propertymark

HOUSING 2025

DECEMBER 2015

Disclaimer

Authorship and acknowledgements

This report has been produced by Cebr, an independent economics and business research consultancy established in 1992. Cebr delivers economic analysis and forecasts to a wide array of retained private and public sector clients, and provides bespoke economic impact analysis of different policies and regulations at whole economy, sector and individual company levels.

The report was authored by Nina Skero, Cebr Economist; Associate Director, Scott Corfe; and Senior Economist,Colm Sheehy. The views expressed herein are those of the authors only and are based upon independent research by them.

London, December 2015

CONTENTS

It's not a house, it's a home.

It is that **word** - the one not used in housing policy discussions - that haunts the debate.

The hardest political problems to discuss are the most personal ones. Take health and education. We are the experts in our own bodies and we all went to school - so we have strong views about how things should be. Strong and valid views. But there is an element of detachment - most adults, most of the time, aren't fully engaged with health or education as services. So, while the personal is always a strong strand in views and responses, facts matter too. Housing, however, is something that all adults are intimately involved with all their lives. Buying or renting, decorating or renovating, extending or downsizing - different things in different phases of our lives, but housing is always present.

And housing is freighted with meaning. Somewhere we are born, grow up, bring up children, settle down and hope to end our days in. Something we shape to the size of our households and our personal tastes. Something we invest in and which rises in value and which we hope to pass on as an inheritance. A haven from the world and an expression of our identity to the world. The multiplicity of meanings are crystallised by the phrase we use about where we live - it's not a house, it's a home. It is that word - the one not used in housing policy discussions - that haunts the debate.

There are powerful forces at play in the UK housing market. Some macro-economic - the purchase of high-end London properties as a safe place to hold global funds. Some micro-economic - the rise of buy-to-let as an income or a supplement to a pension. Some demographic - increased household formation. Some deeply personal - a need for space or independence.

This is not an exhaustive list, nor should it be seen as a litany of constraints on either debate or decent policy. It is simply that the interplay of these complex and at times contradictory forces shapes discussions and needs to be fully unpacked in order to achieve a sustainable settlement.

It is in this context that the conclusions of this report should be considered, and debate shaped.

To summarise these conclusions briskly, they are:

- Tackling skill shortages in the house-building industry;
- Providing long term certainty and stability through an independent Housing Policy Committee, modelled on the Monetary Policy Committee of the Bank of England;
- Providing private landlords with quality certificates through a certification board
- Offering incentives for downsizing for older households;
- Relaxing the Green Belt; and
- Expanding the Private Rented Sector by underpinning large-scale institutional investment with government guarantee

As the detail in the report shows, these are all sensible and evidence-based reforms. What is interesting is to consider the obstacles of bringing these ideas to fruition.

MARKET BASED REFORMS

Firstly, there are the market based reforms. Quality certification is probably pushing on an open door given the number of local authorities who, in some form or another, are moving in this direction. It benefits both tenants, landlords and lettings agents. The question will be one of cost and how burdensome administration would be. Cost is the issue, too, with the proposal to underpin expansion of institutional investment. With government on a medium term trajectory of reducing both debt and deficit it is reluctant to take on additional 'on the books' investment. These, though, can be profitably explored.

SKILLS SHORTAGES IN HOUSE-BUILDING

The second group of issues is more difficult because it is just more difficult – what the civil service term a 'wicked' issue, one that does not give easily to a government or industry solution. Skills shortages in house-building are not a new problem and they have proved difficult to sort – even with access to the wider European Union workforce opened up by EU expansion. Policy instruments such as allowing skilled non-EU migrants in to work in the UK will always be part of this. As will adjusting Further Education (FE) and skills funding – which will gain a new and important

focus with devolution of powers to city regions. But perhaps more significant is the human factor – there are probably enough former building workers in Britain to fill the vacancies in the workforce. Exploring why people leave the industry and what could motivate them to return would be a productive piece of work.

HOW DO WE INFLUENCE HUMAN BEHAVIOUR

This leads to the third and most difficult question – how do we influence, and in the end, alter human behaviour. The figures on under-occupation and over-crowding are stunning – 1.1 million households in England and Wales (4.5% of the total) are overcrowded, while 16.1 million households (69.0% of the total) are under-occupied. It is probably right that some households, particularly older people, may want to access the capital locked in their homes and to move to smaller, more tailored accommodation that is easier to maintain – and it may well be that a small change in occupation patterns could make a big difference. But the scale of 'under-occupation' is so great that it may be that we are using the wrong terms. Private households have spent a large amount of money over the last few decades on modernising and upgrading their homes – in fact, in some areas private sector investment by individual households in their own homes probably dwarfs public sector regeneration funds, while complementing them. Additional rooms reflect new needs – for home-working, for 'boomerang' children, for en-suite bathrooms. These are deeply personal and deeply human – and thus hard, if not impossible, to shift.

LONG-TERM SOLUTIONS

The fourth point is that the true long-term solutions may be the hardest to achieve, but will be the most lasting – if we can brigade the various factors and provide a human face and motivation. The desire to have and shape a home is, at base, a desire for place-making. That is also the motivation for relaxing the Green Belt – it is far from 'green' in some places at the moment, in fact it can look like a poorly maintained 'Brown Belt'. Accessible green space, more parkland, better remediation, Green Wedges – all are ways to balance the apparently competing needs for homes and the Green Belt. The point is that relaxing the Green Belt is the end point of a conversation – not the starting point. The proof point is the delivery of the improvements, so they must come first and the new-build second.

The same applies to the very sensible notion of a Housing Policy Committee which puts long-term policy decisions that affect housing outside of day-to-day politics. That too is the end of a debate not its starting point. There are many things we need to agree first. Price stability has to be balanced with home-owners' desire for visible capital growth in their property. Affordable rents with return on investment for investors large and small. Provision of social homes with the need for labour mobility.

There are a range of competing policy objectives which can be reconciled if they can be balanced. That balance and consensus can be achieved, but it must be earned by an open and honest debate. That starts with the facts – and this report makes a substantial contribution to establishing those.

John McTernan
Policy and housing specialist,
and former adviser to three Prime Ministers

EXECUTIVE SUMMARY

The past decade has been turbulent for UK house prices.

Prices fell sharply in 2009 in the face of the financial crisis, only to rise again in recent years. In 2014,the average UK home was valued at just under £250,000. We expect this to increase to £385,000 by 2025.

Many of the UK regions that have higher house price levels also witness higher average rents.

This is because high property prices prevent many prospective buyers from getting on the property ladder, which creates demand for rental properties. In London, the country's least affordable region, average weekly rent is currently £227. By 2025 we expect this to stand at £285.

Over the past decade and a half it has become more difficult and less common for Britons to own a home.

Both transaction numbers and mortgage approvals are well below pre-financial crisis peaks and the average first time buyer is getting older. Rising prices, higher deposit requirements, and tougher mortgage eligibility criteria are among the reasons behind this. The current homeownership rate in the UK (63.6% in 2013) is the lowest it has been in a generation and has fallen substantially below the EU average of 70% in 2013.

Singapore, Germany, and Sweden provide useful case studies for the pros and cons of greater state intervention in the housing market.

Although it is unlikely that the UK would introduce measures as drastic as these countries, if the affordability crisis continues some additional forms of intervention may become necessary.

Failure to adequately address planning constraints in order to correct the under-supply of homes in many areas (including rental properties), will see continued upward pressure on both rents and house prices.

With housing costs expected to account for an ever-increasing share of household spending, this could squeeze disposable incomes to the extent that it weighs on consumption growth.

In order to prevent continued supply shortages and make house prices and rents more affordable for the UK's expanding population, a drastic and immediate policy overhaul is necessary. A specific set of policies that would begin to address these issues includes:

Skill shortages are one of the factors contributing to an unsustainably low level of housebuilding. Hence, **the government should incentivise firms in the construction sector to offer more apprenticeships and training programmes.**

As training a new labour force will not address skill shortages in the short term, it is also necessary for the Home Office to **add construction sector occupations, e.g. brick layers, to its shortage occupations list, thereby making it simpler for employers to hire non-EU nationals.**

The Government should extend the London Rental Standard scheme, making it mandatory across the UK. The scheme offers accreditation for letting agents and private landlords, and would create a way of distinguishing landlords who maintain their properties to a high standard, thereby improving the condition of private rental properties coming onto the market. It would make it easier and quicker for prospective tenants to assess the condition of an advertised property and most importantly raise lettings standards across the private rented sector.

