10,000 or so less then they would still have risen hugely, to beyond the reach of most households. The report estimated that in twenty years house prices would be another 13% higher than they would otherwise be if net inward migration continues at the current rate. Blaming immigration for the troubles of the housing sector is to make a small part of the problem into its main cause.

In terms of social housing, only around 7% of social homes went to those who were not UK nationals.[140] While it is true that social housing has been seen as failing to support existing and longstanding working class communities, (e.g. in the East End) this has been a long ongoing process and is more related to the "needs-based" criteria than immigration *per se*, (e.g. in the East End larger Bangladeshi/Pakistani families, where women are less likely to work, are more likely to be 'needy' than others.) If social housing only went to UK nationals, the waiting list would be 1.6 not 1.8 million. Immigration is an issue in housing, but a modest one.

The UK housing market's problems are not primarily caused by unsustainable lending

While the UK has higher levels of mortgage debt than most, it has *always* had higher levels of mortgage debt than most. If anything, the UK has moved closer to, not further from the average when compared with the mortgage debt outstanding internationally since 1983.[141]

The UK's rise in mortgage debt between 1990 and 2006 is lower than many other countries that more than doubled their levels of mortgage debt to GDP, a key borrowing measure (Australia, Denmark, Ireland, Spain, the US, the Netherlands, Italy).

Since, as we saw earlier, between 2000-2009 the proportion of mortgages for first time buyers fell to 35% from 50% in the previous 1990-99 period, banks have clearly not been lending to new, more risky households. Lending in the UK can hardly be unsustainable and reckless when fewer people can get a mortgage than they could in previous decades. Banks were more and more lending to existing owner-occupiers changing properties or withdrawing equity. Even if in other

137 *International Passenger Survey estimates of long-term migration*, ONS, 2009

138 *Adopted from New projections of households for England and the regions,* DCLG, 2007

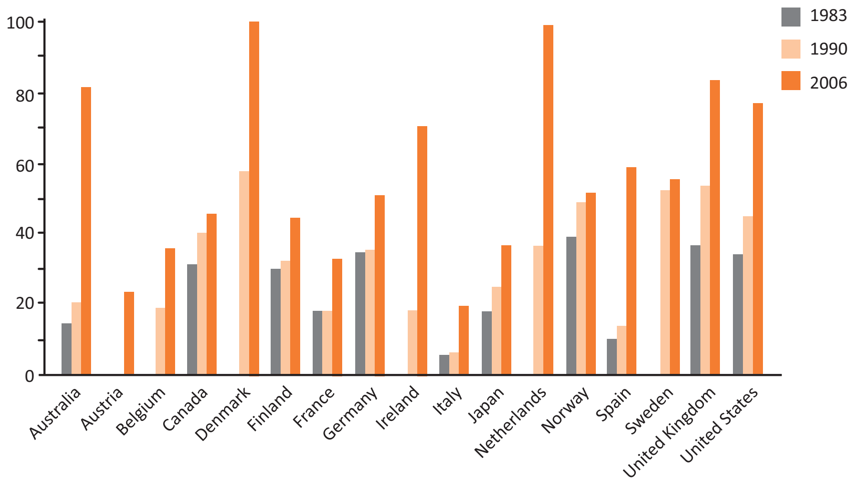
139 *The Economic Impact of Immigration, House of Lords*, HMSO, 2008

140 *New immigrants and migrants in social housing in England,* Local Government Association, 2008,

141 *The World Economic Outlook, Housing and the Business Cycle*, IMF, 2008

countries, like the USA, lending was too relaxed in terms of allowing those with a poor credit history to take out sums that they could not afford, this was not the case here. In the UK, large mortgages are more of a *reaction* to high house prices than driving them. First time buyers do not dream of a huge mortgage, but usually it is the only way they can get onto the bottom rung of the housing ladder.

Figure 5: Mortgage debt outstanding (percent of GDP)



Further, those who argue for more restrictions on mortgages ignores the fact too many restrictions are likely to lead to households extending non-mortgage debt, taking out the maximum they can, and engaging in other risky behaviour. Limiting large loan-to-value and loan-to-income mortgages is necessary but only part of the solution to high house prices.

Meanwhile clamping down on buy-to-let mortgages might increase the numbers of houses for sale, but it will also reduce supply of rental properties and so push up costs. This means that those saving for a 10-20% deposit might need a few thousand pounds less, but rents will rise, putting most households back exactly where they started.

Internal population change is not the cause of rising prices

Aside from immigration, UK demographics are unlikely to be having an impact in causing rising prices. Between 1971 and 1991 average household size fell from 2.84 to 2.45 people while house prices barely rose in real terms. Between 1991 and 2011 household size is predicted to fall from 2.45 to 2.28 people, or half as fast as previously. Thus shrinking households cannot be the cause of the recent sharp rise in prices – because the impact of this factor is diminishing over time.[142]

Internal population growth (i.e. excluding migration) between 2001 and 2031 is predicted to be around 3 million, the same level of growth as between 1971 and 2001, so neither can this be to blame for house prices' recent steep rise.[143]

142 *Economic and Labour Market Review*, August 2009, ONS, 2009

143 *Economic and Labour Market Review*, ibid

There is no house price to earnings ratio house prices will 'trend back' to

House prices over the 1980-2000 period did tend towards a range of around 3.5 to 4 times earnings, but there is nothing to say that this will continue in the future. Moreover, this has not been the case now since around 2000 and there is nothing to demonstrate house prices will automatically fall back to this level. The idea of a fixed ratio that many buy into is reassuring as it means recent house prices are the result of a 'bubble' that will soon deflate back to a 'natural' relationship between house prices and earnings. But such a fixed ratio would require all the variables that explain house prices, (supply of new housing, supply of other housing coming up for sale, demand for living space, household numbers through demographic change and net migration, mortgage availability, income devoted to housing etc), to constantly balance around a set point. This balancing act simply does not happen.

This belief that house prices would inevitably trend down has had a paralysing impact in terms of halting action to bring house prices down to a more reasonable level. It is crucial that politicians understand that for house prices to stop rising sharply they must change policies.

Building 'low-cost' homes can't make housing affordable

An unhelpful theme in recent policy was attempts to offset rising house prices by increasing the proportion of low-cost properties in the new homes coming onto the market. This led to central government requiring or pushing for local/regional plans to include targets on 'densification' (houses per hectare) and a higher number of affordable/low-cost homes in each development. This means that the developments least likely to be approved were those at the middle and top end of the market, particularly larger, more expensive family homes, while smaller flats for a mix of incomes were the most likely to be approved.

This is based on the theory the UK housing market is split into segments, and supplying the bottom of the market will be most helpful in lowering prices for low income/ first time buyers. However, the theory supplying new homes at one part of the market in particular will help with housing affordability is simply wrong. The different parts of the housing market maintain their value against each other over time. Table 12 shows the median (average) and lower quartile house price, (the point halfway between zero and the average,) since 1996 and the % increase in house prices between 1996 and that year.

144 *From Tables 582, 583, and 1000*, DCLG, available on their website (full citations elsewhere)

Table 12: Median and lower quartile house prices in the second quarter for 1996-2009[144]

	1996	1997	1998	1999	2000	2001	2002	2003	2004	2005	2006	2007	2008	2009
ENGLAND lower quartile price (£ 000s)	40	43	46	49	54	59	69	81	104	112	120	127	122	121
% Rise since 1996	*N/A*	*7.5*	*15.0*	*22.5*	*35.0*	*47.5*	*72.5*	*102*	*160*	*180*	*200*	*217*	*205*	*202*
ENGLAND median price (£ 000s)	57	60	66	72	82	91	110	127	150	157	165	176	172	168
% Rise since 1996	*N/A*	*5.2*	*15.7*	*26.3*	*43.8*	*59.6*	*92.9*	*122*	*163*	*175*	*189*	*208*	*201*	*194*

Between 1996 and 2009 lower quartile and median house prices rose largely in tandem. Lower quartile prices rose by 202% from 1996 to 2009. Median prices rose by 194% over the same period. This gap means that median prices rose at 96% of the rate of lower quartile prices. Lower quartile prices actually rose slightly higher than the median. This was during a period when theoretically, the government's programme was holding down lower quartile prices by increasing supply of low-cost homes so as to increase home-ownership. This attempt to influence house prices through changing the constitution of new stock was clearly failing.

This is because houses in different sectors of the market are 'substitute goods' – if the price for one part of the housing market shifts, this has an impact on prices in the other sectors of the market. When supply expands in one section of the market, prices fall in this section relative to other parts of the market. This pulls in demand from other sections of the market, lowering the prices in the other parts of the market as their supply remains the same. This readjustment continues until the relative value of the houses is restored to roughly where it was before supply increased. There might be short-term fluctuations, but these will not change the long-term ratios between different parts of the property market. It is a fallacy to assume making new homes 'low-cost' will help increase affordability – it makes no difference to house prices whether you build cheap or expensive new homes.

Building affordable housing has been a fig-leaf not a real solution

So ensuring new homes are 'low-cost' is not the way to increase home-ownership. Neither is one of the major solutions championed by all political parties – the building of heavily subsidised (and very expensive) 'affordable homes'. As noted earlier, affordable housing made up just 2.5% of all house purchases in 2007 and 0.1% of all households in the UK. Between 2000-1 and 2007-8, the number of affordable houses built almost quadrupled from around 6,000 to 24,000,[145] while lower quartile house prices more than doubled. Thus this 'solution' had no real impact on reducing house prices or dealing with issues of housing affordability. Its current main purpose is to provide a fig-leaf that allows government to ignore the causes of rising housing costs and demonstrate it is 'doing something'.

The key reason affordability is deteriorating is because too few new homes are being built

The key reason housing affordability has deteriorated is the consistently low level of new homes coming onto the market. Aside from the Barker Review and recommendations, which unfortunately failed to increase the numbers of new homes, the previous government did not consider enough how a falling supply of new homes might impact on the UK. The decade between 2000-2009 saw talk but very little in terms of results – with the average number of new homes running at around 162,000 a year – even fewer than in the 1990-99 period.

145 *Table 1000; Additional affordable homes provided by type of scheme*, ibid

Housing supply has fallen consistently from the 1960s onwards, when it averaged 362,000 new dwellings a year, as Table 13 shows. It now runs at 160,000 new homes every year, around 200,000 fewer homes per year, every year, than forty odd years ago. To put this into context the reduction in new supply of homes since the 1960s for just one year is nearly equal the *entire* stock of 235,000 second homes in the UK.[146] If supply ran at 1960s levels we would have more than the entire 762,000 empty homes estimated to exist across the whole of the UK in just four years (and more than all the long-term empty homes (350,000) in just two).[147]

Table 13: Average new dwellings completed per year in each decade[148]

1960s	361,885
1970s	314,343
1980s	217,498
1990s	189,776
2000s	162,275

In 2007, at the peak of the current and unprecedented housing boom, just 174,000 new dwellings were completed[149] – a total that would have been the fifth lowest year in terms of new homes between 1950-90. Even a huge house price boom was having almost no effect on increasing the supply of new houses. Moreover, more of these new homes were small flats, making the rise in housing supply even smaller than it first appears.

However, while our problems have got worse in recent years, the UK has been building too few homes since at least the 1980s if viewed in an international perspective. In terms of new dwellings per 1,000 households among the EU15, the UK was third from bottom in 1985, third from bottom in 1995 and second from bottom in 2002.[150] The UK has been failing to provide enough new homes for decades now.

The UK's limited supply of new homes has had a major impact on affordability

It is this limited supply of new homes that the UK has seen in recent decades that has helped push up UK house prices higher than in almost any other country. Kate Barker's review showed that between 1971 and 2001 UK house prices rose rapidly compared with most European economies – unsurprising given we were building fewer new homes than almost any other country in this period. The Barker review also stated that to reduce house price rises to the real terms EU average of just 1.1% required an extra 145,000 homes a year, while to reduce this to 0% would require an additional 240,000 new dwellings each year.[151]

A 2005 DCLG report on housing supply argues that given relevant elasticities, 100,000 extra homes a year lowers prices by 12-14% over a decade.[152] Extrapolating backwards, if supply had run at 1960's levels since 1980, (around 175,000 extra dwellings a year) then real term house prices would have risen by

146 *English Housing Survey 2005/6*, DCLG, 2007

147 Based on figures from *The Empty Homes Agency* website, a charity focused on the issue of empty homes, http://www.emptyhomes.com/whatwedo/campaign_agenda.html

148 From *Table 244; House Building, permanent dwellings completed*, ibid

149 *Table 244; House Building, permanent dwellings completed*, ibid

150 *Housing Statistics in the EU*, ibid

151 Kate Barker, *Review of Housing Supply*, HMT, 2004

152 *Affordability Targets: Implications for Housing Supply*, DCLG, 2005

60-70% less than they did, so from £75-80,000 to just £104-110,000 rather than to £160,000. This would have brought the UK's experience of rising prices close to that seen in other countries which did build more homes. As basic economics would predict and research confirms, housing supply is crucial in determining house prices.

We need new homes for the next generation as older households no longer downsize

Of course, given that the UK's population is only growing slowly and household size is falling slower than it did in previous decades, some would argue that this shortage of new homes in recent decades should be less of a problem since we have roughly the same numbers living in roughly the same number of houses.

The problem with this argument is that it ignores the crucial point about *who* is living in *which* homes. Those who have moved into home-ownership before house prices shot up are increasingly living in homes with many spare bedrooms. We saw earlier how the under 50s hold just 18% of the UK's housing wealth, while wealthier older generations (mainly owner-occupiers), now live in homes larger than previous generations did, and do so for longer thanks to rising life expectancy. According to government figures in 2008-9, around 7.8 million households of the total 22 million households in the UK, (35% or so) were 'under-occupiers', with at least two or more empty bedrooms in their home. Another 36% had one spare bedroom. These under-occupiers are often affluent couples continuing to live in their family homes for decades after their family has moved out – 47% of owner-occupiers are 'under-occupiers' with two or more spare bedrooms, compared with just 11% of social tenants. Only 16% of owner-occupiers have homes where all the bedrooms are in regular use.[153] Thus, the older generation live in large family homes (which they have usually paid the mortgage off for), while the younger generation struggle to obtain a decent sized property to live in.

This is not to condemn the elderly for living in homes they have worked hard for. But what it means is the generation in their 20s and 30s are now facing a severe shortage of family sized homes. Owner-occupiers are remaining in their existing, larger homes, but few new homes are entering the market. Other countries are adjusting to this demographic change by building more homes even though their population is rising, (like the UK's) at a historically slow rate. The UK is not building more homes – and it is this lack of new homes combined with many people living in larger homes that contain empty bedrooms which is driving the UK's high house prices.

The lack of new homes is largely due to too little land being released for housing

The main reason we are building so few new homes is that in the UK the planning system rations land for development very tightly. The issue of development and planning is dealt with in substantial detail in other Policy Exchange papers, such as *Unaffordable Housing*, and *Better Homes, Greener Cities*.[154] Kate Barker's work also sets some of the issues out.[155]

153 *English Housing Survey 2008-9*, ibid

154 (This paper recommends these earlier papers for a full grasp of the issues).

155 See for example Kate Barker's *Review of Housing Supply*, HMT, 2004

However, to recap, the 1947 Town and Country Planning Act, particularly as amended by the 1990 Town and Country Planning Act, gives councils strong powers to halt development. Land with planning permission is therefore increasingly rare and costly – limiting development.

Since the 1990 Act land with planning permission has become even scarcer, as shown by the fact that between 1992 and 2002 a study found the proportion of a new home's cost made up from land rose from 15 to 34%.[156] Research by the Halifax indicates that between 1983 and 2003 residential land prices increased nine-fold whereas house prices increased 'only' four-fold.[157] Land therefore makes up a growing proportion of the cost of a new home.

In 2009, after the recent 'crash' in land values, a single hectare of land with residential planning permission costs £1.87 million (£2.47 million in the South East). An average hectare for industry costs around £600,000. The same hectare of land for farming costs around £16-17,000.[158] This very high rate for residential land was actually down from £3.16 million in 2007, at the peak of the boom.[159] Given average density for new homes is 43 dwellings per hectare, the land for each new property costs a staggering £45,000, (down from £60,000 in 2007).

Councils are not allowing enough land for development

The reason too little land is released for development is that local councils, who largely control planning matters, are not releasing it. In part this is due to the fact that the UK's local government structures strengthen NIMBYist tendencies – as we will see later. But while the 1980s and 1990s saw very low levels of new homes, the 2000s were even worse – even though house prices exploded. And this is because the framework for development in these years pushed for developments that local residents were least likely to support, which in turn discouraged councils from allowing development in their area.