A source of numerous market failures in the housing market is the frequent and often politically motivated changes to policy. This also leads to a lack of policy certainty which discourages investment. A way to address this is by **forming an advisory body in the form of an independent housing policy committee, which is not directly elected.** The independent body would have authority over housing policy in a way similar to which the Bank of England's Monetary Policy Committee (MPC) controls monetary policy.

Analysis conducted in 2014 by the Office for National Statistics suggests that 1.1 million households in England and Wales (4.5% of the total) were overcrowded. On the other hand, 16.1 million households (69.0% of the total) were under-occupied. **Offering stamp duty exemptions to pensioners looking to downsize** would free up under-occupied properties more suitable for larger families.

Additionally, **over-65s' bonds, which offer substantially higher rates of interest than normal savings accounts, and available only for funds obtained through downsizing property,** would create an incentive to sell unnecessarily large homes.

The green belt is a policy introduced in the UK in the 1940s which designates areas of countryside in the proximity of urban regions where development is not permitted. Given the pressing need to create more homes, it is necessary to **revisit the idea of reducing the land area of the green belt and to designate a committee which would explore this possibility in detail.** Steps in this direction have already been taken with the government planning to relax regulations for certain types of development on the green belt.

Giving a wider scope of powers to the Private Rented Sector Taskforce and providing government debt guarantees would encourage large-scale institutional investment into the private rental sector – something which is necessary as it is becoming increasingly common for Britons to spend larger periods of their lives as tenants.

1. INTRODUCTION

The debate on housing has been at the forefront of public discussion in the UK for some time. From proposed changes on property taxation to calls to limit foreign ownership, hardly a day goes by without a housing related story making the headlines. This report takes a comprehensive approach and presents a succinct yet detailed explanation of the current state of the housing market with a focus on both homeownership and the rental sector. Additionally, core housing market indicators are forecast up to 2025.

After establishing the general state of the market, the report offers additional insight into specific market segments. This includes an international perspective which examines how the rental and buying markets in the UK differ from those in Germany, Sweden, Hong Kong, Australia, and Singapore. Each case is related back to the UK in terms of lessons that can be learned. Furthermore, we look at the housing mix and provide insights into various areas such as the demography of renters in the UK. We also consider whether or not the UK is building enough family homes and examine the regions in which home ownership is most prevalent.

Finally, the report outlines a set of policy recommendations that would ensure continued strength of the UK housing market, but also address the problems facing renters and prospective buyers. Specifically, we explore the achievability of current housing targets as well as other topical issues such as encouraging 'rightsizing', the green belt debate, and the extension of the Right to Buy scheme.

The structure of this report is as follows:

Section 2 discusses the current state of the UK housing market and presents 10 year forecasts for a number of market indicators.

Section 3 gives an international perspective by discussing various elements of global property markets and analysing how they might be applied in the UK.

Section 4 focuses on the UK's housing mix.

Section 5 outlines a set of policy recommendations and explains how these may impact the UK housing market between now and 2025.

Section 6 draws conclusions based on the preceding analysis.

2. THE UK HOUSING MARKET

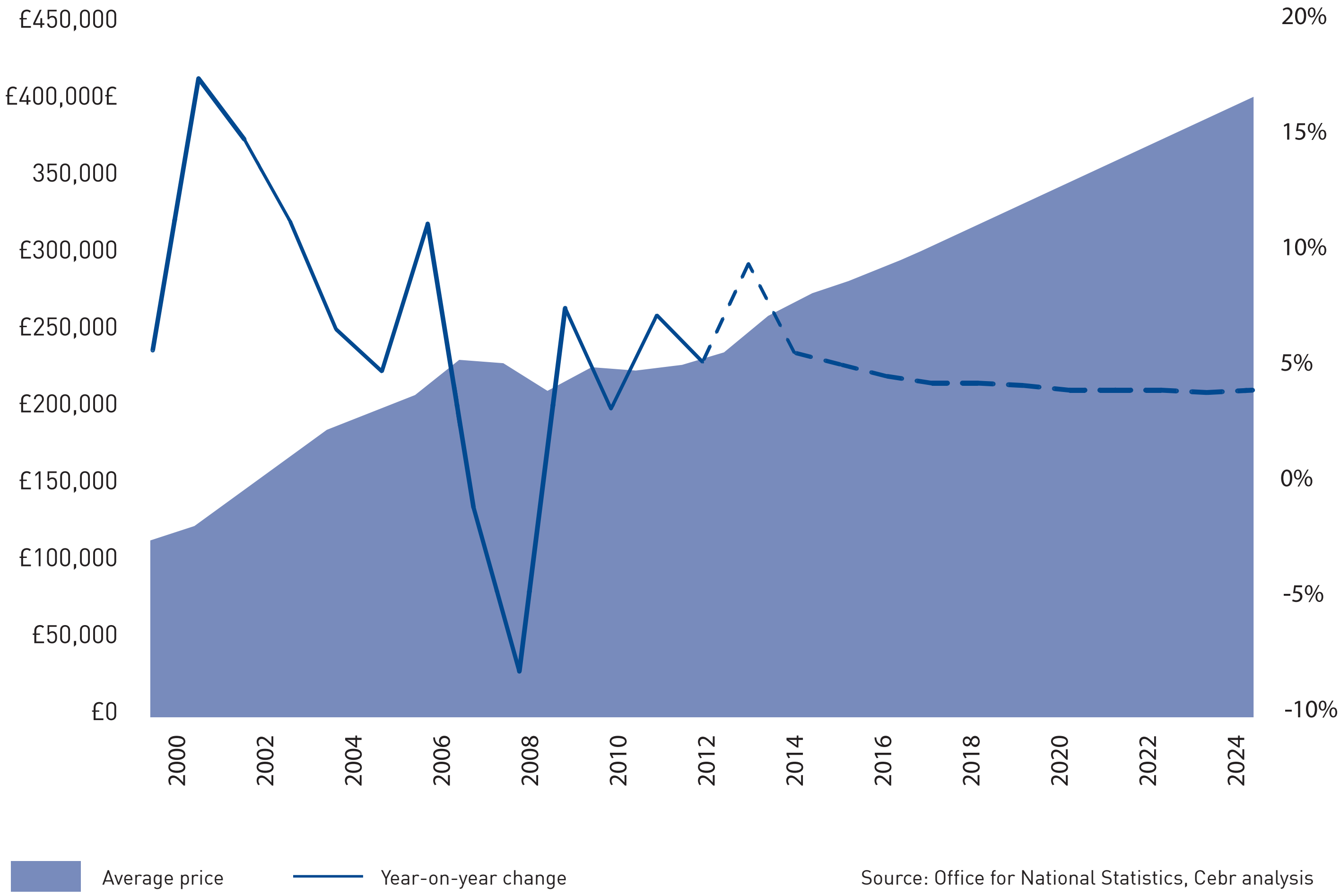
2.1 Regional house price growth and rent averages

The past decade has been turbulent for UK house prices. After years of growth, prices plummeted in 2009 in the face of the financial crisis. Very strong price inflation returned in 2014 as the UK's solid economic performance and safe haven status boosted foreign demand, specifically in London. In the medium and long term we expect annual price growth of about 4% on average.

Beyond 2020, the general state of the UK property market will be determined largely by supply-side developments, and also by growth in the number of households. A combination of rising demand and supply shortages is expected to continue pushing up prices.

Further policy measures are necessary to address the fact that many prospective first time buyers are still priced out of the housing market and that people are having to wait until later in life to own their first home. Boosting house building via measures such as encouraging public-private partnerships and easing planning constraints would address affordability concerns and help more first time buyers get on the property ladder. Section 5 of this report discusses these and other policy recommendations in more detail.