The quality of new developments determines how they impact on existing residents

It might sound obvious, but the impact of a new development on existing residents is down to the nature of each new development. The Council for the Protection of Rural England's paper, *Planning for Affordability*, showed how new homes being built in an area often does not reduce local house prices. It showed a large amount of new homes could actually *raise* house prices in particular areas. The CPRE argued from this that in some areas "house building has failed to have any detectable impact on housing affordability".[160]

> To quote "*The evidence from the case study of Poundbury in West Dorset demonstrates that significant releases of land for housing can result in house prices rising locally rather than falling, where the development is of high quality... This finding is consistent too with Department for Communities and Local Government research, which found that 'land release may have a regenerative effect and hence increasing the supply of land could lead to house prices rising more quickly.*"[161]

However, the CPRE were failing to distinguish between regional and national versus local effects. While more homes in the UK lowers prices across the UK as

156 *UK Residential Research Bulletin*, Savills, 2003

157 *Residential Land Prices Significantly Outstrip House Price Growth*, Halifax February Research Release, 2003

158 *Property Market Report July 2009*, Valuation Office Agency, 2009 (three different sized land plots simply summed then divided by three)

159 *Property Market Report July 2009*, ibid

160 *Planning for Housing Affordability*, Council for the Protection of Rural England, 2007

161 *Planning for Housing Affordability*, Council for the Protection of Rural England, 2007

a whole, in each specific area it is the housing supply and demand for homes within this specific area that determine house prices (as the saying goes, location, location, location). Thus if a sharp increase in housing supply in any given area is counterbalanced by a bigger rise in demand for houses in that area, house prices in that area rise. Local house prices rise if new homes make existing residents' quality of life better rather than worse, through bringing new amenities, (e.g. shops), or just because attractive housing is itself likely to raise quality of life for nearby households.

"To encourage development it is important to understand what types of development existing residents would generally welcome, and which they would oppose"

The bigger a development, the bigger the potential impact on surrounding areas' house prices. Though the Poundbury development in Dorset or the regeneration of the Docklands (for example) sharply increased housing supply in their area, house prices in the surrounding area rose as the location became more desirable and so demand increased. People in the 1970s who would not have considered living in the Isle of Dogs saw it as a real possibility by the 1990s. But this doesn't change the fact a net increase in supply across the UK as a whole will lower house prices – though paradoxically house prices may rise in the areas where these extra houses are built.

So development impacts on existing residents' quality of life and house prices. But developers have no interest in what their houses do to the prices of existing homes or residents' quality of life – if they ruin the character of a local village, this has only a small impact on their profits, which are based on selling their newly constructed homes. This means even those existing residents not instinctively hostile to development, are therefore (understandably) wary of developers. Only with new homes that local residents approve of can developers overcome this hostility. Therefore to encourage development it is important to understand what types of development existing residents would generally welcome, and which they would oppose.

The most popular types of new development are larger homes with character – not flats

There is clear evidence about the types of homes the public like and those they don't. The Joseph Rowntree Foundation found in a 2004 survey that 55% would accept new detached and semi-detached housing in their area, while just 20% would oppose it. However, over 60% would oppose new flats being built in their area, with just 20% supporting them.[162]

In 2002 a MORI poll found 30% of people said bungalows were their preferred home, 29% a village house, 16% a Victorian Terrace, 14% a modern semi and 2% a modern loft apartment. No one opted for a tower block.[163] Assuming people like homes they themselves like to be built near them, the best homes for existing residents are clearly quality decent sized homes with gardens. However, people are not against all high density homes, e.g. Victorian-style Terraces, which are high density, are quite popular with the general public. So to encourage new homes the planning system should encourage or support building new homes that will be popular with existing residents.

162 *Housing Futures*, the Joseph Rowntree Foundation, 2004

163 *Bungalow's are people's choice in England*, ibid

But government imposed developments that are the complete opposite of this

However, in recent years government decided to impose a different, top-down view of what new developments should look like rather than listening to what people actually wanted. Government pushed for local plans drawn up by councils to facilitate development to include targets on densification, affordable housing, and to go for low-cost developments. To take one example, Public Sector Agreement number 6 for the DCLG from the 2004 spending review argued that new housing developments should be at least 30 dwellings per hectare and housing density of between at least 30 to 50 dwellings per hectare should be encouraged.[164] The DCLG reported in 2009 that the goal was 'on track' with average densities at 44 dwellings per hectare, a sharp rise from just over 25 dwellings per hectare in 2000.[165]

This political push for affordable and low-cost housing has meant a push for cheap housing. Even more, it means a push for cheap flats – because current high house prices mean that flats are about the only form of housing that are low-cost, or can be sold as part of an 'affordable' housing scheme (even with government subsidy). This explains why around 50% of new dwellings are now flats. These cheap and flat based developments are the exact opposite of what people would be happy to allow in their area, and are the type of development most likely to lower quality of life and house prices for existing residents.

Residents feel they have little control over development – so use local councils to oppose it

The result of recent policy was a widespread feeling that government was ignoring local wishes and increased hostility to development. The Saint Consulting Index on development found 49% felt they were not adequately listened to on development in their area, against 25% who felt they were.[166] The Regional Spatial Strategy policy pursued in recent years, where regional bodies decide and allocate a certain number of new homes to be built in each local authority they control made this worse, (e.g. the South East has a single body that then passes on to each local authorities a minimum number of new houses that are supposed to be built there). This did not just alienate residents, but actually reduced housing supply.

The Regional Spatial Strategies (RSSs) established only *some* new developments in *some* areas. The idea was this would be supplemented by other development. However, since communities felt new development did not take account of their views, (a view that RSSs and government targets reinforced), this led to a rejection of development. According to one survey in the last few years the proportion of households that objected to development in their area rose from 13 to 21%.[167] And because except where the Regional Spatial Strategy over-ruled them, councils controlled local planning, councils put the brakes on new housing across the country. This helps explain why, despite a tripling of house prices, the numbers of new homes barely increased in recent years.

Expensive land pushed developers towards poor quality housing

Another reason new homes are often opposed is that there is a general consensus that new UK homes are not as attractive as they could be. As we saw earlier, they are often small and badly designed. But UK homes are unattractive not just

164 *DCLG Autumn Performance Report,* DCLG, 2009

165 *Land Use Change Statistics (England) 2008 – provisional estimates,* DCLG 2010

166 *Saint Consulting Index*, Saint Consulting, for years 2007, 2008, 2009, available at http://tscg.co.uk/survey/summary.html

167 *Saint Consulting Index*, Saint Consulting, ibid

because of government interference but because the expensive land created by the UK's planning system leads to unattractive (as well as unaffordable) homes. The greater a % of a house's value is from land, the less important other factors such as light and aesthetics are. Developers make more profit from throwing up badly made homes cheaply and then moving on to the next scrap of land with planning permission rather than spending time, money and effort in creating desirable homes. Table 14 sets out the economics of how the rising cost of land reduces the value of a home coming from other factors.

Table 14: Value of 'different factors' making up value of a £160,000 house

	% of house's value from land with planning permission	% of house's value from other factors (e.g. light /aesthetics)
Land costs £10,000	6%	94%
Land costs £45,000	28%	72%

So the more expensive land is, the more developers have an incentive to cram in as many dwellings as possible with as few or as small gardens as possible, (even before government targets push them to do so). As the UK's high house prices mean home-owners will accept almost any new house to get onto the housing ladder, this further reinforces a tendency for new homes to be quickly put up, small, and shoddily made. High land and so house prices also mean that attempts to tackle the UK's problem of new homes being flats or too small through spatial standards or requiring new homes to be a certain size will fail. Even if standards force new homes to get bigger, older ones will just be broken up into smaller dwellings as this is the most profitable thing to do with them. Developers may also hit new standards on housing space by simply reducing the gardens available in new homes. Only a general increase in housing supply that means real house prices stop rising will tackle the problem of housing affordability.

Overall, we are trapped. Fewer new homes leads to lower quality new homes, strengthening opposition to development and leading to even fewer new homes and an ever worsening cycle.

There is less hostility to new development *per se* than people think

Yet while people don't like bad developments near them, they are less hostile to development in general than is often thought. A 2007 YouGov poll found that 33% of people thought that the UK's housing shortage was very important, while a further 45% said it was fairly important. Just 10% said it was unimportant.[168] The poll also found 82% felt the support of the local community was important in the development of new homes – something top-down targets reduce. Government research separately found that 73% of people would support new homes if they were well designed and in keeping with the local area – unsurprising when we recall that quality homes can raise house prices and improve the feel of an area.[169] Government policies on amenities also have a role

168 *80% of Britain's want action on housing shortage*, New Homes Marketing Board, available at their website

169 *Public Attitudes to Housing 2010,* DCLG, 2010

to play – with the same research showing over seven out of ten households would generally support new homes if they were accompanied by the necessary infrastructure, like roads and utilities. This research also found that even in areas where opposition to new homes was strongest, such as in the South of England, less than 30% said they would oppose new homes to buy in their area – a substantial minority but far from a majority.

A separate 2004 YouGov poll found that 72% of people agreed that Britain needed more homes. There was even support from most people for building new houses in their suburb, town or village, with 55% in favour and 29% opposed. Similarly the margin of those who said they wanted their council to encourage development without qualification was 43% in favour as opposed to 34% who said they should discourage or prevent such building. The poll showed the strongest opposition to development, (though still a minority at 48% of people polled,) was when people were asked if they wanted new housing built 'in their street'. People recognise that the impact of housing is directly related to their proximity to new homes and their position on development changes accordingly. If you like where you live, (which as you live in your home you probably do), you will be most worried about development in your immediate vicinity.

The current planning system does not do enough to recognise that the impact of development is focused on those closest to development nor reward communities for allowing new homes, despite the positive social impact of allowing development. But people do recognise there is a housing shortage, and are supportive of general measures to reverse this. What is needed is a way to harness this support, while persuading most residents that allowing new housing in their area can benefit them too.

The council based planning system strengthens NIMBYism

But if the majority are not against development, how can it be that we are seeing fewer homes built over time? While recent government policy made a bad situation worse, even in the 1980s and 1990s the UK was near the bottom of the list for the number of new homes across the EU (adjusted for population size). So simply going back to the past will not solve the UK's chronic housing shortage. The Head of the Home Builder's Federation has made clear that plans by the new government toward greater localism may even have a major negative impact on the amount of land being released for development – "there is a real danger in my view that we will see the supply of permissioned land (for development) decline even further".[170]

The current council system strengthens the power of NIMBYs. With turnouts at just 30-35%, local issues are often neglected in favour of national ones for many voters, meaning allowing development – and alienating a small number of committed voters who are likely to vote against you – is very difficult. Those who support development are unlikely to change their vote on the basis of new housing. The 43% who say they support encouraging development in their area are much less likely to vote in favour of councillors who have proposed new dwellings than the 34% who say they want to discourage new development in their area are likely to vote against them. A small hard core of NIMBYs can block development – despite all the problems this brings.

170 *Speech by Stuart Baseley, Head of the Home Builders' Federation, 13th October 2009,* available on their website.

The evidence for this view is the limited numbers of new homes that were built in the 1980s and 1990s and by a scan of council websites, MP's websites and other channels for elected officials, which highlights a massive and overwhelming trend – the new government's planned scrapping of central targets is likely to lead to even fewer new homes. There is no one (but the new government) saying that the scrapping of these targets will lead to a higher numbers of new homes. If planning interacted with local government in a positive way then more councils would be stating they would look forward to being able to build more homes once central targets were scrapped. That they aren't should be ringing very loud alarm bells in government.

Most land in England is not developed – and the key issue is what we do with our land

When considering development and planning, it is important to remember that the proportion of the UK which is developed is actually quite small. The proportion of England, by far the most populated part of the UK, classified as 'green space' was 115.7 thousand km^2, out of a total land mass of 132.3 thousand km^2.[171] This was roughly 87.5%. Another 3.4 thousand km^2, or 2.5% was water, while of the 10% that was 'developed', much is domestic gardens – not concrete and tarmac. We could protect almost all of our green space over the next few decades while allowing a large increase in the number of new homes in the UK. The only question is whether we want to have quality housing with green urban spaces, and lose a small proportion of the existing 87.5% of green space to accommodate this, or if we want to cram their population into small box-homes without gardens situated in ugly, unaffordable cities.

VAT on extending existing homes is reducing housing supply and raising demand

A final brief point on the issue of housing supply is the current system of charging VAT on extending existing homes discourages people from expanding their house rather than moving (though it is true that there are some horrendously complicated exemptions for certain actions – see HMRC Reference Note 708).[172] But generally a household that wants to convert a loft or basement is instead encouraged to move into a new home by a 17.5% addition to the cost of conversion. This means someone who could extend their living space is instead pushed to move, meaning that instead of increasing housing supply (via an increase in the size of their home), we see an increase in housing demand (as they need a larger house). This is the exact opposite of what good policy should do.

Though there are complications due to the EU's role in discussions on VAT,[173] this urgently needs review as it makes no sense to penalise those who would increase the net UK housing stock with their own funds. It is madness that we are penalising people from paying to expand the UK's housing stock when we are in the middle of a housing crisis.

171 *Land Use Statistics, Generalised Land Use Database, 2005,* ONS, available at their website

172 *HMRC Reference Note 708, HMRC*, available at their website

173 *VAT on Construction, Standard Note: SN/BT/587*, House of Commons, 2009

The UK needs to move to a virtuous cycle of development

The last decade saw even fewer new homes than previous ones. Higher house prices and bad government interventions created unattractive new housing developments that residents opposed, meaning opposition to new homes grew – opposition the current council-based planning system further exacerbated. The UK needs to move to a virtuous cycle where higher quality development is encouraged, reducing opposition to new homes and leading to more and better homes over time. This will reduce housing costs and allow home-ownership to rise again.

Part Two
Solutions

1
Existing Solutions Won't Work – A New Template is Needed

As shown in Part 1 the scale of the problems in housing are huge. Yet government needs to make unprecedented spending cuts. What is needed is a coherent and far-reaching positive policy narrative that removes current failures on housing *and* generates billions in savings. The outline of a new narrative and some concrete proposals that create a new template for housing policy are set out below.

In this new template then home-ownership, the goal of most people, must become central to the government's efforts. House prices need to stop rising steeply as they have done in recent years. The key is to build more homes. A new system of 'community-controlled planning' should replace the current local government based system, with housing developments permitted unless local residents 'directly impacted' by a proposal vote against it in a ballot. Developers would be free to offer incentives to those balloted on the new homes (either in the form of community amenities or through direct cash transfers). This will remove the past few decades' heavy planning constraints. As safeguards, in National Parks or Areas of Outstanding Natural Beauty planning restrictions would remain much tighter while each council would also be free to designate up to 75% of existing undeveloped land as 'protected' and off limits for developers. This will change the antagonistic planning system into one that favours win-win solutions and should mean more new homes, more stable house prices, and greater ownership over time. More homes will hold down rents and Housing Benefit costs, as well as inflation more generally.

The pro-renter support system currently in place should change so that home-owners receive support equal with renters. Greater help on deposits, repairs and for those that lose their job should all be made available. More social housing (outside expensive areas) must be built, using a new 'Path to Ownership' model, which abolishes the upfront costs to government of building new social homes. But social housing needs to become a 'stepping-stone' to ownership rather than a final destination, with those in the new Path to Ownership model being moved automatically toward home-ownership when they pay their rent. For existing tenants the Right to Buy should be revamped so that most tenants can purchase their home at no additional cost to renting, while tenants should also have a Right to Move and Buy to make their deposit 'transferable' if they want to buy a property other than their current one – particularly useful for those in expensive properties. To remove current perverse incentives, social housing allocation systems need to be changed from the 'needs-based' system and be based on the length of time tenants have waited. Finally, social rents should rise to meet market rents – but through increases in housing supply that hold down market rents, not simply raising social rents more quickly than in recent years.

There is no disguising the radicalism of these proposals. However, the savings they deliver are around £20 billion a year in the first few years, running at £15-20 billion in future. On top of this, the reforms will increase home-ownership, transfer money and control back to local communities that allow development, permit more social homes to be built, and reduce the poverty trap that social tenants currently face.

2

Make Home-Ownership Affordable by Raising the Supply of Homes

Firstly, housing and home-ownership must be made more affordable over the next couple of decades. A large increase in the number and quality of new homes will limit future house prices, reduce private rent increases, and lead to shorter social housing waiting lists.

Housing affordability should be at the heart of government policy

House prices must take centre stage in policy with the starting point for government being that home-ownership should become affordable for all. Currently, no one in government is even particularly accountable for steeply rising house prices. They do not come under the Bank of England's existing CPI inflation target despite being a clear increase in the cost of a good (housing). A procession of Housing Ministers focused occasionally on top-down building targets but more often simply trumpeted affordable housing schemes of marginal impact.

The new government has made clear it wants to incorporate housing costs into the Bank of England's inflation target. This would be welcome as it ensures that the Bank of England is able to react to rising housing costs rather than seeing it as something beyond their remit. But much more is needed. To place housing costs and home-ownership at the heart of government policy, a new target for housing affordability should be set as a flagship indicator for the DCLG. The goal should be that everyone who works, and wants to own their home, is able to do so. The practical realisation of this goal would be the target that by 2030, the average English lower quartile property should be no more than four times the income of a household on the minimum wage working a 35 hour week.

The current situation is that a 35 hour week on the minimum wage brings in £10,800, while across England lower quartile house prices were £130,000 in the final quarter of 2009.[174] This means the present ratio that we want to bring down to 4:1 is around 12:1. If we posit that between 2010 and 2030, the minimum wage will rise each decade at a similar rate as it has since 1999, (65% between 1999-2010, from £3.60 to £5.93), house prices would have to remain flat between 2010 and 2030 for this ratio to move to the desired target of 4:1 (the minimum wage having reached around £29,000 in nominal terms.) This gives

174 *Table 583; Lower quartile house prices based on Land Registry Data, by district, since 1996*, DCLG, available at their website

us a rough annual goal of house price stability and while a small rise in house prices in some years is not a disaster a repeat of the past decade, where prices spiralled ever upward, is unacceptable within this framework.