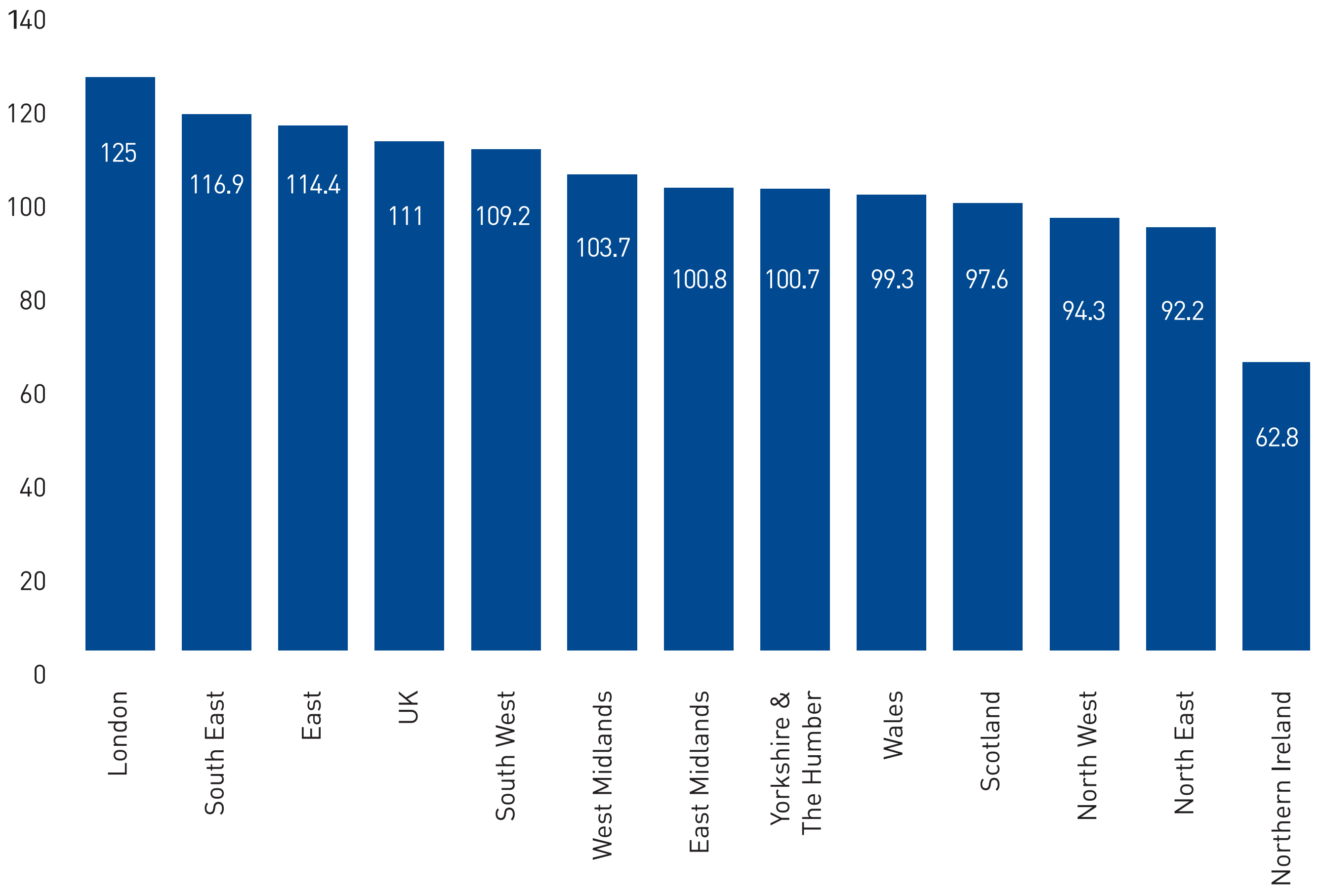
Figure 1.
Annual percentage growth in UK-wide mix-adjusted nominal house prices (RHS) and average nominal price (LHS)



Source: Office for National Statistics, Cebr analysis

From a regional perspective, since the start of 2008 house prices have increased far more rapidly in London and the South East than other regions, reflecting strong demand to live in the UK's most prosperous region, combined with a shortage of housing supply.

Figure 2.
Regional average house price, Q1 2015, indexed so that Q1 2008 =100



Source: Office for National Statistics, Cebr analysis

As is shown in Figure 2, average house prices are now comfortably above the level seen at the start of 2008, after falling during the financial crisis. However, in certain regions house prices remain below their pre-crisis peak but now appear to be catching up. Our expectations for regional house prices over the years to 2025 are shown in the following tables.

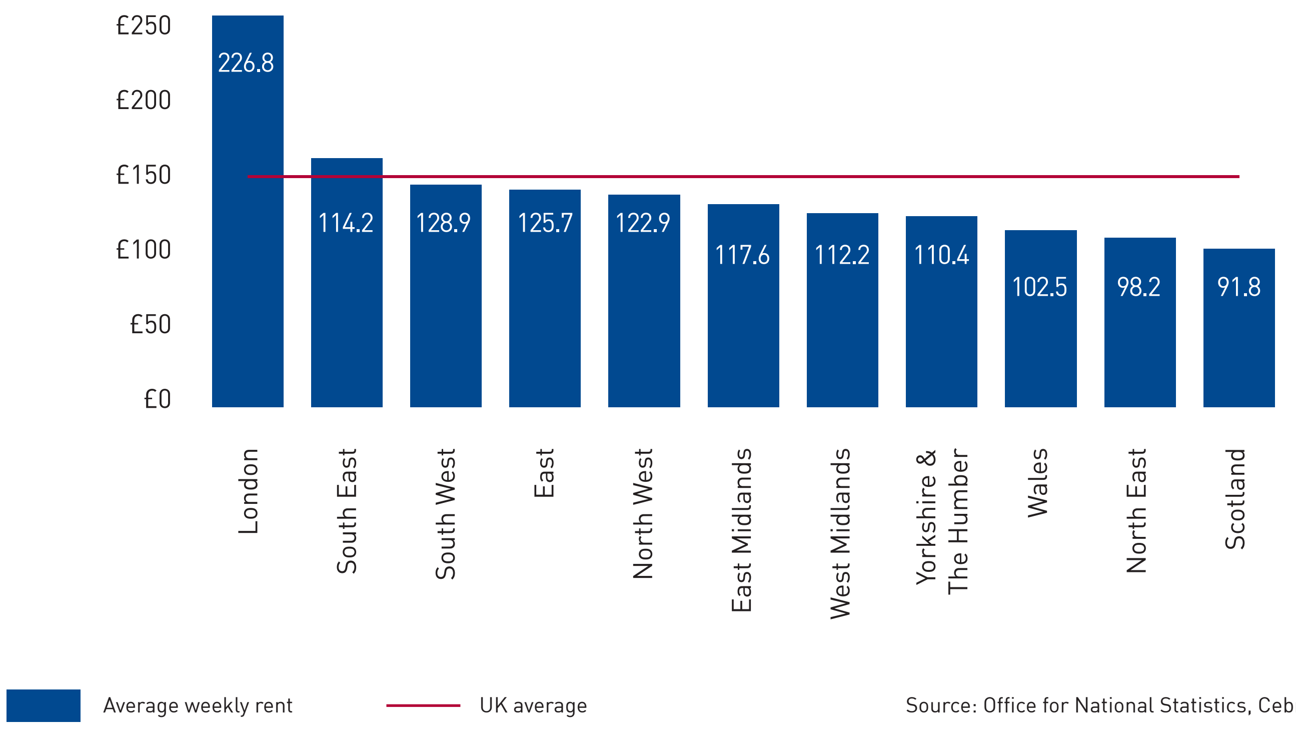
Table 1.
Annual regional mix-adjusted[1] nominal house prices, £

	South West	Yorkshire & Humber	South East	London	East of England	Scotland
2000	106,191	71,446	146,894	174,873	119,132	73,717
2001	118,674	77,745	160,150	187,767	129,186	76,646
2002	143,973	89,484	185,189	214,790	157,686	83,674
2003	170,560	107,325	213,115	236,477	181,494	92,006
2004	191,426	131,280	227,726	257,266	197,187	110,266
2005	199,231	143,281	233,070	266,328	204,215	124,390
2006	207,018	152,595	240,655	281,438	211,337	139,081
2007	224,503	163,583	266,968	329,191	231,089	159,157
2008	218,281	159,253	265,829	331,454	228,737	161,782
2009	199,978	147,815	242,303	301,025	208,168	157,586
2010	214,802	152,319	265,937	335,020	226,916	166,371
2011	215,886	153,093	272,643	352,545	235,043	171,390
2012	224,332	161,396	288,817	388,049	246,871	179,446
2013	229,089	165,703	299,551	423,920	255,306	181,386
2014	243,418	174,058	327,105	490,467	277,171	190,924
2015	256,952	181,741	350,747	515,388	300,374	196,799
2016	273,917	191,561	379,591	550,956	319,987	199,807
2017	284,542	200,641	407,428	589,853	343,935	208,907
2018	292,435	208,358	435,031	626,133	372,139	218,474
2019	300,693	217,056	460,056	659,277	401,630	226,670
2020	309,376	224,977	486,004	690,014	427,187	239,041
2021	318,967	231,726	515,650	733,436	453,246	247,168
2022	328,855	238,678	547,105	778,442	480,894	255,572
2023	339,050	245,838	580,478	826,210	510,228	264,261
2024	349,560	252,230	612,404	876,909	541,352	272,718
2025	360,396	258,788	646,086	930,719	574,374	281,445

	North East	North West	East Midlands	West Midlands	Wales	Northern Ireland
2000	65,206	74,287		91,822	72,921	78,032
2001	69,786	84,335	89,060	98,697	81,219	85,997
2002	78,309	93,190	110,043	114,442	89,624	96,067
2003	94,590	108,956	133,215	132,898	104,139	102,348
2004	121,260	133,647	151,340	154,758	130,648	109,184
2005	131,814	146,111	159,294	163,945	145,825	129,580
2006	139,481	152,606	162,543	169,854	154,628	159,637
2007	148,107	162,021	172,486	178,412	165,196	230,431
2008	144,528	157,685	166,079	172,059	160,482	211,854
2009	133,643	146,575	151,775	159,846	147,325	178,536
2010	137,356	152,398	161,003	169,457	150,816	161,775
2011	138,979	152,743	162,463	170,210	150,120	145,483
2012	143,313	159,291	169,239	177,886	156,070	131,265
2013	145,680	162,762	173,182	183,933	161,836	129,950
2014	151,270	171,309	183,788	194,536	168,986	137,577
2015	156,909	179,986	194,008	203,016	172,626	153,360
2016	162,315	188,924	201,047	208,867	176,426	158,374
2017	167,590	198,660	204,063	212,894	178,924	159,097
2018	174,780	206,046	209,613	218,218	182,162	161,232
2019	183,042	214,134	215,799	224,876	186,945	163,889
2020	191,404	222,969	223,031	232,636	192,228	167,164
2021	197,529	230,995	229,945	239,848	197,034	171,009
2022	203,849	239,311	237,074	247,283	201,959	174,942
2023	210,373	247,926	244,423	254,949	207,008	178,966
2024	217,105	256,852	252,000	262,853	212,184	183,082
2025	224,052	266,098	259,812	271,001	217,488	187,293

Source: Office for National Statistics, Cebr analysis

Figure 3.
Average weekly rent, by region, 2014, £and average nominal price (LHS)

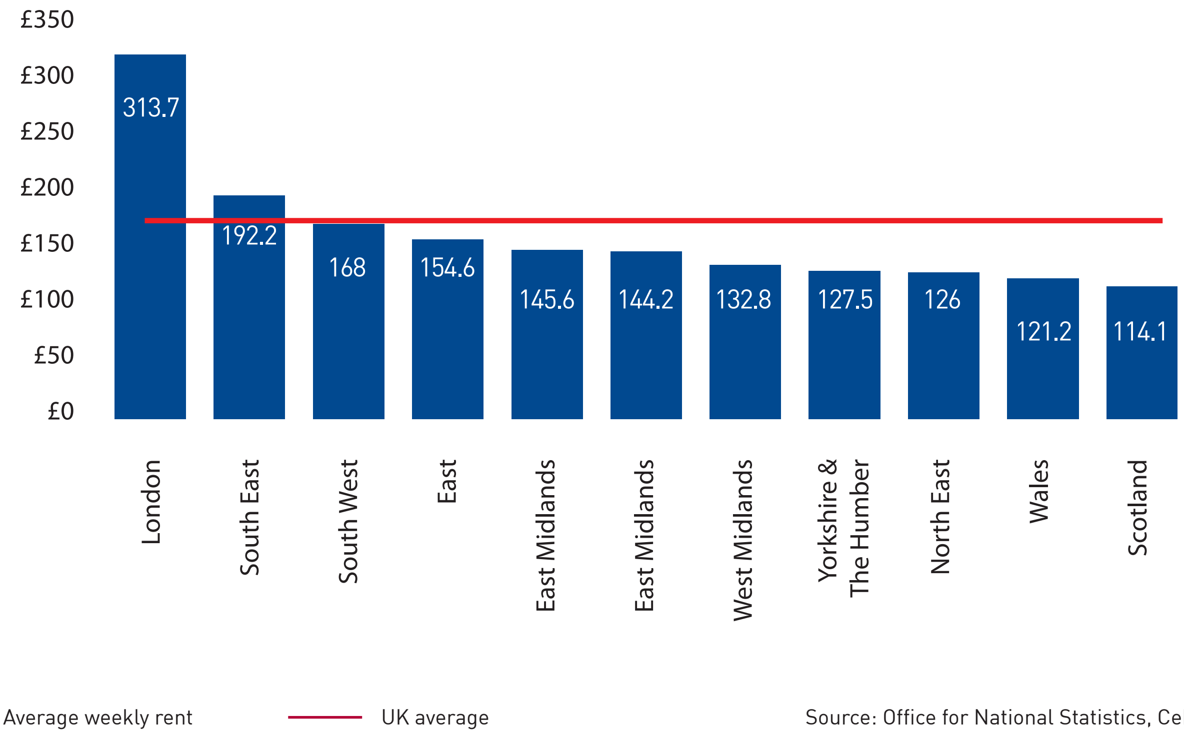


Source: Office for National Statistics, Cebr analysis

Many of the regions that have higher house price levels also witness higher average rents. This is partly because high property prices prevent many prospective buyers from getting on the property ladder, which creates demand for rental properties.

As house price affordability worsens in the medium term (affordability is discussed in more detail in section 2.3) home ownership will remain out of the reach for many. This effect will be further intensified when interest rates start rising, most likely at some point in 2016. Hence, we expect average weekly rent in the UK to increase from £134 in 2014 to £164 by 2025.

Figure 4.
Average weekly rent, by region, 2025, £



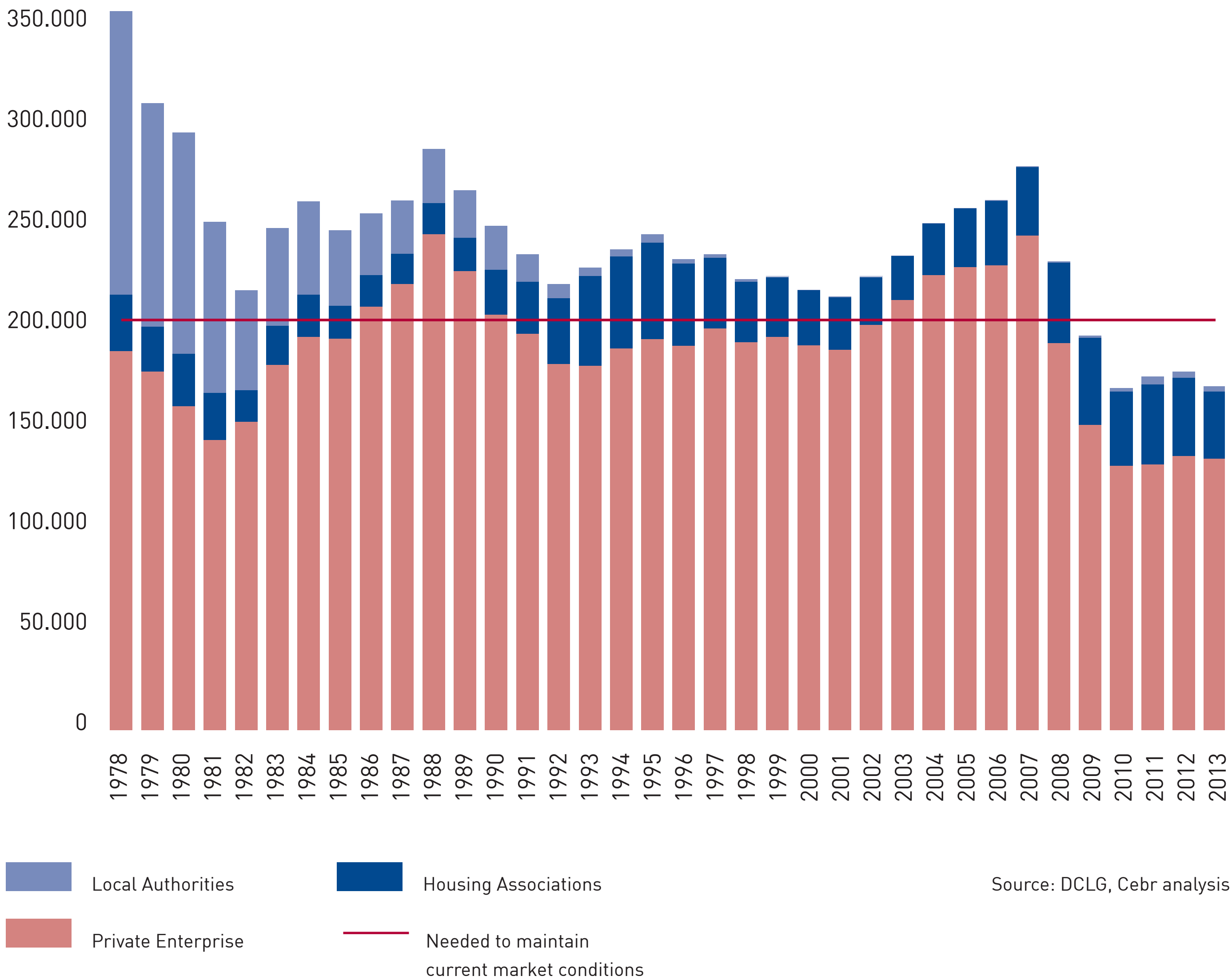
Source: Office for National Statistics, Cebr analysis