This framework makes unrealistically feasible assumptions about how economic circumstances will look over two decades. But the key point is that in doing so it both sets a short-term target of nominal house price stability in the short-term and a final goal within twenty years – that home-ownership should be available to all who work and want to own their own home.

Government should annually publish an open letter on achieving these goals

Each year, the Housing Minister and the Permanent Secretary for the DCLG should write an open joint letter to the Prime Minister, stating movement toward the 2030 goal, house price changes over the year, their assessment of changes in housing supply and demand over the year, and measures they will take in the following year to assist progress toward the target.

This letter should also include an assessment of immigration's impact on housing demand in the UK. If the government wants to allow large scale net migration into the UK and still hit the affordability target set out earlier it needs to see greater amounts of building required in the UK. Government should be honest about this and explicitly feed it into housing policy in the letter from the Housing Minister to the Prime Minister. This measure will both make Ministers focus on the impact of immigration on housing but also help refute those who argue that immigration is the sole or even major cause of our housing difficulties. Sweeping this difficult issue under the carpet is the surest way to bad policy, a stilted debate, and political unpopularity.

Making homes affordable requires measures to increase housing supply

It is unhelpful for the government to set detailed targets for increasing housing supply, but they must aim for a sustained and large increase in housing stock from the current record lows. This must flow from local communities being incentivised to support development – rather than heavy-handed top down planning. The exact annual total is less important than a substantial and sustained expansion in the numbers of new homes.

The measures that would most help encourage development, (especially if we want to do this in a politically acceptable way) are to allow local communities to decide exactly on what development they want – and reward them for allowing development to go ahead. However, greater localism must not further strengthen the power of a small NIMBY minority.

Government must scrap targets that are imposing low-cost, high density, 'affordable' housing

As shown earlier, building low-cost housing doesn't lower prices any more than building more expensive housing. Meanwhile, government sponsored affordable housing is ineffectual in spreading property ownership, annually making up just 2.5% of all housing transactions and totalling around 0.1% of the homes/households in the UK.

The problem is that for homes to be 'affordable' then even with subsidies such housing almost invariably has to be smaller and less attractive than most homes (and usually affordable housing consists of small flats not family homes). Centralised targets and goals on this and other issues (e.g. densities) that prescribe what new developments must look like have had the impact of making new developments unattractive to existing residents, increasing opposition to new homes and reducing the supply of new houses – making affordability even worse. Despite a huge rise in house prices the last decade saw even more anaemic growth in housing supply than the already low levels of new homes being built in the 1980s and 1990s. Instead of counter-productive targets then if we want to increase housing supply in general, we should allow higher quality and higher cost development, generally popular with local residents, not the unpopular flat-based and 'low-cost' and 'affordable' homes previously pushed by central planners.

The conclusion is simple. All central targets and goals, from housing density to low-cost and 'affordable' housing schemes, should be scrapped. It should be entirely down to local communities to determine what developments in their area look like, not central government.

Allowing desirable development increases support for new homes

As the CPRE state "*so far as existing homes are concerned, the role of planning in affecting affordability is limited principally to affecting the nature of development in the surrounding area. The value of any home is significantly affected by its environs*".[175]

High quality homes, especially if built alongside new local amenities can actually lead to better quality of life for existing residents, raising house prices in an area and bringing gains for local home-owners. Developments such as the Docklands or Poundbury brought with them attractive housing, money to pay for parks and other new communal spaces, and residents who require attractive shops and amenities. Sympathetic development can spur regeneration and also help sustain rural life. A village of 10,000 can more easily sustain a local pub, post office and shops than a village of 5,000 can.

Developers should make the case clearly and directly that high quality development in local areas will make local residents better off rather than worse off. As we saw earlier, the opposition to new homes was largely dependent on what was proposed, with three times as many opposing flats versus homes. 73% supported homes that were well-designed and in keeping with their local area. People also have clear preferences in terms of what kind of housing they prefer and don't and government should respect this. Of course, if local people want to allow flats then developers should be free to build them in a particular area – but it should be down to local residents to decide what is built in their area. However, the main point is that a greater say for existing residents is likely to lead to a greater number of higher quality developments.

175 *Planning for Housing Affordability*, Council for the Protection of Rural England, 2007

Higher quality housing allows everyone to 'trade-up' and can be done high-density

Building higher quality housing is preferable to building poor quality homes at the bottom of the market. Increases at the higher end of the UK housing market allow everyone to 'trade-up' to better quality housing. As expensive housing becomes cheaper, middle class families can afford to buy it, reducing current demand for mid-range housing, which falls in price. This allows lower income families to move up, reducing demand and lowering prices for housing at the very bottom of the market, thus allowing some households to become owners for the very first time.

To those who argue that this plan means the richest will simply have more second homes, the proportion of second homes in the UK is 235,000 – around 1%.[176] So for every 100 new homes built at the top of the market, 99 households will be able to 'trade-up' to better housing, 99 households below them will then trade up and so on. This 1% might increase slightly, but such an increase would have an almost negligible impact on the market as a whole.

Some argue government rules are necessary to ensure we build high-density housing to protect our green spaces. Yet as only around 10% of England is developed, a decline in housing density is not necessarily a bad thing if it leaves people in and living near better homes with gardens. But there is no need for abandoning density targets to actually reduce housing densities, Victorian terraces and semi-detached houses are popular with the public – despite not being particularly low-density. What is more important than high/low density is the quality of what is being built – something top-down targets will almost always reduce.

The public don't mind well-planned high density as shown by the fact two of the most expensive and popular parts of the UK have very high population densities. Kensington and Chelsea is the most densely populated part of the UK while Surrey is one of the most densely populated non-urban counties.[177] High density does not halt their popularity or quality of life for those living there. Those in favour of high density housing should spend more time creating schemes the public like rather than pushing central government to impose diktats – and we would all benefit.

A new 'community based' planning system for approving new homes

So the first step is to remove central government targets in the housing market and allow for better quality new homes. The second step is to ensure local people feel they have a say in how development in their community will look – without strengthening the NIMBY minority. Regional planning boards are remote from individual communities. What they allow is often undesirable to local residents. Following the general election, the new government has indicated they are to be removed – and this welcome.

But local councils too should lose their ability to approve or reject new housing development. Councils are currently failing in their duties in this area, as shown by the fact that the Audit Commission found three out of four local authorities

176 *Survey of English Housing 2005/6*, ibid

177 *Population Density 2002, regional trends 38*, ONS, available on their website

inspected by the Commission since 2000 were rated as fair or poor,[178] and by the Saint Index which found that three-quarters were unhappy with their local council's performance in planning.[179]

As noted earlier, the existing system seems to be strengthening the power of NIMBYs and reducing the numbers of new homes. The noises coming out of local government demonstrate what will happen if the new government's plans for decentralisation go ahead – a fall in the already very low numbers of new homes built. It should be remembered that the whole reason Regional Spatial Strategies and so on were brought in was a consistently low level of new homes built in the 1990s and early 2000s – when councils were in charge of planning.

"Instead of simply allowing councils to decide on planning applications, the government should move to a system of community-controlled planning, where those 'directly impacted' by a development are balloted over any proposed development registered with the local council"

Instead of simply allowing councils to decide on planning applications, the government should move to a system of community-controlled planning, where those 'directly impacted' by a development are balloted over any proposed development registered with the local council. It would be the results of this ballot that allowed development to go ahead or not, rather than the agreement of the local council.

Having received a proposal, the council would set a deadline and post out ballot papers, with those objecting having to return their ballot paper by the deadline. Any proposed development would automatically pass unless a majority of those balloted voted against it. The cost of this would be small. A 2002 study of postal votes found that the cost per elector was around £1. Assuming costs have increased slightly since 2002, a ballot of 1,000 homes would cost around £1,500 or so – very little compared with the overall costs of development.[180]

What exactly 'directly impacted' should mean would be developed in consultation and via government guidance, but three main elements to consider would be proximity, size of development and visual impact.

Development in this context does not just mean new homes but anything that changes the housing stock in the UK – so for example a building changing planning designation from a business or industrial use to a residential one (or vice versa). Demolishing a tower block and replacing it with another would also fall within this definition. The idea should be that those who live in an area will be those who make the decision about what is allowed and what is not allowed there.

This would lead to better quality housing and engagement with local people

This system is about involving communities and designing homes that existing residents can accept. It is about moving away from the current adversarial nature of planning to a more conciliatory and consensus-building model. Under this system, planning permission is more likely to be granted where homes are attractive as existing residents will not oppose them. Developers and local

178 *Building Better Lives*, The Audit Commission, 2009

179 *The Saint Index*, ibid

180 *Best Practice Guide for Postal Voting*, Royal Mail Group, 2002

residents can gain from working together for their mutual benefit. Developers would be wise to undertake brief market research in areas to help inform their proposals – so that they reflect what the majority of local residents would like to see – engaging with local people directly. Society does not have to be imposed through top-down state planning – it can be private groups engaging directly with each other with the goal of a mutually beneficial outcome.

In the long run, the aim under this system is that development becomes seen as a positive boon for the community. Large numbers of quality homes in an area can actually raise existing households' quality of life and house prices, as large case studies like Poundbury or the Docklands have shown and the DCLG has itself found.

Developers rewarding local residents and limiting ballots to home-owners

However, developers should be free to offer financial rewards to those households being balloted on any development, using the windfall gain that they receive should planning permission be granted. As was discussed earlier, the average value of a hectare of land rises from around £16-17,000 to around £1.9 million if it goes from agricultural to residential land, (£2.47 million in the South East). This means an average windfall in planning gains per home allowed (at current densities/prices) is around £45,000 in 2009 (£57,000 in the South East). Obviously, developers would be free to pocket almost all of these gains, but those who are sensible would recognise that recycling some of this increases the chance of new homes being accepted. Under this new system developers could purchase land with agricultural planning permission, put in their application for housing development – and if they failed, simply resell the land on.

The sums that they could offer local residents are large. If a village decided to increase in its size from 2,000 to 3,000 households, incorporating a large and high-quality development, this would easily permit a £10,000 payment to every existing household in the village. Indeed, if the whole of the planning gain was recycled to existing homes then based on average land values it would be a £27,000 payment per household, (though developers recycling the entirety of planning gain in this way is very unlikely). This is on top of any rise in local house prices if the development is done well, and on top of the fact that in rural areas new homes could help protect local amenities such as schools or shops by raising the local population.

Of course, as the amount of land being released for new homes rises the price of land with residential planning permission will fall, but even so the gain from allowing new homes will be substantial. If over five years land prices fall by 25% due to an increase in the supply of land for residential purposes the cost of land for a new home would fall by £11,000. But this would still mean that every new home allowed in an area would generate gains of £34,000 or so, allowing substantial compensation to local residents. As a knock-on positive effect, such a fall in residential land prices would help the government hit its target of stable house prices.

The government should also make provision for developers to contribute to local communities to persuade local residents to allow development. For example, a one off sum from planning gains could be used to create a trust that could then be used to subsidise a village shop that would otherwise close down, or upgrade a local school, and so on. The developer could use some of the funds obtained from a major development to purchase nearby land and create a large new park for all residents of a village or town to enjoy. In many areas and ways these measures would be a cost effective way for developers to persuade local residents to allow proposed development, and developers could engage with communities to see what would be the most popular way to recycle some of the planning gains. It may be that rather than a simple cash incentive, which appears rather cold, people may prefer the idea of developers contributing to the community – good for house prices, their quality of life and the community that they live in.

This system would still allow substantial profits for developers

This system should still allow developers to make the profits necessary for them to expand. Most developers use the 'residual valuation' method, where they assume they can sell houses at price X, they then subtract profit, the cost of construction, and the cost of land. Developers can continue to 'price in' their profits in this system – as they do already. Developers would gain by increasing the numbers of new homes that they could bring to the market and expanding their business over time. The main losers from this new planning system would be (agricultural) land owners who convert their land's planning permission then sell it on. But such gains from planning permission are not 'productive' but a form of rent-seeking – they do not create wealth but rather simply redistribute it to a small number of agricultural land owners. Fortunately, as these changes only affect potential gains in future for some land-owners this makes it easier for these changes to be brought in. Further, since under this system it would be easier to convert agricultural land to residential land, the value of agricultural land would rise and all holders of agricultural land would gain from this – and this gain would be definite (whereas planning gains in the future are uncertain).

Protecting local services and ensuring fair government funding for new homes

The final reform that is necessary to help persuade most people to allow new homes in their area is to ensure that new homes do not damage local services. Even with community-controlled planning, this will be a real concern for many. Seven out of ten people said they would be content to allow more homes in their area if it did not lead to worse services for local people.

The coalition government has proposed that new homes in an area should bring with them additional funding for six years. This is to be welcomed as a step in the right direction. However, more could be done. A review should be held to see if population figures that help determine government funding across a range of areas, from PCTs to local government grants, which are often based on out of date population figures, should be collected more often. To collect more up to date figures every couple of years would not be a huge financial undertaking and would allow for better targeting of funding where populations are changing. An alternative option could be to track in greater detail the movement of people into an area (i.e. through a short one page form whenever someone moves home detailing if they had any particular need for government support). This would help ensure funds are targeted correctly and remove existing concerns over damage to public services. If necessary, the funds for this could be provided by the savings outlined throughout this document. Without changes, there will continue to be worries that the amount of funding that councils have will not be enough to accommodate substantial population growth within their area – especially given cuts in funding over the coming years.

Obtaining planning permission for new social housing would act as 'quality control'

If councils want to build more social homes, they could grant themselves planning permission as long as they won in a ballot of those 'directly impacted' by such development in the usual way.

To help ensure that their proposals were supported, they could provide financial incentives by allowing private development alongside their proposed new social housing, and offering local residents part of the planning gain raised through these new private homes. This would mean that areas that permit greater development can ensure that they also develop social housing should they want to do so.

The community-controlled planning system would also act as a quality control for new social housing. Social tenants have often found themselves in ugly estates that alienated and demoralised many who had to live in them. Work by Alice Coleman in the 1980s showed bad design, (e.g. large communal areas no one felt they 'owned', which in turn were more likely to attract graffiti, or covered alleys where people could be mugged easily) were twice as common in social housing built in the previous few decades as they were in private housing built in the same period.[181] The community-controlled planning system should stop such mistakes in future.

Encouraging brownfield development and ending 'garden grabs'

The changes set out would not just encourage greenfield development but brownfield development as well, since even in urban areas the average price for a hectare of land for industrial uses was just £600,000, much less than the £1.87 million for residential land.[182] New homes on brownfield sites are more likely to improve an area so that the incentives necessary in these sites would be small and the willingness to support development is likely to be much higher. Where this requires a change in land use (e.g. from commercial to residential) this would be done using the community-controlled planning model and as part of the same ballot. Since regenerating urban scrub is unlikely to prove unpopular with those who live nearby, developers should find it easy to obtain permission to build new homes in many brownfield sites.

In brownfield sites where there are no residential dwellings near by, (e.g. in an industrial area with fields on one side and factories on another) then it should be taken as automatic that any proposed development is allowed to pass unless the local council halts it due to 'exceptional' reasons – in which case the council would be required to publicly set out the reasons as to why it believed that there

181 Her work is expertly explored in James Bartholomew, *The Welfare State we're in*, Politico's, 2006

182 All figures in this paragraph are from *Property Market Report July 2009*, ibid

was a strong case for not allowing the development to go ahead. This would further act as a major incentive for the redevelopment of run down urban areas by making it reasonably easy to get through developments in these areas.

The new government has already made 'garden grabbing' for developers more difficult – a welcome move in preventing the destruction of suburbs across the UK. Under community-controlled planning 'garden grabbing' households would have to win a ballot of all those impacted, (likely to be all neighbours), a very difficult task to achieve. This means that approval of new homes on existing residential land is only likely to occur where what is proposed is a positive benefit to the local community (e.g. replacing an old run down tower block with a new one).

Limits on Areas of Outstanding Natural Beauty and National Parks

These parts of the UK should be exempted from this new planning system, retaining their already stricter planning laws. While in most areas allowing new homes will be beneficial, in these areas there are particular benefits to low population densities in these areas. The benefits are not just for locals – these areas are visited by millions each year. Therefore the whole of the UK would benefit if these areas retain their existing planning laws.

Protecting 75% of existing green space in each local authority

While this proposal should open up land for development, this should not lead to areas losing all of their green space. A further problem is that under these proposals developers might seek to seize areas like woodland, open fields and so on – areas which many people may enjoy, but no one actually lives near to – so the community-controlled planning rules would not apply. This would be the worst possible outcome, as such areas are usually highly valued by local communities and should be last to be developed.