2.1 Housing starts

Based on central population projections, the UK grows by roughly 200,000 households every year. This implies that in order to keep the state of the market and affordability at current levels it is necessary to build at least as many homes annually.

In order to improve affordability, it would be necessary to build many more. Despite strong population growth, the number of annual housing starts in the UK currently stands far below the critical 200,000 value.

Figure 5.
Number of housing starts in the UK



Source: DCLG, Cebr analysis

Part of the reason for this may be that the private building sector is reluctant to build many properties given the hardship endured in the 2008 crisis. Additionally, skill and material shortages may present a greater issue now than in previous decades. Many firms in recent years have reported having to offer substantial increases in wages to attract skilled individuals who are in short supply – such as bricklayers. The free movement of labour across the European Union has provided a boost to the number of workers in the sector. If this is limited in any way going forward, skill shortages will present an even greater challenge. Additionally, the changing nature of the building sector makes it more difficult for smaller firms to acquire the necessary materials. This is due to larger construction companies forward buying the limited stock of materials.

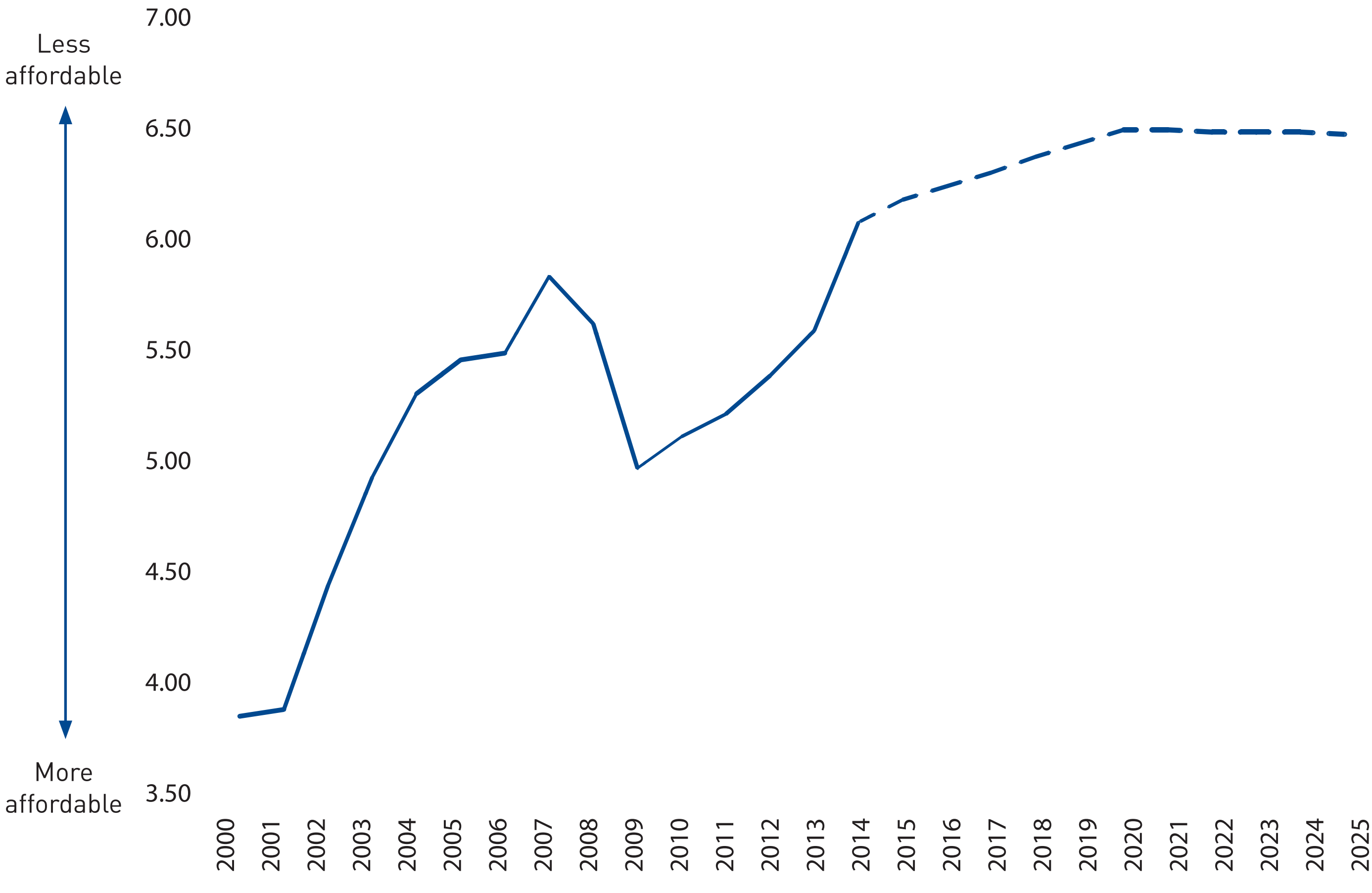
However, even if private enterprises are to boost building (which government policies can encourage them to do), they may not reach the needed level of housing completions in the short and medium-term. In the post-War period, the UK has only tended to build a substantial amount of new homes at times when there has been significant local authority involvement – suggesting that direct government intervention in housebuilding may be necessary to solve the affordability crisis.

The Conservative Government campaigned with a promise to build 200,000 reduced price starter homes by 2020 and make them available to first time buyers aged under 40. However, more permanent measures need to be undertaken in order to encourage house building. This would also entail creating more long term policy certainty and depoliticising the housing market. Ideas on how this might be done are explored in section 5.2 of this report.

2.3 House price affordability

One measure of house price affordability is the house price-to-income ratio. The ratio rose sharply in 2014 as strong growth in house prices was unmatched by growth in earnings. Although the 2014 value remains below the 2007 peak (a year in which average house prices grew more than twice as fast as disposable incomes), it is substantially above the levels seen in the early 2000s.

Figure 6.
House price affordability: ratio of house prices to average annual household disposable incomes



Source: Office for National Statistics, Cebr analysis

Another way to assess the affordability of home ownership is by considering affordability of average mortgage payments. In 2014, British mortgage holders spent an average of £152 per week on mortgage payments. On average, this represents 30.1% of weekly household disposable income. As is shown in Table 2, mortgage payment affordability varies substantially between regions.

In London, the weekly mortgage payment represents an average 31.16% of household disposable income. This is nearly 10 percentage points more than the comparable figure for East Midlands; the region with the most affordable mortgage payments.