Therefore to tackle both these problems, councils should have the power to designate up to 75% of the currently undeveloped green space land in their area as off-limits to developers – so that areas do not become completely swamped with new homes. This would ensure that the countryside in any one area is not concreted over, and that existing rural and sub-rural areas retain their current feel. Council owned parks and so on would be excluded from this 75% – this would be 75% of undeveloped land excluding such public spaces. As levels of existing green space make up around 87% of England, and developed areas around 10%, such a cap in each area would still allow for a very large increase in the numbers of homes being built, whilst reassuring people that there would continue to be large green spaces across the UK and in their locality.

Existing planning teams adjusting to this new system

These reforms will not require an increase in the number of people involved in the planning system and may even reduce the total needed. Existing officials can be redeployed as they will not be needed to adjudicate on new homes, but should focus on planning for the consequences of allowing more development. The planning system overall should become less complicated and less prone to appeals and wrangling.

Adjusting for loss of Capital Gains Tax to the Exchequer

At present the value of windfall gains from planning permission generates Capital Gains Tax. This will no longer be the case once our system is in place. The Barker Review argued that because of reliefs and roll-overs in 2000-1 just £50 million was raised from the windfall gains due to planning permission from changing agricultural land to residential land.[183] If we triple this to reflect rising land prices and double this again to capture the value of industrial sites changing planning permission we might estimate roughly £300 million or so at present is raised per year.

The sum given to individual households for allowing development as set out above is likely to be taxed as capital gains, which could replace the sum lost above. If more is needed, a levy that goes to central government could be considered, (perhaps £500-£1,000 per new home or something like £30,000 per hectare granted for development). The exact way to recoup this would best be decided following consultation and an examination of how much revenue is likely to be lost from any changes.

Demolishing houses would be harder under this system

Another benefit from these reforms would be a reduction in demolitions opposed by local communities. At present councils focus too much on new build and not on renovation.[184] Often, councils are demolishing homes in areas despite the wishes of local people. In future the demolition of properties and their replacement with other properties would have to be approved by those who would be 'directly impacted' by any proposals, just like any other planning proposal. In addition, changing the VAT rules, as set out below, should help reduce demolitions by reducing the costs of renovation for local authorities.

Abolishing VAT on renovating or expanding homes (up to a set limit)

To further expand the supply of housing in the UK the government should urgently examine the possibility of abolishing or removing VAT on renovating or expanding housing space, to a set maximum, (e.g. £15,000) per dwelling, rather than continue with the complicated and confusing rules that exist at present. This would require discussion at EU level as it has partial competence in this area, though a 5% rate is clearly allowed where it is part of the "provision, construction, renovation and alteration of housing, as part of a social policy."[185] Amending VAT on housing within these reforms would be just that.

This would encourage rather than penalise those who want to expand their home rather than move. Those who extend their property rather than move expand supply and reduce demand for new housing. Instead of a family having to move from a two bedroom to a three bedroom or from a three bedroom to four bedroom house, the family pays for an extension that has permanently expanded the UK's housing stock. This should be encouraged as it is simpler and cheaper to facilitate than building extra homes.

The costs of this might be around £1 billion, if capped at a level (e.g. £15,000 per house) that means the most expensive extensions still pay VAT on spending above this. (This was the level estimated in 1998 it would cost to abolish VAT on repairs and renovations altogether.)[186]

183 Kate Barker, *Review of Housing Supply*, HMT, 2004

184 *Building Better Lives*, The Audit Commission, 2009

185 *VAT on Construction; Standard Note SN/BT/587*, House of Commons, 2009

186 *VAT on Construction; Standard Note SN/BT/587*, ibid

Increased supply of new homes will keep rents lower – boosting incomes and the economy

Private monthly rents rose from £341 in 1997-8 to £558 in 2007-8, an increase of roughly 64%.[187] As noted, this was even higher than wages during this period (52%), meaning that renters saw their living standards reduced due to the higher cost of housing.[188] One impact of increasing the housing stock and improving home-ownership affordability will be to reduce demand for renting, while an increase in the numbers of new houses may increase the supply of homes to rent as well as homes to buy.

Within these reforms and a framework of rough house prices stability, rents should only rise slowly – perhaps at around 1% or so a year. Achieving this would provide a much needed boost to living standards as wages rise much faster than rents over the next decade. An annual 1% rise in rents when wages tend to rise at around 3.5% would cut housing costs each year by 2.5% or so. If housing costs make up a third of spending for a household, this is equivalent to its disposable income rising by 0.8% a year – allowing a steady rise in income growth for rental households – which many will spend in the wider economy and also reversing the recent situation where disposable income was falling due to rising rental costs.

Private rents rising more slowly will also reduce Housing Benefit to private landlords

In addition, more stable rents will halt the inexorable rise of Housing Benefits. As we saw earlier, private rents and Housing Benefits have risen in almost exact parallel, both going up by 64% in recent years. Housing Benefit has risen from £12.2 billion to £20 billion, with around £10 billion of this going to private renters.

If rents rise by 1% in the coming years rather than roughly the 5% rate they rose at between 1997-8 and 2007-8,[189] this would save substantial sums in Housing Benefit.

The government has announced a series of reforms in Housing Benefit designed to shave off around £1.8 billion from Housing Benefits. As discussed, those savings that are one-off should be achievable without too much difficulty. But the idea that Housing Benefit can be further reduced by simply pegging it to the CPI will be difficult. The main problem with Housing Benefit is not that claimants are greedy or landlords are being exploitative, but that rents are rising very sharply, and so attempts to hold down Housing Benefit by uprating it with the CPI will push the cost of housing onto lower income households.

Forcing low income households to pay for rising rents out of their own pockets is undesirable. Accordingly, when calculating savings at the end of this paper, to ensure no double counting, then it is assumed Housing Benefit for private renters will fall by £1 billion due to government plans to cap and reduce Housing Benefit and limiting claims to the 30th percentile in an area. However, after these savings it assumes Housing Benefit for private renters will rise at 5% or 1% due to broader housing policy, in line with private rents. This means that each year the government will spend less than it would as rents rise at this lower rate. Within five to ten years this will amount to serious savings (e.g. within five years rents rising at 1% not 5% trims £2 billion from government spending, within ten it cuts expenditure by £4.7 billion).

187 *Table 731 rents, lettings and tenancies; private rents and tenancies,* ibid

188 *Bank of England Inflation Calculator,* bank of England, http://www.bankofengland.co.uk/education/inflation/calculator/flash/index.htm

189 *Calculated from Table 731 rents, lettings and tenancies; private rents and tenancies,* ibid

Reform also ensures the CPI (and so benefit rises/ interest rates) will be lower

As was discussed earlier, the current plan to save £6 billion from linking benefit rises to the CPI rather than the RPI will not work if the government proceeds with its (very sensible) plan to incorporate housing costs into the CPI. The overwhelming majority of the difference between the CPI and RPI is due to housing costs being incorporated in the RPI and not the CPI and thus incorporating housing costs into the CPI will eliminate most of the savings from switching measures. This will mean the majority of the hoped for £6 billion worth of savings will not materialise under existing plans. Only if rents and house prices rise more slowly will the new (and more accurate) CPI rise at a slower rate than the RPI in recent years – allowing for these savings to be realised for government. The reforms set out in this paper are therefore essential to safeguard billions worth of existing savings that the government has pencilled in from welfare.

Further, if the CPI includes housing costs and reforms in housing are not undertaken, then it is likely that the Bank of England will be forced to raise interest rates higher than it otherwise would – as once housing costs are incorporated into the CPI it will be more likely to rise above the 2% inflation target. Since 2000, the average annual RPI change (which includes housing costs) was 3% or over in five out of the ten years.[190] Obviously higher interest rates will have a negative impact on the economy over the next five years – an economy which will probably face considerable headwinds in any case.

190 *RP04: Retail Price Index (RPI) all items, percentage change over 12 months,* ONS, 2010

3

More Equal Support for Home-Owners and Renters

If the key thread for future housing policy is helping home-owners into home-ownership if they want, then there must be a more level playing field between renter and owners. Government support must be made more equal so low income households can choose the tenure that reflects their preferences. Presently low income home-owners receive little support from government compared with the assistance that renters receive. Reform therefore would not 'privilege' home-ownership but reflect the wishes of the vast majority who want to own through providing a more balanced support system. The current situation is deeply unfair – for each pound spend supporting home-owners, dozens are spent supporting renters – yet low income owner-occupiers need support too. This rebalancing of support would be paid for by the scrapping of most current expenditure – which is made possible by the reforms set out in Part 2 (4) further below.

Low income owner-occupiers need support if they lose their job – just like renters

An LSE study looked at 93 working families with an average annual household income of around £17,000. During this year, 15 (or almost one in six) had erratic or highly erratic income that fluctuated substantially from its 'average point'.[191] Similarly a different study by Dean and Shah of 47 low income families found around 15% had in the recent past lost a job, leading to a disrupted family income.[192] Yet low income owner-occupiers receive almost no help if they lose work – unlike renters they cannot claim Housing Benefit. Current support schemes only pay interest on the mortgage, and often only apply after a set period of unemployment. This pushes low income households, who often cannot easily borrow and have few savings, towards renting rather than owning, and increases the risk of default for those who do own.

To rectify this situation the government should offer zero-interest loans on a rolling basis, (up to a maximum of £10,000) to households where one or both individuals have lost their job and would have trouble covering their mortgage payments. This should cover all mortgage payments, not just the interest as is the case at present. This would simplify and extend existing schemes. Once a household returned to work then the money borrowed would be repaid by the loan being added to the household's mortgage and the sum lent being repaid back

191 *Tracking income; How working families' incomes vary through the year*, LSE, 2006

192 H. Dean and A. Shah, *Insecure families and low paying labour markets: Comments from the British experience*, Journal of Social Policy, volume 31, pp 61-80, 2002

to government. If the household goes bankrupt, the money lent to government would be recouped from the sale of their property. Households with savings (excluding pensions) of over £10,000 should be excluded from the scheme. They could reapply if their savings fell below this point, so this should not massively discourage savings.

The cost of this would be low. If in any one year 1 million households, less than 5% of all home-owners, took up this support for six months at the maximum rate of £10,000, the cost would be the government interest on the loans during these six months. This support is likely to cost around £200 million (1 million households borrowing £10,000 at 4% annual interest (government schemes can borrow at low interest) for six months gives £10 billion x 2%). This is substantially less than, for example, Housing Benefit. But it would help ensure that low income households do not have to choose between home-ownership and security.

Low income households should obtain help with deposits for home-ownership

As even a 10% deposit for a cheaper home is now at least £5,000 and usually closer to £10,000, an amount low income households will find very difficult to save, it is hard for them to move into home-ownership (even assuming they can get a mortgage with a 10% deposit). Action should therefore be taken to help low income households obtain deposits.

The government should create an interest free lending scheme for low income households of up to £15,000 to put down as a deposit, with around a 70% repayment of each loan made over ten years. 100,000 maximum sized loans a year would cost £1.5 billion initially, though obviously more could be funded since the average loan will be less than the maximum. Over a ten year period the cost should fall to around £940 million a year as funds coming in were partially balanced with funds going out. (Just over 60% of the money lent would return since inflation would erode the value of later repayments). Should a household which had borrowed from the government go bankrupt, the government would receive the value of the loan owed to them.

“The government should create an interest free lending scheme for low income households of up to £15,000 to put down as a deposit, with around a 70% repayment of each loan made over ten years”

If such loans were oversubscribed they would be given out depending on length of time waiting and good credit history. They should also be able to be ‘topped up’ by funds that households have saved themselves. Both these measures should ensure that this scheme does not act as a disincentive to saving. Social tenants benefiting from Right to Buy should also be put to the back of the queue for these deposits, since they are already receiving support in a discounted purchase of their property. Additionally households with substantially above average income or large alternative sources of equity should not be eligible for these loans, as otherwise these households will borrow money that could be better targeted at low to middle income earners.

Low income owner-occupiers should get help with repair/renovation costs

Concerns over the cost of repairs and renovations to their home explain why many social tenants are concerned about becoming home-owners. Repairs and renovations for renting (social) tenants are covered by government, whereas home-owners have to cover such costs themselves.

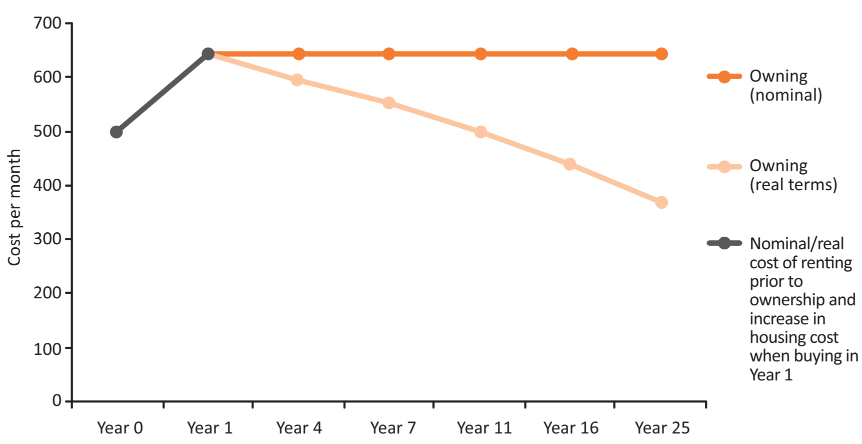
To help low income home-owners with these costs a scheme identical to that of deposits should be set up, with up to £15,000 lent at 0% interest to cover repairs and renovation, and a 70% repayment of each loan required over a ten year period. £1.5 billion should go on this, allowing a minimum of 100,000 such loans a year – with the cost of the scheme falling to £940 million a year over a ten year period just as with the deposit scheme. Length of time waiting would be the key criteria, with those on incomes above a set threshold excluded.

This would help reduce concerns over repairs and renovations and lead to a more equal system between low income (social) renters and home-owners rather than the currently heavily imbalanced system where renters pay nothing and home-owners pay all. Further, encouraging social households to buy their home through this scheme would save government money, as they would share the cost of repairs with government (unlike most social tenants who do not contribute to the cost of repairs to their property at all).

High initial mortgage costs should be smoothed out over time

Over several decades the cost of housing through owning with a mortgage or renting is equivalent. The cost of ownership steadily declines throughout the lifetime of the mortgage whereas rents rise year on year. However, with a mortgage the real term cost of ownership is initially higher than renting. (If this were not the case, almost no one would rent).

Figure 6: Cost of home-ownership over time



This is illustrated in Figure 6. Here, we assume a household moves from a small £500 a month rental property to a small hypothetical £100,000 flat.[193]

193 This example assumes a long run average of 6% interest. The cost of owner-occupation is calculated using Consumer Financial Education Body calculator available at http://www.moneymadeclear.org.uk/tools/hometools.html. Assumes 2.5% inflation.

The household sees a large leap in housing costs from renting to owning in the first year – the 'peak' of housing costs, and then a steady nominal and declining 'real terms' burden. Table 15 shows how real terms mortgage costs in this hypothetical flat decline over time from a high in Year 1.

Table 15: The monthly cost of owning a £100,000 property with a conventional mortgage

	Year 1	Year 2	Year 3	Year 4	Year 7	Year 11	Year 16	Year 25
Owning (nominal)	644	644	644	644	644	644	644	644
Owning (real terms)	644	627	612	596	553	499	439	368

Of course, should the household remain renting, they will pay gradually rising rents, so that overall, renting over an entire lifetime is a much worse option than purchasing a home outright. But the way that repayments are structured over time acts as a barrier to low income households. Such households cannot easily reduce their discretionary spending to pay more for housing costs in the first few years of home-ownership, because they have low levels of such discretionary spending to begin with. For low income households the initial move from renting to owning that costs, for example, £144 a month is often too much, so they stay permanent renters.

To deal with this, government-owned banks should create a new mortgage for low income households where repayments start off roughly equal to renting costs and then rise by a set amount each year, (e.g. 3%), until they reach a level that would repay the mortgage in the remainder of the term, (probably around years 15-18). At this new higher level repayments could then remain stable till the end of the mortgage. This would be entitled a 'smoothed-payment' mortage (SP mortgage), as it spreads the cost of repayment more equally over time. While the annual rise would have to be ahead of inflation as paying now is worth more than paying later, this would still benefit the household compared with renting throughout their working life. Table 16, using the same assumptions as Table 15, shows how a typical mortgage works compared with an SP mortgage set to rise at 3% a year. It shows how the SP mortgage stops any initial 'spike' in housing costs but results in higher repayments in later years. This would allow low income households to own property, without moving into ownership causing a sharp initial fall in their disposable income.