Table 2.
Mortgage payment as share of disposable income, by region

	North East	North West	Yorks & the Humber	East Midlands	West Midlands	East	London	South East	South West	UK
2004	22.89%	24.99%	25.52%	23.87%	24.84%	28.16%	25.78%	27.06%	26.64%	25.17%
2009	24.81%	24.92%	21.83%	23.51%	26.06%	23.96%	26.13%	24.10%	22.14%	23.21%
20014	23.71%	22.13%	23.31%	21.52%	22.63%	23.88%	31.16%	26.19%	24.25%	30.09%

Source: Living Costs and Food Survey, Cebr analysis

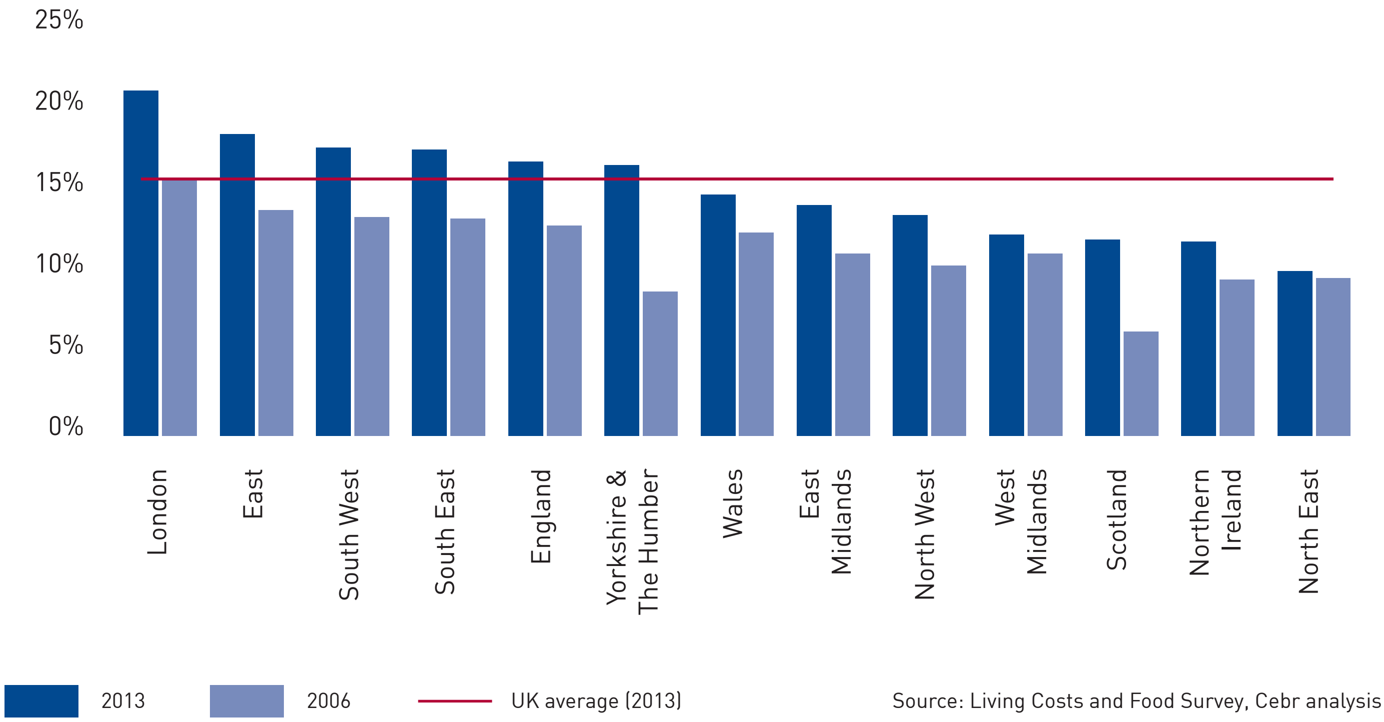
2.4 Rent affordability

Given the persistent obstacles to getting on the property ladder, and the increasing age of a typical first time buyer (the profile of the UK's renters and first time buyers will be discussed in detail in section 4.1), rent payment affordability is becoming an increasingly important indicator of the housing market.

As is shown in Figure 7, due to the high level of property values and concentration of economic activity in the capital and neighbouring regions, which pushes up demand, rent payments are least affordable in London. At the opposite end of the spectrum, average rent payments account for just 9.5% of disposable income in the North East.

In the 2006-2013 period, Yorkshire and the Humber suffered the greatest worsening of rent payment affordability. In 2006, average rent accounted for 8.3% of disposable income which more than doubled to 15.6% by 2013. However, this is only marginally above the 15.4% UK average for 2013. In the same time period, rent payments became less affordable across all regions. This is largely a result of rising house prices and stagnating wages, which have led to an increase in demand for rented accommodation.

Figure 7.
Net rent as a share of disposable income, by region, 2013[2]

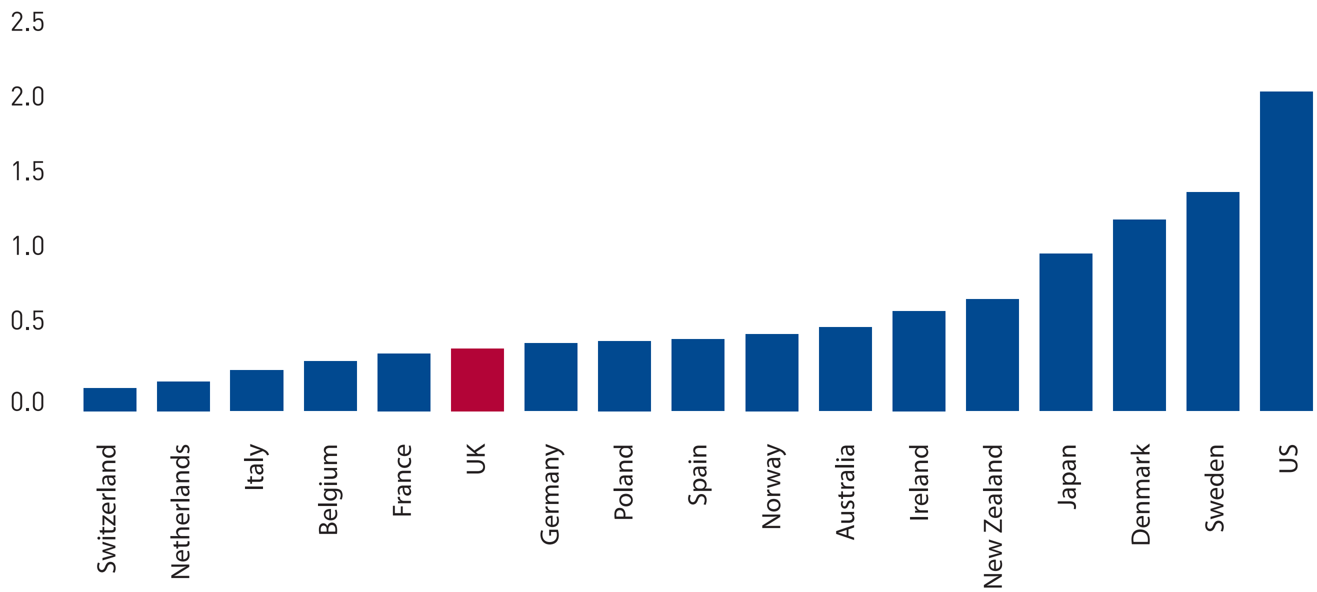


Source: Living Costs and Food Survey, Cebr analysis

2.5 Elasticity of supply

The UK's population growth is problematic when we consider the price elasticity of housing supply. Elasticity of supply measures the change in the quantity of housing supplied following a change in price. A less elastic housing supply is one in which, following a demand surge, prices adjust relatively more than supply. That is, prices rise with little increase in house building activity.