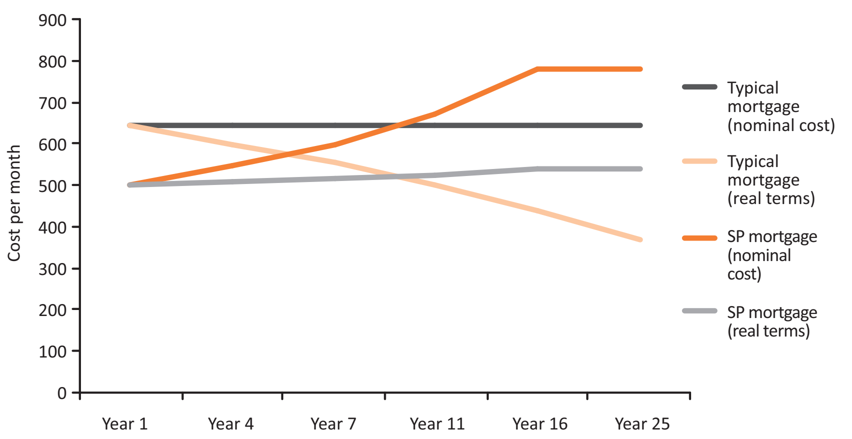
Table 16: Cost of owning £100,000 property under different mortgage options[194]

	Year 1	Year 4	Year 7	Year 11	Year 16	Year 25
Typical mortgage (nominal cost)	644	644	644	644	644	644
Typical mortgage (real terms)	644	596	553	499	439	368
SP mortgage (nominal cost)	500	546	597	671	778	778
SP mortgage (real terms)	500	507	515	525	538	538

194 Table 16 assumes a long run average of 6% interest. Inflation is predicted at 2.5% in terms of nominal cost, and the SP mortgage repayments rise by 3% a year. The cost of owner-occupation is calculated using Consumer Financial Education Body calculator available at http://www.moneymadeclear.org.uk/tools/hometools.html

For an SP mortgage, repayment would look different to a typical mortgage – the difference in housing costs over time compared to a typical mortgage is shown in Figure 7, (Year 16 is shown as the level at which house prices will stabilise, though this is a rough estimate). As even a 3% rise every year would generally be lower than annual wage rises, the real cost of owner-occupation should rise slower than incomes, ensuring affordability for low income households whilst also ensuring repayment of the original debt. This scheme should not make any difference to the bank's balance sheet – it still gains the same assets and pledged repayment, it is merely paid in a different way – and so this should not impact on our ability to resell the banks back to the private sector in the next few years. Of course, there is the question about why banks have not done this in the past. The likely answer is that until 2001 mortgages grew steadily as the proportion of households, and from 2001-07 equity withdrawal exploded. Put simply, the banks were already seeing a steady and consistent growth in their mortgage markets – there was no need for them to think creatively around how to engage low income households as their markets were growing naturally at a healthy rate.

Figure 7: Cost of home-ownership with 'smoothed-payment' mortgage



These measures should be aimed at those with low incomes *not* poor credit history

Some might argue all this will allow 'vulnerable' households to buy a home only to then see it repossessed. But this is to mistake who these measures should be aimed at. The government should not require banks to lend to those they would not otherwise lend to. It should not relax credit requirements and it should tighten reserve ratios for banks in general. However, alongside reform of the financial sector, it should do all that it can to remove obstacles to those who have a decent credit record but face specific distortions caused by our existing model of supporting renters not owners (e.g. the cost of repairs is not borne by renters but it is by home-owners).

There are currently two groups excluded from ownership – those who have poor credit history and those on low incomes, (though they very often overlap). Government should aim to help those on low incomes rather than those with poor credit history. The deposit scheme above should not be extended to those with poor credit history, and this should be taken into account when allocating loans. SP mortgages should not be given to those who have poor lending history. If handled correctly, this deposits scheme could even improve credit systems, meaning if low income households want to obtain government support they will have to behave prudently – reinforcing rather than weakening positive behaviour.

With reforms to support home-owners who get into difficulty, the numbers of repossessions in difficult economic circumstances should fall. Additionally, as the supply of new homes rises, house prices should remain stable, meaning less people will have to undertake risky borrowing to finance the dream of owning their own home. Alternatively without reform then if house prices keep rising, the numbers forced to undertake risky financial behaviour in order to own will inevitably increase and, eventually, so will repossessions.

4

Reforming a Failing Social Housing Sector

The measures above will help to increase home-ownership and ensure that low income home-owners get the assistance they deserve. The final piece necessary for an overhaul of housing policy is to radically reshape the relationship between social tenants and their housing. For all but the most disabled tenants, social housing policies should support social housing as a stepping stone into ownership, not make social housing into a long-term destination. These measures should help transfer stock to tenants and enable the scrapping of most existing housing expenditure – saving tens of billions for government.

Social housing should continue to prioritise the long-term severely disabled

The long-term severely disabled – those with severe physical or extreme mental problems should continue to be prioritised over and above other applicants. The poverty trap and incentive effects identified for social tenants earlier do not apply to this group, who need stable government support for life. In 2007-8 just 30,000 of those entering a new social tenancy (out of 250,000) were unable to work due to sickness or disability.[195] Many of these are likely to be suffering from conditions (e.g. stress, back problems) that should not prevent them from returning to full time work in the long run. We might assume half of these new tenancies will be for those who are severely disabled and so would continue to be placed at the head of the social housing queue.

Merely receiving Incapacity Benefit should not be enough to be a member of this group. Only those judged to never be able to return to work, (and the criteria should be tighter for areas that are harder to demonstrate conclusively) should continue to be placed at the front of the queue for social housing.

The remaining allocation of social housing should be linked to residence and waiting time

The allocation of social housing for all other households should be based on length of residence in an area, family ties to an area, and on how long the household has been waiting. This system will increase the numbers of working low income households being given social housing – which the public want – as it will be 'needs-blind'. Obviously, because the allocation of social housing will exclude those

195 *Table 752; General needs social lettings 2007/8 England, economic status of household reference person*, ibid

on higher incomes, the social housing sector will still house proportionally more with greater need, but it will also house more of those working and on low incomes than currently, and slightly fewer of those with the greatest need (in the short-term).

Primary legislation will be needed to reverse the provision of existing Acts and the exact details of this should be widely consulted upon before being set into a statutory framework. But the broad principles of reform from a 'needs-based' to a 'location-based' system are clear. This is, after all, merely returning how social housing operates back to how it worked before the needs-based system rose to prominence and the 1977 Housing Act.

The possibility of a regional cap on applicants' incomes should be investigated to stop those who can afford to buy from trying to obtain a social property instead. However, such middle class demand is likely to be limited as there will also be a cap on the value of new social tenancies (as set out further below) and a continuing waiting list will deter those who could buy from doing so.

Changing the 'transfer applicant' system in line with this

Of course, changing how social housing is allocated will have limited effect unless the 'transfer applicant' system is changed as well. This must also be changed so that transfer applicants are prioritised by the length of time that they have been waiting to exchange a property, by spatial needs, and if they are moving from a larger to a smaller property (as tenants tend to want to go the other way). The welfare status of the tenant should not be the key to managing to get to the top of the queue (again with exceptions for the severely disabled). The needs-based system will be dismantled for both those waiting for, and those in, social housing.

Allocation changes will impact on social tenants' (and would be social tenants') incentives

These changes mean that tenants or those on the waiting list will be free to return to work and come off benefits without fear that they or their families will be disadvantaged in terms of being able to obtain a social property. The principle here is simple though radical – to return the social housing system to its pre-1977 state – and ensure tenants are not penalised for working by an unfair allocation system. Some stakeholders will loudly oppose these changes, but government should listen to what the public, particularly those on low incomes, want, and press on. The immiseration of social tenants, often incorrectly blamed on Right to Buy is a direct consequence of the perverse allocation system that was put in place in the late 1970s and it needs to be reversed.

Creating a longer-term Housing Benefit for some private tenants

One effect of these changes in the allocation system is that those on the waiting list who are vulnerable, or have vulnerable dependents, will no longer be put to the front of the queue for social housing. To ameliorate the impact of this, when tenants apply for social housing, those assessed as potentially 'vulnerable' (e.g. those with mental illness, those with children), should be able to apply for a 'longer term' Housing Benefit consisting of private sector tenancies for around three years in a particular house or flat. This would provide medium-term security of tenure and prevent disruption to these households while they waited for a social home or managed to sort out longer-term private accommodation.

These longer term contracts would be handled by an additional lump sum payment to landlords (e.g. £4,000) for each such lease, in return for security of tenure. This should be paid upfront to the landlord. If the landlord had to sell the property then the lump sum would be transferred to the new owner. Under normal circumstances, then there would be no way such a contract would be broken (except for unreasonable behaviour on the part of the tenant). But if for any reason the contract was broken, the lump sum would have to be returned to government with a fine on top. This would give vulnerable households the medium-term support they needed without distorting the social housing allocation system (as occurs at present).

“Vulnerable households would obtain social housing over time if they are not be able to return to the private sector, but they would no longer be put to the front of the queue. This removes the highly damaging incentives built into the current system”

If 250,000 such contracts were created annually each with lump sum payments of £4,000 this would cost around £1 billion a year. The government should budget accordingly. In years where there were fewer contracts made, a reserve should be built up in case the numbers of claims surges. This cost is much less than the current system but it achieves the same target – short-term stability for vulnerable households. Vulnerable households would obtain social housing over time if they are not be able to return to the private sector, but they would no longer be put to the front of the queue. This removes the highly damaging incentives built into the current system, while in the long run still giving such households social housing if they need it.

Housing association stock given away in stock transfer should be returned to government

Allocation changes are the first part of reform in social housing. The second part needs to be a drive to increase home-ownership for those social tenants who want it – including for those renting from housing associations. Housing associations have failed as a group to improve the poor levels of deprivation and economic inactivity among their tenants any more than local authorities. They were a worthy experiment but they have clearly failed to achieve their goals. All housing associations created since the 1980s via transfer of local authority stock should have their assets transferred back to central government (though not their day to day running). Primary legislation can overrule any legal issues that might otherwise arise. This would transfer to government an estimated £77 billion of assets,[196] and £41 billion worth of debt.[197]

Those housing associations not formed from local authority stock, (e.g. the Peabody Trust) should keep their largely charitable status and their own rules, on the understanding they will develop plans to encourage their tenants into home-ownership as appropriate. Where housing associations have merged, then the value of the stock that was transferred should be calculated and

196 *Funding Affordable Housing – New Options for Housing Associations*, PWC, 2008

197 *April 2009 Survey of Housing Associations*, Tenant Services Authority, 2009

transferred back into government hands, though where the exact value of this is unclear the government should err on the side of caution when calculating its share. The Joseph Rowntree Foundation estimated that between 1991-2006 housing associations more than tripled their share of stock to around a third.[198] This means in 1991, (3 years after the 1988 Housing Act began the process of stock transfer) around 10% of social stock was held by housing associations.

The purpose of this transfer is that these assets are to be divested to those who live in them should they wish to purchase them, or else transferred into a new and better social model (the Path to Ownership model discussed below). The transfer of these assets was done as part of an implicit deal (that housing associations would improve the outcomes of those who lived in them). With some exceptions, housing associations have failed to do so (despite owning large amounts of stock and generally having tax-free status). The failure of housing associations to improve on these outcomes necessitates the government taking back this stock as part of new schemes that will finally improve the outcomes for social tenants.

The debt of housing associations should be ring fenced and kept separate from the national debt as a whole. It should be paid off within a couple of decades using housing association tenants' rents (including the £5 billion on housing association tenants' Housing Benefits). (Using a mathematical calculator, to pay off £41 billion worth of debt at 5% interest, then if we pay £3 billion a year – feasible from existing rents, we clear this debt in 17 years). As discussed later on, housing association stock will steadily be transferred to its tenants – meaning revenue will come from rents in earlier years and fall over time, so that the paying down of this debt should be frontloaded. Because of this ring-fencing of rents to pay off debts, no further gains to the Exchequer are predicted from housing association rents accruing to government from this reform. This is not a 'nationalisation' in the typical sense – the goal is to transfer the stock to government, who will then administer its redistribution to the tenants who live within it.

New tenants should be offered a 'Path to Ownership' model of social housing

For existing social tenants then a revamped Right to Buy should help them into ownership. But for new social tenants a new model should be created to help them into ownership – a 'Path to Ownership' model. This new model will both move social tenants who pay their rent automatically into home-ownership while removing the current £60,000 or so upfront subsidy needed for each social home constructed.[199]

In the short-term government needs to build more social homes. The waiting list will fall over time as we build more private homes and house prices rise more slowly than has been the recent case. But in the short run, massive stock sales (proposed later on) are only politically feasible and can occur without sharp rises in waiting lists if we deliver more social homes. Central government should therefore push councils to come forward with new plans to expand the stock of social housing – but use a radically different model to deliver this.

198 *Maturing Assets: The evolution of stock housing transfer associations*, Joseph Rowntree Foundation, 2003,

199 *House of Commons Written Answers, 20th April 2007, Column 793*, Hansard,

Local government would propose new homes under the new planning system, which would cut the cost of acquiring land with planning permission (as they could simply apply to change the designation of land they already owned). The ballot of those 'directly affected' is probably best won by rewarding residents by recycling planning gains from other homes built alongside this new social housing stock, and by ensuring new social homes are of a decent quality. Central government would then fund the building of these new social homes by local government by issuing short-term bonds (e.g. lasting 2-3 years) against these new homes. This would enable the interest rate on these bonds to be set at central government rates – around 4% or so. The initial social rent would be based on the interest for these government bonds. This issuing of bonds to fund properties is something that is already occurring with housing associations, but because these institutions are still viewed as more risky than government, they pay a substantial premium over government bonds, meaning a national scheme would cut the costs of new social homes.[200] Further a single central government scheme would be cheaper to administer.

With the social rent on each property based on the interest rate paid on these bonds this should still allow for a substantial gap between market rents and social properties. To give an example, if a new terraced house in cheaper parts of the UK cost £80,000 to build (including cheaply acquired land), this cost would be 'the principal debt' against the property. Government would purchase this asset and issue bonds against this principal debt. The tenants who live in it would pay social rents on the interest on these bonds set based on a rough 4% interest rate (the rate at which the UK government can borrow funds). This would work out at around £266 a month, or £61 a week,[201] slightly below the current average social rent in most of the UK. Of course more expensive parts of the UK would see higher rents than cheaper parts of the UK – but this is not a change as it is already the case now (e.g. social rents in the South East are higher than in most areas at roughly £78 a week). This scheme would work in aggregate, so rents were paid into a pot of money that was constantly being refinanced with new bonds as new homes were built and prior bonds matured. How the scheme works for a new property is shown below:

New social home costs £80,000 → 'Bought' by central government for £80,000 → Central government issues bonds worth £80,000 → Rent for social home equal to interest on bonds

The cost to the tenant of purchasing the property should be frozen at the cost of construction, leading to home-ownership being increasingly affordable over time, since tenants' income will rise each year, but the cost of purchasing their home will not. Tenants could at any point opt to buy their property via a conventional mortgage if they felt they could afford to do so.

Alternatively, as social rents continue to rise at close to their recent rate of 3.5% a year this would generate a surplus payment over and above covering

200 See for example *Licensed to pay the Bills*, Inside Housing, 19th March 2010

201 Cost calculated using Consumer Financial Education Body calculator available at http://www.moneymadeclear.org.uk/tools/hometools.html

the interest payments on the bonds. This would be put toward paying off the principal debt owed by the tenant against their home. This would move tenants automatically toward home-ownership. For example, if after ten years the monthly rent on an £80,000 property rose by 3.25% a year to £366, while the cost of interest payments remained £266 this would allow £100 a month, or £1,200 a year, to go toward reducing the principal debt. Over time, as the principal debt reduced the number of bonds needing refinancing would fall, meaning that less rent would be needed to pay interest on these bonds. Thus more and more of the rent could be used to pay off the principal debt. If after ten years only £72,000 worth of bonds were needed, the monthly cost of interest payments would fall from £266 to £240 a month. Thus every month an extra £26 could be paid off the debt on top of the £100 being put toward paying off the principal debt due to rising rents. This works in the same way a normal mortgage does – over time, more and more of the payment goes toward paying off the principal debt, and less and less toward paying off the mortgage.

Tenants could also opt for higher rents to slowly erode the value of the principal debt, should they feel they were not financially secure enough or financially aware enough, to take on a typical mortgage but wanted to move more quickly toward home-ownership. For instance, a tenant might opt to pay an extra £30 a week for example – around £1,500 in the first year. Because over time this would reduce the principal debt outstanding, fewer bonds would need to be reissued, reducing bond interest payments, and meaning even more of the rent would go to pay off the principal debt. Even a small extra sum like this would very quickly begin to pay off the principal debt used. (Again, this is how a normal mortgage works.)

However, repayment of the initial debt would only occur in those months where tenants were actually paying rent themselves. If the tenant was economically inactive and Housing Benefit was paying the rent, any surplus above the cost of paying interest on the bonds would not go toward paying off the principal/initial debt. The government would simply pay Housing Benefit up to the cost of interest on the bonds, and save the rest. (Over time this might help reduce Housing Benefits, though this would take a long time before such savings became notable and so we exclude it from our savings later on.) The government should consult and investigate options where Housing Benefit is paying part of the rent as this offers a challenge – on the one hand even part-payment of the rent by tenants is a good thing – on the other, getting tenants to pay their (subsidised) rent in full is also optimal (especially if this can be done if the tenant increases the hours that they work).

The key point is that this mechanism would strengthen social tenants' incentive to work. Every time they paid rent they would move a little closer to ownership. Moreover, any amount a social tenant pays off from the principal debt would be passed on to their children or relatives if they died before the property was fully transferred to them. Beneficiaries of a deceased tenant should also be offered the chance to move into the property themselves and take on repayments if they wish (and if they were social tenants too, any accrued payment of the principal in their existing home would be transferred as well). This scheme would thus help families on low incomes build up equity, tied into their social properties. Should beneficiaries of the deceased tenant want to sell the home, they too would gain an additional share of any rise in the value of the property should it have risen (the exact details of this should be consulted on).

Of course, in exchange for not having to pay the upfront cost of subsidising social homes, then the government will no longer gain rents from these properties, and will have to pay separately for the upkeep and repairs to the house. This might be estimated at £2,000 or so a year, or £40 or so a week. This is almost certainly an overestimate, but it is better to err on the side of caution. After a certain point, perhaps when tenants have paid off half the principal of the loan, maintenance costs would begin to transfer to the tenant – on a sliding scale. Thus by the time tenants reached 75% ownership, this would mean repair and renovation costs were equally split, and by the time they fully owned the property, these costs would be entirely on tenants' shoulders. The schemes set out in Part 2 (3) should reduce tenants' concerns over this.

At a time when the UK government is essentially contemplating a 25% cut in Departmental spending, the loss of small net future rents compared with no longer paying for massive upfront building costs is very little to bear. As we will see later, net rents are just £1,250 or so a year for the average social property – compared with the £60,000 in upfront costs we saw earlier for each new social home. Without changing to this model, or something like it, then housing cuts will decimate the very low levels of new social homes being built at a time when waiting lists stand at nearly 1.8 million households. Further this model is preferable for other reasons. It makes social housing into a clear 'Path to Ownership' for tenants and would substantially change for the better the terrible incentives social tenants currently face.

The goal should be that this model should allow upwards of 100,000 new social homes to be built every year, and that as existing stock becomes vacant through the death of tenants it moves into this Path to Ownership scheme (discussed later in this section). An increase to 100,000 new homes is a roughly four-fold increase on the 26,000 new social homes built each year from 1999-2000 to 2008-9.[202]

All new social tenants should be entered into the new Path to Ownership scheme. However, not every tenant would own in the medium-term. Non-working new tenants (particularly those who have retired), could simply live in a social property until they die (though see the section on the Right to Move below), with their social property taken by another social tenant after them at the initial cost of construction. Of course, for new economically inactive social tenants who rely on Housing Benefits, this scheme will still mean that Housing Benefit has to cover their costs. But these individuals require Housing Benefit to support them in any case. Further, as paying private rents will often be higher than the interest on the bonds for these new homes, expanding social housing in the way outlined under this scheme could actually save money (though this is unlikely to be a large sum overall and so is excluded from any calculation of savings from this paper so as to err on the side of caution).

The government should set aside £4 billion a year in the medium-term to support the Path to Ownership scheme, allowing 2 million households' maintenance and repairs to be fully supported at any one time. Obviously, as tenants move into or toward ownership, this £2,000 maintenance fee will be

202 *Table 1006; Additional low-rent dwellings provided by local authority area*, DCLG, available on their website

reduced and over time the numbers coming into the scheme should be balanced by those moving out. As in the first few years there will be fewer tenants being supported than the 2 million this scheme will eventually support, funding for this scheme should start at £1 billion and rise to £4 billion over ten years, saving money in the next few years when government finances are tight.

Continuing to raise social rents at 3%-3.5% a year is essential to raise home-ownership

As housing supply expands, the rate of private rent increases should reduce to perhaps around 1%. However, social rents should continue to rise at 3-3.5% a year toward market rates. Such rises should be above inflation but below wage rises so that working social tenants still gain from employment. Those who are on benefits will not see their living standards fall as they will be protected by Housing Benefit. This is essential both for the success of the Path to Ownership model and for existing tenants being offered a revamped version of the Right to Buy.

This will make for a level playing field between renting in the private and social sector over the medium-term, as various individuals have suggested should be the case – but through reducing the rate at which private rents rise, not accelerating the speed at which social rents increase. The aim should be that in the long run, subsidy of individual households can be reduced – but this can only be done without hurting the poor by doing it over time and only as ownership and private renting becomes affordable for those on low incomes. The time that would be needed to converge social and private rents would differ as social tenants in different parts of the UK receive different levels of subsidy but within a couple of decades the level of subsidy for most social tenants should have dwindled to next to nothing. Obviously, for Path to Ownership tenants then the convergence would be different as it would take place over the duration of the tenancy as rents rose from the initial cost of construction. But over time each social tenancy would see rents rise to market levels.

Stopping the creation of expensive new social tenancies which prevent ownership

A maximum regional cap should be put on the value of social properties being built for participation in the Path to Ownership scheme. This should be around the lower quartile to average house price in each area. For example if it was set at the median house price in each region then in the North East this would mean that no social housing could be constructed with a value above £115,000. In London, no property could be constructed at a cost of over £250,000.[203] Government should consult to see if these values are too high (they are clearly not too low), and it should also make clear to local authorities that the higher the average value of the property they propose, the fewer properties they will be allowed to build. Central government can do this as it will control the issuing of bonds to fund these properties. As discussed further below, not only would councils be prevented from developing properties that are more expensive than this regional cap, but in addition, more expensive social properties valued above this cap should be sold off as the existing tenants living in them die.

203 Table 582 Housing market: median house prices based on Land Registry data, by district, from 1996, DCLG, available at their website

In Part 1 we saw that the average cost of subsidy at present for each social property is around £60,000, so the cap would allow an increase in the cost of the average social property constructed (though any cost of construction would no longer have to be covered immediately as set out in the Path to Ownership scheme). This means that this cap would allow decent quality social housing while achieving the goal of preventing expensive social properties.

Such a limit on the value of such properties is necessary for various reasons. Firstly, it ensures that low income households will be able to buy Path to Ownership properties over time. Secondly, it ensures that rents based on the interest paid on the bonds needed to finance these properties will not be so high as to drive tenants into poverty. Thirdly, government support should not end up subsidising housing that is better than the average home-owner can afford. Finally, these measures will reduce demand. Without some kind of cap, councils may end up housing more affluent households. Social housing should be for working low income households, not middle class ones. This cap will ensure that middle class households do not try to obtain subsidised housing.

This financial cap will also create a three/four bedroom cap as the maximum size of a social property, as in no region homes bigger than four bedrooms could be provided to those in social housing within this cap. This cap follows similar recent changes in Housing Benefit. At present, families are dishonestly encouraged to believe that they don't need to limit their family size and the council will always provide. Government cannot provide ever bigger homes for social tenants. And neither should it, particularly under current financial circumstances.

For this to work there is a need for a further change in how social housing is allocated in London and potentially more affluent district councils. The new cap would mean that in more expensive London boroughs and possibly in the most expensive parts of other regions (e.g. some district councils in the South), social housing will no longer be an option because it is impossible to build a property that would fall under the regional cap.

Therefore, the allocation of social housing in London should shift from the boroughs to a single London-wide allocation scheme run by the Mayor's office. Tenants would no longer be seen as from particular boroughs, but instead as part of a London-wide allocation system, though obviously they would have preference for which area (e.g. west, east, south, north) they wanted to live in, and this should be respected. Similarly, if there are particular parts of the UK where all social property would be above the regional cap, then administration of social waiting lists within that area would have to be merged with surrounding areas so that claimants could live as close as possible to their desired location without obtaining a property more expensive than the regional cap in their area allows.

These changes will enable the scrapping of most current housing expenditure

As detailed at the start of this paper, current expenditure on housing is around £9.3 billion a year. However, as part of these reforms this support can be largely withdrawn – as affordable homes will no longer be centrally supported, and social homes will be funded using the bond mechanism outlined above rather than direct and immediate subsidy. The main reason for continuing to spend on these schemes is to finish the 'decent homes' programme. Fortunately, only 12-14% of council homes are now not expected to be 'decent homes' by this year, down from 42% in 2004.[204] This expenditure can therefore be reduced and post 2010 spending can be targeted on vulnerable households, especially as the proportion of 'non-decent homes' in social housing was already lower in 2007 than in any other group. In terms of maintenance, as changes set out below sharply reduce the size of the social housing sector over time and after providing the funding set out above for maintaining the new Path to Ownership homes then government could cut existing housing spending.

" Current expenditure on existing programmes can be cut to some £1.5 billion, enough to maintain a diminishing level of existing stock, build a small number of homes for severely disabled households, and aim for the achievement of the 'decent homes' standard for all vulnerable social households by 2015 "

Current expenditure on existing programmes can thus be cut to some £1.5 billion, enough to maintain a diminishing level of existing stock, build a small number of homes for severely disabled households (equipped for their needs), and aim for the achievement of the 'decent homes' standard for all vulnerable social households by 2015 and all social households within a few years after that. This cuts £7.8 billion per year from 2009 levels of expenditure.

A renewed Right to Buy: Restoring the value of the Right to Buy discount

The Path to Ownership model will help new tenants into home-ownership. For existing tenants, a renewed Right to Buy will help many existing tenants own their own home.

The first part of a renewed Right to Buy is to restore the value of the Right to Buy discount. The current nominal 33%/40% discount has in practice been capped at low levels across the UK (e.g. London and Birmingham – £16,000, North East – £22,000).[205] Following sharp house prices in recent years this makes the Right to Buy very difficult to exercise for most tenants. This explains why recently each year just 10,500 or so households took up the Right to Buy. The value of the discount should be restored for existing tenants. As a suggestion, discounts should be around 33% or £40,000 for most of England, 40% or £70,000 for the East and South East, and 50% or £125,000 for London. The exact levels should be consulted on, and once set should rise with any house price inflation, but the aim should be that they should allow most tenants to buy their home.

As highlighted in Part 1 (3) the rental subsidy for social tenants is currently concentrated in particular areas. This means that a more substantial discount would allow many tenants to own at a basic cost similar to continuing to rent. Based on the 2004 Hills valuations of social housing stock, then with the more substantial discounts suggested above are in place, then in three areas (North East, North West and Yorks and Humber), there will be almost no difference between

204 *The Decent Homes Standard; House of Commons Standard Note SN/SP/3178*, House of Commons, 2009

205 Your right to buy your home, DCLG, 2009

renting and buying for a tenant living in the average social property, while across the Midlands there will be a moderate but not substantial difference. Only in the East of England, the South East and South West and in London will buying still be very costly after more fair discounts are applied (e.g. a difference of £35 a week in the South East). This is what we should expect given levels of subsidy across the UK – which is largely biased toward the South. Of course, this assumes Hills' valuation is correct at present given recent house price rises and then falls. But even if they are not, discounts should not have to be amended too far. The key point is where social tenants are receiving limited subsidy, once reasonable discounts are applied then the gap in terms of cost between home-ownership and social renting will be small.

Table 17: Weekly cost of buying average council property with new discount versus social renting

Region	Average capital value (£,000) of council properties in *Hills* (2004)	Average capital value (£,000) minus max suggested discount[206]	Average cost of servicing mortgage (weekly)	Average rent (weekly) in 2009[207]	*Weekly difference between purchase and renting*
North East	58.6	38.6	£57.3	£57.4	*£0.1*
North West	65.1	42.9	£63.7	£60.2	*£3.5*
Yorks & Humber	62.2	40.7	£60.4	£57.9	*£2.6*
East Midlands	77.7	51.2	£75.4	£61.5	*£14.9*
West Midlands	73.9	48.7	£72.4	£63.8	*£9.4*
East of England	128.2	76.9	£114.2	£71.9	*£42.3*
London	165.2	82.6	£122.7	£85.0	*£37.7*
South East	128	76.8	£114.1	£77.7	*£36.4*
South West	100.8	66.5	£98.7	£66.2	*£31.5*

1) Cost calculated using Consumer Financial Education Body calculator available at their website.
2) Figures assume 6% interest on mortgage and 25 year repayment mortgage. Obviously at present this cost is even less due to low interest rates.

Moreover, not only would many social tenants find it cheap to move into ownership immediately after these reforms were brought in, they would find it easier to do so with each year that passed. Following these reforms social rents should continue to rise in the medium-term by some 3-3.5% a year (or roughly ahead of inflation but below wage growth), while house prices remain reasonably stable due to a steady expansion of supply. This means that social rents rise faster than house prices each year, so owning should become progressively cheaper when compared with social rents.

Thus tenants who buy in parts of the UK where socially renting/having a mortgage have initially comparable costs would actually be better off over time. Such tenants would not see rents rise year-on-year, but would have stable housing costs based on a mortgage. For example, an average household in the North East that bought under these discounts would pay £57 a week in five years time if they bought their property now, but £68 a week in social rent if rents rose by 3.25% a year) – a difference of £10 a week. This would substantially help improve many working low income households' income over time.

206 Uses new discount set out in this paper of 33/40% or £50,000 or £75,000

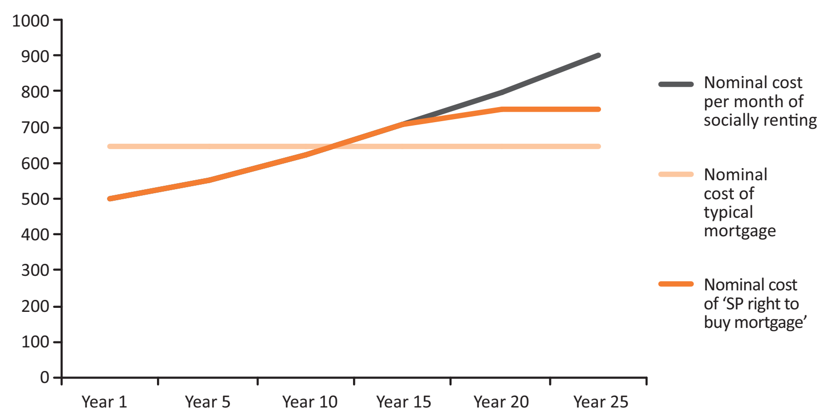
207 *Table 703; Registered Social Landlord rents and Table 701; Local Authority Average Weekly Rents by Region*, DCLG, available on their website

However, for the parts of the country where moving into home-ownership would cause a notable rise in housing costs, a new smoothed-payments Right to Buy mortgage is needed to ensure that any rise in housing costs is spread in a way that low income tenants can afford.

A renewed Right to Buy: A new smoothed-payment Right to Buy mortgage

As part of the renewed Right to Buy tenants must be offered a way into ownership that does not immediately and substantially raise their housing costs. This can be done through offering a form of the smoothed-payment mortgage discussed earlier, where repayments rise over time – in this case, pegged to social rents. This would mean social tenants who become home-owners would never pay more for their housing than they would as social renters. Obviously, this would be of most use to tenants in more expensive parts of the UK, such as the South East, who would otherwise see their housing costs rise sharply if they bought their home, even under proposed new larger discounts. Again this new smoothed-payment Right to Buy mortgage could, if necessary, be offered initially by government owned banks.

Figure 8: Housing costs over time under three different options



For those who get a mortgage under this scheme, mortgage repayments would start at the same level as social rents and rise in line with social rents over time – until they reached a level where repayments would then be enough to pay off the mortgage within a typical 25 year term. How this might work for households in an expensive area is shown on Figure 8. A household buying an average property in London under this scheme no longer sees housing costs jump steeply when it moves to become an owner-occupied household, but instead carries on paying at social rent rates, rising at 3-3.5% a year every year. The amount paid each month should reach a stage where this rate will pay off the remainder of the loan within 25 years from the start of repayment (like a normal mortgage). At this higher level repayments will then stabilise. Figure 8 sets out a rough illustration of how this would work with a hypothetical property where social rents are £500 a month and to purchase this would raise housing costs to around £650 a month. The smoothed-payment mortgage repayments track social rents until they diverge after Year 15, where they stabilise at a rate higher than the initial cost of home-ownership that allows the remainder of the mortgage to be paid off within the typical 25 year timeframe. (This is a rough illustration not a fully worked out example of how this might operate.) Figure 8 shows how repayment schedules differ over time in the different schemes.

The same initial loan is paid off under this scheme, and the amount of interest is actually slightly higher, but the key reason why it makes owning more attractive to low income households is that at any one point in time home-owners never pay more than social renters. Together with the new more substantive discounts put in place, this means that low income working tenants across the UK should be able to purchase their house at no extra basic cost compared with continuing to rent. Of course, there will still be the possibility of additional costs due to repairs and so on – but some of these concerns should have been addressed with the schemes in Part 2 (3) to help low income owner-occupiers.

This pegging of repayments to social rents can also be used to help tenants in cheaper areas if a conventional mortgage of 25 years is too short for a particular household – e.g. if a tenant in the North East has only 20 years of working life remaining, and so would have trouble paying a typical 25 year conventional mortgage, they can buy their property under this scheme and see their rents rise for the first few years in line with social rents, ensuring they pay off the mortgage on their property within 20 years. This should be encouraged as it is likely that otherwise such tenants' housing costs will have to be covered by the State in their retirement.

A renewed Right to Buy: The 'Right to Move and Buy' for those in expensive homes

The two measures above will allow almost all social tenants to become home-owners at no extra cost, within the framework of greater support for low income home-owners outlined in Part 2 (3). But a small number of tenants in expensive social properties are unlikely to be able to purchase them, even with the changes outlined above. This means that the pathway to ownership for these tenants would remain closed – removing much of the incentive for tenants these schemes create, and unhelpful given the poor incentives and high levels of poverty and economic inactivity among many tenants in some affluent areas (e.g. Inner London).