Figure 8.
Price elasticity of housing supply



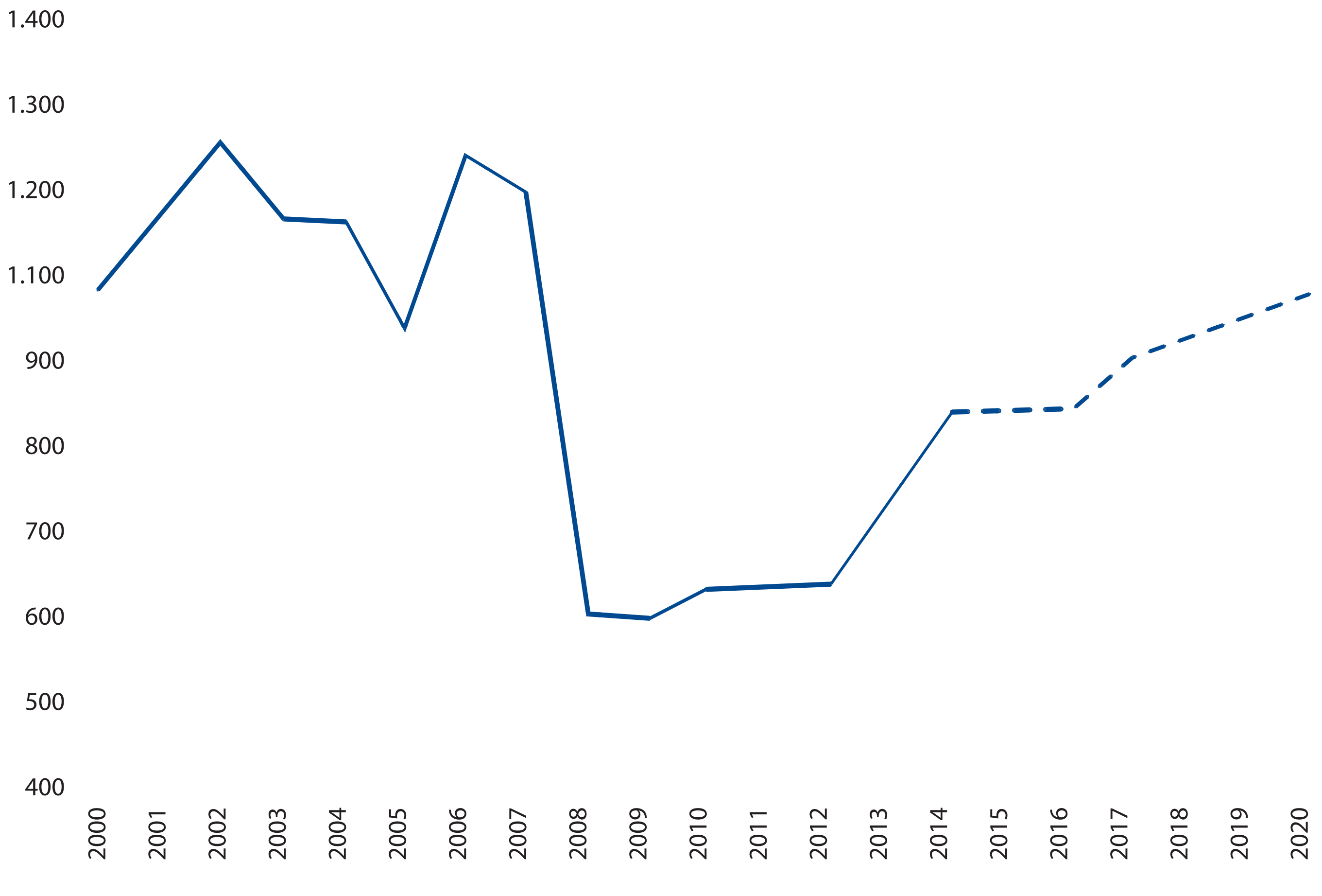
Source: OECD

The UK has one of the least responsive housing supplies in the developed world. This means that when demand goes up, the market responds by increasing prices more than supply. Given the country's strong population growth projections and current affordability crisis, it is especially crucial to understand why housing supply is so inelastic. Empirical evidence suggests that supply responsiveness is lower in countries where it takes longer to get building permits and where procedural obstacles to building are greater. This would suggest that policy reforms have the capacity to encourage supply side adjustments in the face of growing demand.

2.6 Mortgage approvals

In 2014, total mortgage approvals for house purchases reached 773,400. While the number of approvals has somewhat recovered recently, it remains well below pre financial-crisis levels. This is due to a number of reasons. Firstly, the number of housing transactions drastically decreased after 2007. This is shown in Figure 9.

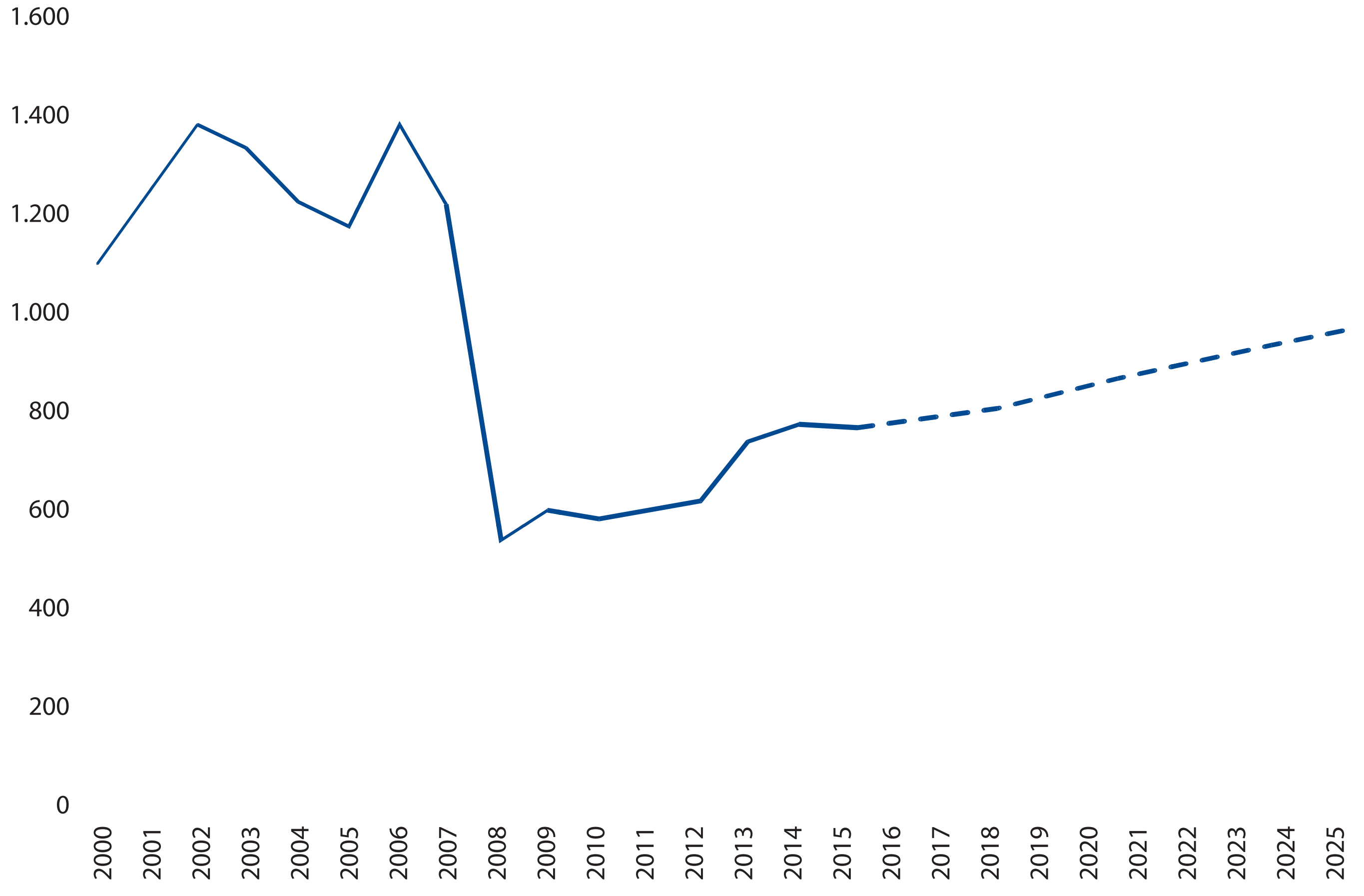
Figure 9.
Annual number of housing transactions, 000s, England and Wales



Source: Land Registry, Cebr analysis

Additionally, the impact of the crisis on banks and other lending institutions meant that many were reluctant to extend mortgages to higher risk applicants. This became even more of a constraining factor when the Mortgage Market Review (MMR) guidance was introduced in April 2014. The review recognized that the regulatory framework in place earlier allowed for particularly risky lending and borrowing practices and aimed to boost accountability in the mortgage granting process. However, it also reduced the number of prospective mortgage holders that meet the new, stricter, mortgage eligibility requirements. This, along with high deposit requirements, will continue to weigh on the number of mortgage approvals in the medium term.

Figure 10.
Total approvals for house purchase to individuals, 000s, seasonally adjusted



Source: Bank of England, Office for National Statistics, Cebr analysis

Since the start of 2015, a number of realtors and other industry professionals have reported the lack of housing being put up for sale as a market constraint. Given the shortage of properties coming onto the market, the level of mortgage approvals is expected to remain broadly at current levels in 2015 and 2016.