The solution is for all tenants to be offered the 'Right to Move and Buy' – whereby any social tenant could move to another area and take the discount they are entitled to from their current home with them. It should be emphasised that this is only an option, and if tenants wish, they should be able to stay in their existing property until they die. This expands the choice for *all* social tenants as any tenant could be able to move to another property that they liked. But it particularly expands the choices available for tenants in these expensive areas who could not afford to buy their current property, but would gain a large discount if they moved from their current property to a similar one in a nearby area.

For instance, a working single mother in a two bedroom £230,000 flat in Hackney could take her 50% discount (£115,000) to buy a flat or house further out of London. With this discount she could obtain a property worth perhaps £155-165,000 (with a mortgage of around £40,000 – £50,000). Her mortgage payments could be contained in the first few years by the effects of a Right to Buy smoothed-payment mortgage, ensuring this is an affordable option for her in the first couple of years. Her moving is a win-win as government gains half the value of the property when it is sold off, and she gains home-ownership in a property that she wants.

An added strength of this system is that the very option of home-ownership also acts as an incentive for those living in more expensive areas to move into employment as well – because they can then move and buy a property should they want to do so. For social tenants who do not like their existing home but would like to become home-owners it reinforces any moves into employment – as it is only working tenants who will be able to exercise the Right to Move and Buy. Indeed, it is likely that there would have to a be a minimum period of employment preceding the Right to Move and Buy (e.g. 12 months), so that tenants do not exercise this too soon after returning to the labour market, before they are settled in employment.

The transaction costs for tenants who want to use this route can be rolled up and subtracted from the discount of the tenant. To make this simpler, this might be done via a flat levy – and some of the money raised from this be used to support the costs of introducing a Right to Move for social tenants, as explored below. This Right to Move and Buy would have a major effect on improving tenants' welfare, and increasing the numbers who would want to move into home-ownership by widening the choices open to them.

These reforms could also allow the Right to Move to operate effectively

An exciting idea first proposed by Professor Tim Leunig in a 2009 Policy Exchange paper was the Right to Move. This was explored within the paper and will not be repeated here in detail. Essentially, this would allow tenants to transfer their social tenancy from one building to another, requiring the government to sell their existing property and purchase another of equal or lesser value, with the tenant then moving from one to the other.

There is no doubt this would improve quality of life for social tenants. As the paper pointed out, it would improve the ability of tenants to move if they wanted to, bringing serious welfare gains to tenants (e.g. a social tenant who wanted to move closer to an elderly relative to care for them could do so using this new right). The two main problems were a cost of around £400 million a year (potentially much more in the first year), and that it would have made obtaining a social property even more desirable than currently.

But if the reforms proposed above are enacted, this will eliminate the negatives of the Right to Move. Firstly, the reforms remove the distorted incentives social housing creates for tenants and those on the waiting lists, so while the Right to Move might increase waiting lists a little, this will not lead to more people being caught within the bizarre incentives currently in place. In addition, more affordable private housing and greater numbers of social homes being built mean that any rise in the waiting lists due to the Right to Move would be manageable.

In terms of the cost, then the Right to Move and the Right to Move and Buy could possibly be funded from the same stream, with a small levy taken from the discount of those operating the Right to Move and Buy to fund the entire programme. This removes the serious problem of finding several hundred million pounds at a time of severe financial strain.

One final point is that social tenants should have a cap on the value of the home that they could move to under this Right to Move. This should be around (though possibly higher than), the value of the regional cap for their area. This would enable tenants to move without allowing them to purchase properties that they could never afford to own in future, or properties that were well above the average value in their area. Otherwise the risk is that those who have struggled to buy their own home previously may well (justifiably) resent those in social housing moving into nearby homes that they themselves could not afford. Having no cap on the Right to Move could also act as a deterrent for tenants to exercise the Right to Move and Buy by allowing them to move to more expensive and better homes if they move and stay social tenants than if they purchased a property outright. This would be counter-productive.

A renewed Right to Buy: Ending mobility restrictions for those exercising the right to buy

Restrictions introduced on allowing tenants to move once they have exercised their Right to Buy should be stopped. These restrictions ignore the fact home-owners may have very good reasons to want to move, such as jobs or family. As tenants are to be offered the Right to Move and Buy, it would be odd to also allow tenants to exercise the Right to Buy and then penalise them for moving afterwards.

The impact of these reforms on welfare dependency in the social housing sector

The impact of these reforms will be to reduce welfare dependency among social tenants. As we saw, social tenants have lower employment rates (even taking account of labour market disadvantages) due to the specific disincentives they face. Taken as a whole, the above proposals should sharply reduce these problems. (Future) tenants would no longer have to worry that the more they help themselves, the more they will be pushed down the waiting lists to get into, or move within, the social housing system. They will have the incentive of owing their property – and if they don't like their existing home, they can move to another one and purchase that one.

The 'unexplainable gap' in employment rates was estimated as around 20-25% for similar households within and outside the social housing sector. This lower rate of employment would generate an additional 550,000 social households reliant on out-of-work benefits.[208] By combining these reforms, which remove the particularly strong poverty trap that has grown up for social tenants and instead offers them a real chance of home-ownership, with a

208 For this and other figures on social tenants socio-economic make-up in this and the following section, see earlier footnotes in part 1 (3) on social housing.

renewed push on welfare-to-work, we should be able to eventually remove perhaps 20% of this 20-25% employment gap within a decade. This would raise the employment rates of social households to just under 70% or so – still around 20% lower than for private tenants. This requires just 55,000 individuals in existing social households to move into work each year – 550,000 over a decade. To put this in context employment currently stands at around 28 million individuals.[209]

In Part 1 (3) the cost of 550,000 additional welfare dependent households was estimated at around £7 billion a year. Removing this would provide corresponding savings. To be cautious about any savings, this excludes increases in tax revenue that arise from getting these tenants back into work. These savings would be gradual over a ten-year period as tenants steadily return to work, rather than all at once. It is also important to note that this £7 billion is not a set figure on welfare savings, nor does it preclude higher gains – other policies that enhance employment and reduce the poverty trap in general will also yield results. This £7 billion is an assessment of how much reducing most of the gap in employment rates between disadvantaged groups in social tenancies and similar disadvantaged groups outside the sector saves.

Assuming that other policies to increase employment among disadvantaged groups are introduced, at least several hundred thousand more existing social households should return to work (a rough estimate would be 300,000, to give an employment rate for social tenant households at around 80%). However, the reforms in this paper would not be the cause of this – and would rely on wider changes to remove barriers to employment and create better welfare-to-work policies. Thus no further savings from welfare are assumed over this £7 billion. Without these reforms social tenants will face additional barriers to returning to work over and above those most low income individuals face. The existing record in reducing the numbers on out-of-work benefits is appalling – as we saw, bar reducing widow's benefit, the government moved only 150,000 off the welfare rolls in an eight year boom. A complete overhaul of how the welfare system works is needed – including changes to the perverse incentives social tenants face.

Existing tenants who don't want to buy won't be pushed to do so

It is important to emphasise that existing tenants will not be required to change their contracts. No social tenants' existing tenancies would change. Should they want to tenants will be able to retain their existing home until they die. Obviously, this will be particularly important for elderly residents, who should not feel that their tenancy is under threat from the widespread reforms proposed in housing policy. The point of these reforms is to expand the options available for social tenants and improve the incentives facing them.

Of course, existing tenants will no longer be able to move to higher value properties, as these will be sold off as they become available. Thus some tenants may not be able to move within very expensive areas, (e.g. if their family expands, they will face a choice between a more cramped home or moving to a less

209 *Labour force survey; employment status by occupation and sex, April-June 2009*, ONS, available at their website

expensive area – though this is no different from the choice most families have to face). But against this, even these tenants will still have additional choice in which property they would like to move to because of the Right to Move set out above.

These reforms create mixed communities – which may work with a change in incentives

In Part 1 we saw how mixed communities were failing at present. But this is because the biggest problem facing social tenants is that of incentives. Under these reforms a large scale social house-building programme will begin across the UK, with councils most likely to be able to obtain planning permission with mixed developments. The Right to Move and Right to Move and Buy will disperse social tenants much more than is currently the case.

The author does not believe that mixed communities are the answer that many believe them to be. Current evidence of their success is clearly weak. However, it could be that once you change the incentives facing social tenants, mixed communities of social/private tenants would lead to better employment levels. It would reduce the stigma of living in certain areas that some social tenants say they feel is displayed toward them. Certainly, as those already living in social housing purchase their homes this would show to other tenants that home-ownership was a realistic prospect for households similar to them, and should act to demonstrate that work really does pay. It is hard to see how overall this could be anything other than a positive development.

How many existing social tenants are likely to take up the renewed Right to Buy?

The revamped versions of Right to Buy will provide a major opportunity for working social tenants to own their home. Around half of social tenants state outright they want to become home-owners. For those who don't, the majority cite perceived barriers to owner-occupancy rather than a positive preference for social renting, indicating they would probably own if they could, something this package of reforms should substantially encourage. Those who actively want to stay social renters tend to be pensioners, who could never buy their home.[210]

Under the renewed Right to Buy, tenants will be able to purchase their homes at no extra cost both now and in the future, knowing that they are likely to be better off doing so in the medium-term than if they stay social renters. They would also be aware that there would be a substantial package to help low income households in place, (e.g. on repairs and for them if they lose work). The Right to Move and Right to Move and Buy would also allow those tenants who did not want to purchase their existing property to buy a different one or move to one they liked (and so would be more likely to want to buy). Overall many working tenants should take up the opportunity these reforms offer to realise their goal of home-ownership.

As stated earlier, there are a total of 1.28 million social households in work, around 33% of tenants. This group is likely to overlap with the 33% of social households that do not rely on Housing Benefit to pay their rent. Additionally,

210 For this and other figures on social tenants socio-economic make-up in this and the following section, see earlier footnotes in Part 1 (3)

reform should raise the numbers of social households in employment by 55,000 each year. By the end of the decade, this would mean around 1.83 million households in employment. The majority of these should want to purchase properties over time, as this would involve no increase in weekly costs for them and there would be major support schemes in operation for them as low income owner-occupiers.

If in the first year just under one in five of the existing 1.28 million existing social tenants in work uses the new schemes to purchase their home, this would transfer around 240,000 households in the first year. This would be around 6% of all social tenants. To put this in context, surveys show that around 50% of all tenants want to own, so this is reasonably cautious. This rate is likely to drop after the first year as tenants who have wanted to buy for some time do so immediately. If the rate then falls to 175,000 households a year, as existing tenants that work and new tenants returning to the labour market purchase their homes, continuing perhaps for another four years, and then falling again to perhaps 105,000 a year for another five years after that, this would mean 1.46 million or so tenants purchasing their property over a ten year period – around 85% of working tenants.

This would only transfer housing stock into the hands of around 37% of tenants over a ten year period – much less than the half who state they would like to buy outright, and even less considering many of the barriers that put off most remaining tenants would be removed within these reforms, (e.g. no jump in housing costs, better support for repairs). Further, this figure of 1.46 million works out at around 146,000 a year, not that much higher than initial Right to Buy sales between 1981-2 and 1990-1, which ran at around 104,600 a year.[211] Moreover, the new revamped Right to Buy is even better value for social tenants than the original Right to Buy as moving into ownership should not increase social tenants' housing costs and will be done within the context of a substantial increase in support schemes for low income home-owners. Those working households who do not take up this offer are likely to be those who were too close to retirement and are so unlikely to take up this offer of home-ownership, or else tenants who are very reluctant to buy.

Assuming that additional welfare-to-work reforms will have returned more social households into employment over the next decade or so, then these households will also want to purchase their home. The total numbers that should be returned to employment were estimated at a conservative 300,000. If these slowly and steadily purchase their homes in the second decade after reform this gives sales of 30,000 homes per year in years 11-20 after these reforms.

Selling off stock on the market or on to the Path to Ownership model as it is released

Around 2% of social housing is released each year due to older social tenants dying.[212] As elderly tenants will largely be unable to exercise the Right to Buy as they are either retired, or very close to retirement, the number of properties released as tenants pass away will be reasonably constant at roughly 80,000 a year for the next couple of decades.

As this stock becomes available, it should be sold off. For stock valued below the cost of the regional cap, this should be then bought back under the Path to

211 *Table 670; Social Housing Sales to sitting tenants*, DCLG, available on their website

212 *Using the British Household Panel Survey to explore changes in housing tenure in England*, LSE, 2007

Ownership model, with bonds issued against the value of the property and the social rent set as the interest against the government bonds in the way set out earlier. For stock valued above the cost of the regional cap, this should simply be sold on the open market. Under both systems the value of the stock will transfer to the government in the short-term, raising substantial sums.

The reasons for stopping tenancies in expensive areas were discussed earlier. The total outflow of stock from this policy should not be too great. Only around 20% of social housing is located in the 50% least deprived areas,[213] which if we use as a rough proxy for more expensive stock, would lead to a net outflow of stock of around 16,000 properties a year. Even if we double this to allow for the fact that in some areas there may be high-value social homes in deprived areas (e.g. Inner London), this would be a net loss of stock from these sales of just 32,000 properties. If we hit the earlier target of at least 100,000 Path to Ownership properties being built then this would still mean that the net gain of new social properties would be over 70,000 extra homes a year – nearly triple the rate of recent years.

What these changes means in terms of stock changes and revenue raised

Firstly, there will be sales to working social tenants and social tenants returning to work. Using the figures for estimated Right to Buy sales set out in earlier paragraphs gives a transfer of stock as laid out in Table 18. Overall, 44.1% of existing stock would be transferred to working tenants over a twenty year period.

Table 18: Net transfer of stock to working tenants (including those returning to work from Year 2)

Year	1	2-5	6-10	11-20	Total
Annual total of stock transferred to working tenants (number)	240,000	175,000	105,000	30,000	1,765,000
Annual total of stock transferred to working tenants (% of current stock)	6	4.4	2.7	0.7	44.1

In addition to these sales would be the stream of sales from properties released as older tenants pass away, which will be reasonably constant at roughly 80,000 a year from 2011-12 (assuming this is the first year of the scheme) to 2031-2. This transfers 10% of the existing stock by 2015-6, 20% of stock by 2021-2, and 40% of stock by 2031-2.

Combined these two sets of sales will transfer around 84% of the existing stock into the private sector or Path to Ownership model within twenty years. This asset transfer will do three things – raise ownership rates, reduce welfare dependency, and bring in large revenues – particularly in the first few years. For the government, these reforms and the revenue they bring could not be more urgent in the face of a £156 billion deficit.

John Hills assessed the social housing sector in the latter part of 2004 as worth £400 billion. House prices are similar to their 2004 valuation, albeit slightly higher at present (e.g. Nationwide judged the average house price in the second half of 2004 as £152,000, by April 2010 this was £162,000).[214] However, using the 2004

213 *The Hills Report into Social Housing*, ibid

214 *UK House prices since 1952, Nationwide*, ibid

valuations when estimating revenue hedges against a modest decline in the next few years. It also accounts for the fact that some of this housing stock will have been held by housing associations pre-1988 housing stock transfers and so asset sales will not benefit government (as these assets will remain with the housing associations that own them). While this stock is less than 10% (and probably only around 5%) this still shaves a notable sum off revenue gains and so our overly-cautious valuation of stock helps ensure our final figures are not over-estimates.

Using this, every 1% transfer of stock from the 3.9 million of households, around 40,000 properties, is worth roughly £4 billion to the Exchequer. If we reduce gains from transfers to working tenants by around 33% or so as these tenants receive a discount on their properties, in the first year each 1% transfer of stock would raise £2.64 billion. If house prices remain broadly stable in future, this figure will be eroded by inflation, perhaps by around 2% or so a year. So every 1% of stock sold will raise around £2.64 billion in the first year, £2.58 billion in the second year (due to inflation), and so on. For the 80,000 properties sold off annually as existing tenants pass away, no reduction in value from sales due to any discount is needed. This would therefore raise £8 billion a year for the next 20 years, declining by 2% a year in real terms for the reasons explained.

Table 19 sets out gains to the Exchequer due to projected sales. To avoid counting sales that would have occurred without these reforms, we need to subtract the value of existing Right to Buy sales to tenants from future gains. Right to Buy sales have declined sharply over time and the average annual total raised in 2006-7, 2007-8 and 2008-9 was just £771 million from around 10,500 sales a year.[215] But if we assume that without these reforms Right to Buy raises £1 billion a year in future once the property market is more stable (though higher prices will eventually choke off even these limited sales), we should subtract this from our overall savings. Regardless of this, revenue gains due to projected sales are very substantial.

Table 19: Revenue from sales of social housing over twenty year period (figures are £ billions to nearest decimal)[216]

	Year 1	Year 2	Year 3	Year 4	Year 5	Years 6*-10	Years 11* -20
Sales of housing stock to working tenants	15.8	11.4	11.1	10.9	10.7	6.4* falls to 5.9	1.5* falls to 1.2
Selling off social housing stock as tenants die	8	7.8	7.7	7.5	7.4	7.2 falls to 6.7	6.5 falls to 5.4
Total raised (subtract existing Right to Buy sales)	22.8	18.2	17.8	17.4	17.1	12.6 falls to 11.6	7 falls to 5.6

* Of course in reality the declines seen in Years 5 to 6 and 10 to 11 are not likely to be as steep and abrupt as this and there is more likely to be a decline over several years. However, there will be a likely falling away around these points, so we will leave the figures as they are. The key point should be clear – these sales will generate very substantial sums for the Exchequer, particularly in the next five years.

Decline in rents paid by working tenants under this scheme

Against the many ways that these reforms will raise revenue, one way that these reforms will lose it is that government will no longer gain social rents paid by working tenants in existing social properties. Where rents are paid by Housing Benefit, this does not matter – as it is a reduction in government income *and* expenditure. But 33% of social tenants, or around 1.3 million, pay their rent. As almost all working tenants in existing tenancies move from social tenancies to ownership, this will reduce the rents government receives.

215 *Table 643; Social Housing Sales: Financial data on local authority homes sold through right to buy, by region*, DCLG, available at their website

216 Table 19 includes the effect of depreciating house prices.

The average rent of housing associations and councils summed and divided is £67.50 a week, or £3,510 a year. Astonishingly, the Hills report found that by 2005-6 supervision, maintenance and regular and major repairs were costing £45 a week per local authority dwelling,[217] and only fractionally less for housing associations. The DCLG found that in 2008/9 annual gross service costs were £2,232.[218] These high figures are likely to be predominantly down to poor cost management and an ageing stock.

If we subtract the figures for maintenance from rent paid, the *net* rent after maintenance costs was therefore around £1,250 per dwelling in the last year. The loss of just under 1.3 million working households would therefore cost around £1.6 billion a year in terms of lost rent once all working tenants exit the sector. This sum would build gradually as existing working tenants moved out of the sector. This loss is not a huge sum when compared to the savings the reforms outlined in these pages will create.

Potentially grouping existing housing stock sales

An option for government is that instead of selling off each and every social property individually, government could decide to group together some sales, selling off housing (and flats) in blocks to developers. Developers would then gain each property as tenants left or died, while government would continue to look after tenants who remained.

While there would have to be legal safeguards against allowing unscrupulous developers to bully tenants out who don't want to leave, developers could be free to offer incentives to tenants to move voluntarily. This would be of particular use for some of the larger estates where developers could then redevelop entire estates, knowing that they would gain from any subsequent rise in property values on these estates as they owned most of the properties. The government would gain because developers would improve these estates at no cost to them. Tenants living in redeveloped estates who didn't want to move would gain from a better estate and so better quality of life.

In London and other urban areas, this could be done in co-operation with the Mayor's office and other locally elected council leaders. This would allow for large scale planned redevelopment across urban parts of the UK. However, this is excluded from the calculations of savings later on as it is an option that may not be pursued. It would have to be popular among tenants and agreed to politically in each area. In any case, this option would not impact on the total savings from these reforms, though it would impact on when they were realised.

Will many new owners default?

As discussed earlier in the section on providing greater support for low income households there is no reason why those using new Right to Buy and Right to Move and Buy will see higher rates of repossession than the existing average for low income households. In addition, these Right to Buy households would be helped by the introduction of greater support for low income households that lose work as set out in Part 2 (3).

Additionally, new tenants under the Path to Ownership model would still be renting from the government, meaning that these tenants would not be at risk of

217 *The Hills Report into Social Housing*, ibid

218 *Evaluation of management and maintenance costs in local authority housing*, DCLG, 2009

defaulting on their mortgage as this is not how their borrowing operates. Indeed, because the Path to Ownership model provides a new and stable route into home-ownership for low income families, then the impact of reform may even be to lower default rates amongst low income households.

Paying to demolish the very worst estates with some of the funds from reform

On a small number of very bad (usually high rise concrete) estates very few individuals will want to buy their home. Developers are unlikely to want to help redevelop these estates as they stand, since they face almost intractable problems of crime and deprivation. These estates need to be demolished. The process of identifying these estates should be widely consulted on, but the key point is to find a way of ensuring that it is local residents who push for demolition, while making certain that this policy is focused on the very worst estates in terms of the deprivation and social problems that tenants face, as measured by government indices.

Where there is general support for demolition, tenants in these estates should be offered local council properties and/or the maximum discount for their area to purchase another property. £1 billion a year should be set aside for discounts for working tenants within these estates who want to use the Right to Move and Buy. Another annually topped up fund for compensating those who have bought property in these estates would also exist, with funding running at £1 billion a year. This would put the annual cost of these measures at £2 billion a year. Those who do not want to buy should be able to move into the Path to Ownership model in another social property. The aim should be that this £2 billion a year, or £20 billion over ten years, should help the 5-10% of tenants living in the most run-down and desperate estates move out to better properties, and that these estates should be demolished.

The land that these estates sit on should be auctioned to developers with these funds returning to government. The Valuation Office Agency states the average hectare of land with residential planning permission is worth £1.87 million in the UK. Even in deprived urban areas land values for large scale residential development are likely to be close to this. Because of the terrible deprivation on these estates, the value of the homes on these estates is very low – such that the properties within the estate would probably be worth no more than the land itself with planning rights to redevelop the site. Therefore no change in asset sales receipts is projected from this.

The Right to Move (and Buy) will reshape Inner London while the reformed Right to Buy will reshape other urban areas

The reforms set out in this paper will dramatically reshape the UK's urban landscapes. While existing tenants would be free to stay in their homes there will no longer be expensive new social tenancies in Inner London or elsewhere. While it is true that these changes will reshape Inner London over time, the goal should be to end, not export poverty. As was demonstrated earlier, social housing in Inner London is making deprivation and problems of low employment worse, not better. Poverty is not a zero sum factor that needs to be 'shared' geographically, but is due to economic factors that current social housing policies are exacerbating rather than reducing.

Other urban areas would also be reshaped through these changes, in particular by the revamped Right to Buy which should help millions move into home-ownership. In less affluent urban areas in the North and Midlands where social tenants would find purchasing their homes cheapest and easiest, the introduction of the revitalised Right to Buy will help to spread wealth, reduce dependency, and create real housing incentives for social tenants. Working social tenants should, just as others are, be able to purchase a home for themselves and their families. These measures will help allow the millions of low income households that want to move into home-ownership to do so. In the long run, greater owner-occupation in these urban areas will reduce housing costs and spread wealth. These reforms offer a boost for parts of the UK that have been too long reliant on state support that does not promote private wealth – a situation that cannot, in the long run, be tenable.

Reform will generate long-term savings from not paying retired social tenants' rents

These proposals will also reduce the long-term liabilities of government as social tenants who become home-owners will not need to rely on Housing Benefit to pay their housing costs when retired. The cost of paying Housing Benefit for retired social tenants was earlier estimated at roughly £3 billion a year, and so if perhaps two-thirds of tenants own in the long run, this will save £2 billion compared with what all retired social housing tenants would otherwise cost. However, these long run savings are largely excluded from our calculations of costs and benefits, except for the last five years of the second decade after reform, when they would contribute £100 million in the first year, rising to £500 million in the final year.

5
Broad Effect of These Reforms on Other Areas

These three-fold strands of reform – more homes, better support for (low income) home-owners, and helping social tenants into ownership – add up to a transformation of housing policy. Such a radical shake up would also have some broad positive impacts on other areas of policy. This paper will not attempt to go into the detail of every knock-on effect, but it is worth highlighting some of the particularly notable improvements that would be achieved outside of areas over and above housing itself and the direct benefits to the Exchequer.

Reduction in poverty by reducing social tenants' dependency

Between 1996-7 and 2007-8, poverty fell by just 500,000 from 14 to 13.5 million, within which child poverty fell from 4.3 to 4 million – despite huge sums being spent on it.[219] Now poverty (measured as 60% of median income) will have be reduced or at least kept steady whilst cutting a huge government deficit – a tall order. Approaches that involve heavy focuses on tax credits and similar measures often show the cost of substantially reducing poverty to run into tens of billions of pounds.[220]

But in one way, reducing poverty can go hand in hand with generating savings. Increasing the rates of employment for social households will help reduce poverty figures. This is particularly true for child poverty. 79% of children in workless single parent households and 88% of children in workless couple households live in poverty. Social housing with its low employment rates exacerbates these problems. 58% of children in social housing are living in poverty, while the Inner London boroughs contain both the largest concentrations of social housing in the UK and the largest proportion of "children on benefits" families in the UK.

While accepting that these are a crude calculation, if the reforms set out achieve the 20% increase in employment rates for social housing households discussed earlier, and just half of this is in households with children that move out of poverty due to employment (over time), this would be around 270,000 social households. If we assume slightly more than one child per household, these reforms would lift more children out of poverty than was managed in the entire 1996-7 to 2007-8 period – while bringing in huge amounts of revenue.

Further reductions in poverty would come from the fact that social housing households would often be better off over time if they bought under the

219 Brewer et al, *Poverty and Inequality in the UK,* Institute for Fiscal Studies, 2009

220 *Micro-stimulating child poverty in 2010 and 2020,* Institute for Fiscal Studies, 2009

reforms in Part 2 (4). Housing costs for those buying in many parts of the country would fall over time when compared to if they continued to socially rent – improving the income of these households once housing costs were accounted for.

Increase in home-ownership following reform

The total number of existing social tenants that would move into home-ownership in the long run is estimated in this paper at around 1.75 million households out of a total of roughly 22 million households – around 8% of all households. Around 1.45 million social households are estimated to move into home-ownership in the first ten years or so.

Meanwhile, as housing affordability grows due to changes around planning, more first time buyers should be able to get onto the housing ladder. As we saw earlier, there are 2.9 million private renters in the UK. If we assume that over ten years, holding nominal prices roughly stable would take the numbers renting back to where it was in the late 1990s, this gives around 2 million households renting.[221] This would represent a net transfer of 900,000 or so households into home-ownership. It might further be expected that more (let us estimate at least 100,000), or so of those currently living with their family move out to own over the next decade.

> “While the government should avoid setting an arbitrary target, increasing home-ownership rates so substantially within a decade would provide a marked contrast with recent declining home-ownership rates”

Taken together, this could mean that home-ownership might rise by some 2.4 million, an increase of around 11.5%, in the next ten years. This would give a home-ownership rate of close to 80% by 2020. On top of this, most social tenants would own at least part of their home under the Path to Ownership model. While the government should avoid setting an arbitrary target, increasing home-ownership rates so substantially within a decade would provide a marked contrast with recent declining home-ownership rates. This would also help show that the government is serious above giving everyone a real stake in society. By the middle of the next decade, the government should be close to a situation where all who want to own can do so, fulfilling the aspirations of the vast majority of the population.

Reduction in wealth inequality

The increase in home-ownership envisaged in this paper has a further strength in terms of reducing the sharp levels of wealth inequality within the UK (especially between social tenants and home-owners). Social tenants have less than 5% of the wealth of those who own their home outright, and around 15% of the wealth of those with mortgages. Continually rising house prices and a failure to help social tenants into ownership will lead to this inequality growing, as those whose families own find it much easier to get onto the property ladder than those whose families do not. By contrast, reform will help many into home-ownership over time.

221 *Table 801; household characteristics, tenure trend from 1918*, ibid

If a social tenant bought a home worth just two thirds of the average value of a UK property, then by the time they completed paying for it they would own an asset worth £100,000. This could be passed on to their children, ensuring that lower income families accumulate wealth over time, just as more affluent ones do. Helping social tenants into a £100,000 social property increases their eventual wealth five-fold from the current average of just £20,000 we saw in Part 1. It would also reduce the wealth gap between those who currently own their property outright and these new owners from the existing factor of twenty to one to a factor of just four to one.

Reduced transport demand and congestion in and around London

Another major effect of the proposed reforms would be to help ease the burden on transport in and around London and the South East. This may seem like a side issue but in fact it will be crucial given the tight financial constraints the government is facing in the next few years.

The South East and London's commuting belt will feel the brunt of cuts in the transport budget. London and the South East accounted for around two-thirds of all rail passenger journeys in recent years,[222] and between 2002-3 and 2007-8 the number of rail passenger journeys in London and the South East rose sharply by around 20% from 679 to 833 million.[223] Between 2000-1 and 2007-8 annual passenger kilometres rose from 4.7 million to 7.7 million on the London bus network and from 7.3 million to 8.5 million on the Tube/DLR network.[224] TfL alone received around "£4 billion this year from the most recent government funding settlement."[225] All in all, demand for transport in and around London is a large share of the UK's transport budget, and investment is barely keeping up with demand. The recent London Assembly *Big Squeeze* report set out the problem of rail services within London, including the fact that two thirds of London commuters are dissatisfied with crowding on peak rail services.[226]

While a breathing space has been bought by the recession, this has been small and temporary. Passenger journeys in London fell 0.3% in 2009 (although the tube saw a larger fall).[227] As the economy begins to recover, demand will again begin to rise. Business leaders are already pointing out the folly of cutting back on transport due to a temporary lull in demand when the UK needs to be upgrading its ageing infrastructure. The problem is that the money to pay for the necessary improvements to transport infrastructure will be very hard to find in the current financial climate. Transport faces unprecedented cuts of around 25% in the next few years. There has already been a review announced on the previous government's expansion of rolling stock, and a question mark hangs over tube upgrades.

However, a solution comes if we reduce the medium-term demand for transport, particularly in London and the South East. The changes set out in this paper do just that. While no existing tenants will be required to move, as households in Inner London exercise the Right to Buy and Move and Right to Move, and other expensive stock is sold off as existing tenants die, these Inner London homes being vacated by their current occupants are likely to be bought by young, working households or those who rent to such households. This will

222 *Public Expenditure, Statistical Analyses,* HMT, 2009

223 *National Rail Trends 2008-2009 quarter one,* Office of Rail Regulation, 2008

224 *Travel in London, Key trends and developments, Report number 1,* TfL, 2009

225 Transport for London Business Plan 2009/10 to 2017/8, TfL, 2009

226 *The Big Squeeze; Rail over-crowding in London*, GLA publication, 2009

227 *London's Economy Today, Issue 88, December 2009*, GLA publications, 2010

move younger working households closer to their work. The areas of Islington, Tower Hamlets, Camden, Hackney, Southwark and Lambeth will all undergo substantial demographic change. Cycling, walking and shorter bus journeys will become more viable for those who work in Central London and move into these areas.

The changes will lead to those who work in Inner London living closer to it, while largely economically inactive households are no longer located centrally. This means that transport spending can be focused on improving transport within Inner London. Rather than having one train making a one hour journey into London and then returning out to come back in again, the same train could do two half hour trips in and out of London – potentially moving twice as many people in the same time. The same applies with bus routes.

In addition, as currently deprived areas regenerate and undergo demographic changes this will spread demand in rush hour across new areas. (For example, the northern end of the Piccadilly line, which runs through many deprived areas, is far emptier in rush hour than the Northern line, which goes through more affluent areas. Should more people use the northern part of the Piccadilly line this eases overall congestion at practically no cost.) This in turn will help transport systems cope with increasing passenger numbers by easing existing bottlenecks. The alternative is that as demand climbs whilst funding is slashed in the next few years then transport systems in London and the South East will simply be unable to cope and will grind to a halt.

Reform will help maintain growth, rebalance the UK economy and raise living standards

The final strength of the changes above are that they will help rebalance and strengthen the UK economy. Firstly, by adopting these proposals the government will generate over £100 billion for the Exchequer over the next five years. This will reduce the need for cuts elsewhere – cuts which are to be done within a timeframe and scale unprecedented in UK peacetime. These savings would also mitigate any impact on growth that very sharp cuts in the next couple of years or so might have. The changes to planning outlined should act as a stimulus in the short-term by expanding the numbers of new homes being built, without costing anything to the government. Again this should have particularly useful effects over the next couple of years.

An increase in the size of the construction industry would create new job opportunities within it, albeit over some years. The UK's construction sector is large in terms of its value but low in employment share compared with other EU nations (what you would expect given the high house prices and low levels of building in the UK).[228] An expansion of the construction industry would help provide jobs as part of a much needed rebalancing of the UK economy and would help provide a new batch of skilled jobs (e.g. plasterers, decorators). Reforms would help move the UK away from the risk of another boom and bust in the housing market and hold down the UK's real estate sector, which stands at a substantial 16.2% according to the Financial Times, nearly double the size of the (supposedly too large) financial sector.[229] Property speculation is churning wealth rather than creating it – as shown by our small and often unattractive homes and

228 *Statistics in focus, 7/2010; Industry, Trade and Services,* Eurostat, 2009

229 *Manufacturing fades under Labour,* Financial Times, 2nd December 2009.

falling home-ownership rate. The economy will soon have to try to absorb those coming off benefits into the workforce – who will be competing against experienced public sector workers. The jobs that building new homes create, from builders to plasterers to interior designers will all help create some of the millions of private sector jobs that the country needs over the next few years.

Finally, changes to increase the supply of new homes will make the nation as a whole better off. Bigger, more attractive homes for ourselves and those around us are a positive, not a negative. Rents rising more slowly will deliver higher living standards for many in the coming decade – at a time when households are likely to feel squeezed. Those who want to own will be able to, while 'trading up' will become easier for households beginning a family or just wanting a nicer place to live. These reforms make sense both in terms of helping grow and rebalance the UK economy whilst simultaneously improving the quality of life for citizens.

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