In the outer forecast years, we expect mortgage approvals to grow at a slightly faster rate due to the impact of the government's pledge to build affordable housing, which should help some first time buyers get on the property ladder.

The recently announced Help to Buy: ISA may also boost mortgage approvals in the medium term. However, given that the amount of the government bonus available to savers is capped at £3,000, the extent to which this will impact the market may be relatively minor.

2.7 Obstacles to home ownership

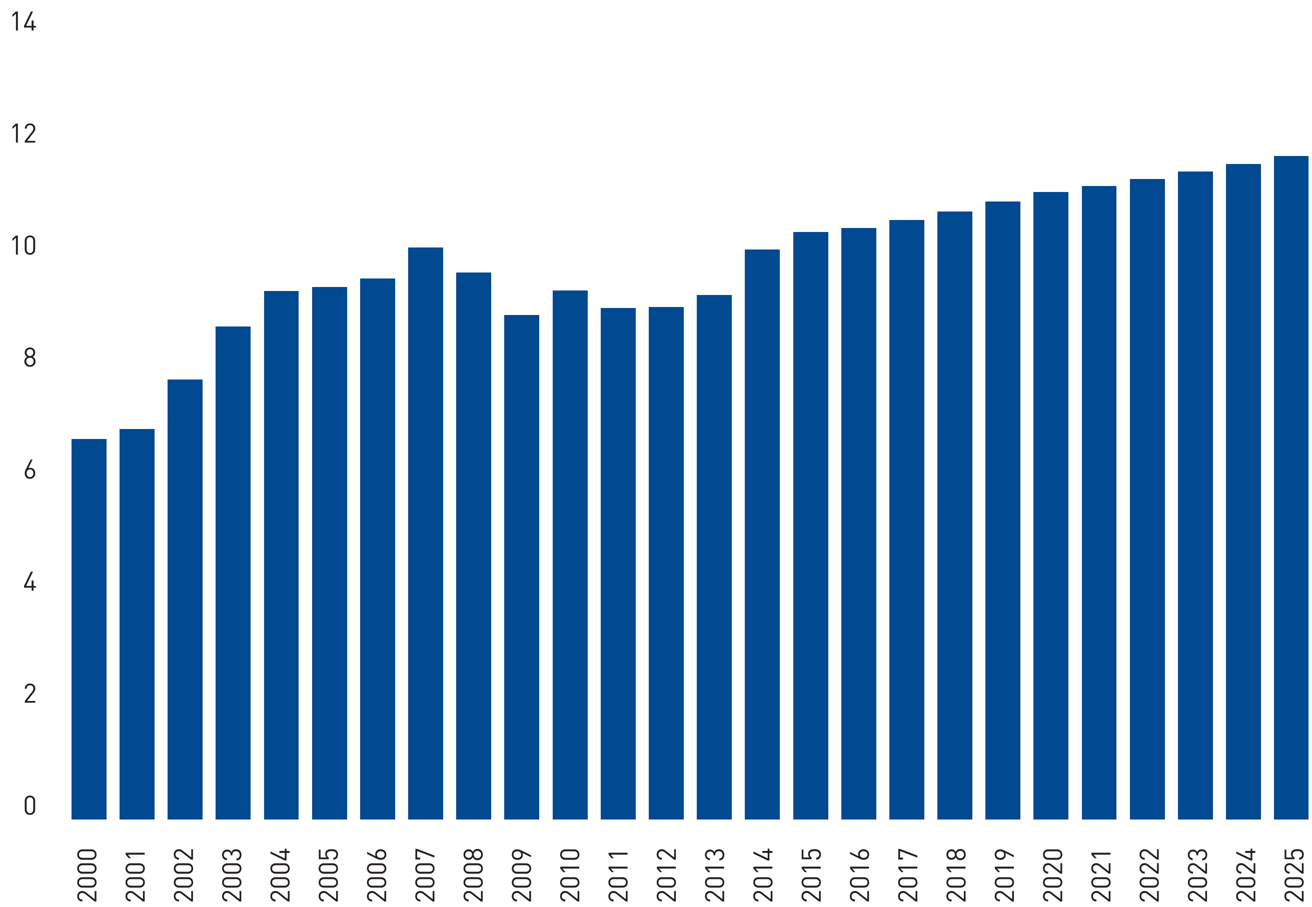
The fact that both transaction numbers and mortgage approvals are well below pre financial-crisis peaks, and that the average first time buyer is getting older (as will be discussed in section 4), suggests that it has become more difficult and less common for Britons to own a home. A number of surveys attempt to understand the causes behind this and many reach similar conclusions. Among the primary obstacles to home ownership are the high deposit requirements and other mortgage-obtaining constraints.

According to the Halifax Generation Rent 2015 report, 21% of 24-45 year olds believe it is virtually impossible to obtain a mortgage. A further 34% think it is very hard, while only 8% think of it as easy or very easy. There is however evidence to suggest that some prospective first time buyers have been impacted by the negative perception of the lending environment in the post-financial crisis period and are therefore discouraged from actually attempting to get on the property ladder. In 2015, 70% of prospective buyers reported that they are put off from applying for a mortgage by the general perception that everyone is rejected by lenders, making it pointless to apply[3]. Additionally, 27% of 20-45 year olds are not aware of the impact that the Help to Buy scheme has had on their ability to buy a home. This suggests that despite the introduction of new government programmes, not everyone has been keen to explore the options available to them. This is not to say that purchasing a home has not genuinely become more difficult for a number of prospective buyers. It is now more common than in the past to expect (and require) your parents' financial support when purchasing your first home.

2.8 How will the housing picture change up to 2025?

The house price and rent forecasts presented in the remainder of this section take into account the current state of the housing market and the future impact of confirmed housing policies. In 2014, the average UK home was valued at just under £250,000. We expect this to increase to £385,000 by 2025. In London, we expect an average home to nearly double in value from £507,000 to £997,000. This is an even faster rate of increase than the 87% increase in average price over the decade from 2005 to 2015. Most UK regions that have higher house price levels will also witness higher average rent growth. This is because high property prices prevent many prospective buyers from getting on the property ladder. A declining homeownership rate will boost demand for rental properties, thereby driving up prices. In London, the country's least affordable region, average weekly rent is currently £227. By 2025 we expect this to stand at £285 as renters become the majority in the capital's housing market.

Figure 11.
Average UK house price as a multiple of average gross earnings



Source: ONS, Cebr analysis

This vision of the housing market in 2025 is informed by past trends and, even more importantly, by an evaluation of current housing policies, which do not go far enough in terms of addressing the affordability crisis or the lack of supply.

The Housing and Planning Bill will encourage housebuilding by extending office-to-residential development rights, ensuring all councils have local building plans and implementing changes to the brownfield land planning permissions process. However, the focus of the bill is singular as the chief focus is reducing prices by boosting building. While low levels of housebuilding is one of the issues in the market, addressing other areas such as demographic shifts, a rise in the number of renters and the lack of existing properties coming onto the market are of concern as well. The alternative set of policies presented in section 5 of this report take a more complete view of the housing market and thereby present a more realistic way of making house prices and rents more affordable.

Chapter notes

[1] A mix-adjusted price attempts to overcome the fact that average prices may be influenced by changes in the composition of the properties sold in a particular period. Hence, a mix-adjusted price does not look at the average property price (which can be influenced by outliers), but instead at the price of a 'typical' house. A number of characteristics, for example size, number of bedrooms, and location, go into determining what a 'typical' house is.

[2] The figure for London may be higher in reality as the disposable income of renters is likely to be lower than the overall average.

[3] http://www.lloydsbankinggroup.com/globalassets/documents/media/press-releases/halifax/2015/150407-halifax-generation-rent-report_final.pdf

3. AN INTERNATIONAL PERSPECTIVE

3.1 Overview

Homeownership in the UK is at its lowest level in decades. If current trends continue, we are looking towards a future where more than 30% of households rent their properties from a private landlord and the average age of a first time buyer exceeds 40.

In many countries, restrictions on foreign ownership of residential property, taxes on capital gains from selling a primary residence, and rent controls have been introduced to attempt to address issues of affordability in the private rental market, to deter foreign investment in the residential property market and to correct the perceived imbalance between renters and homeowners.

Introducing these kinds of policies in other countries has in some cases produced unintended consequences that have reduced supply in the private rental market, made homeownership less affordable and removed incentives from the real estate investment market.

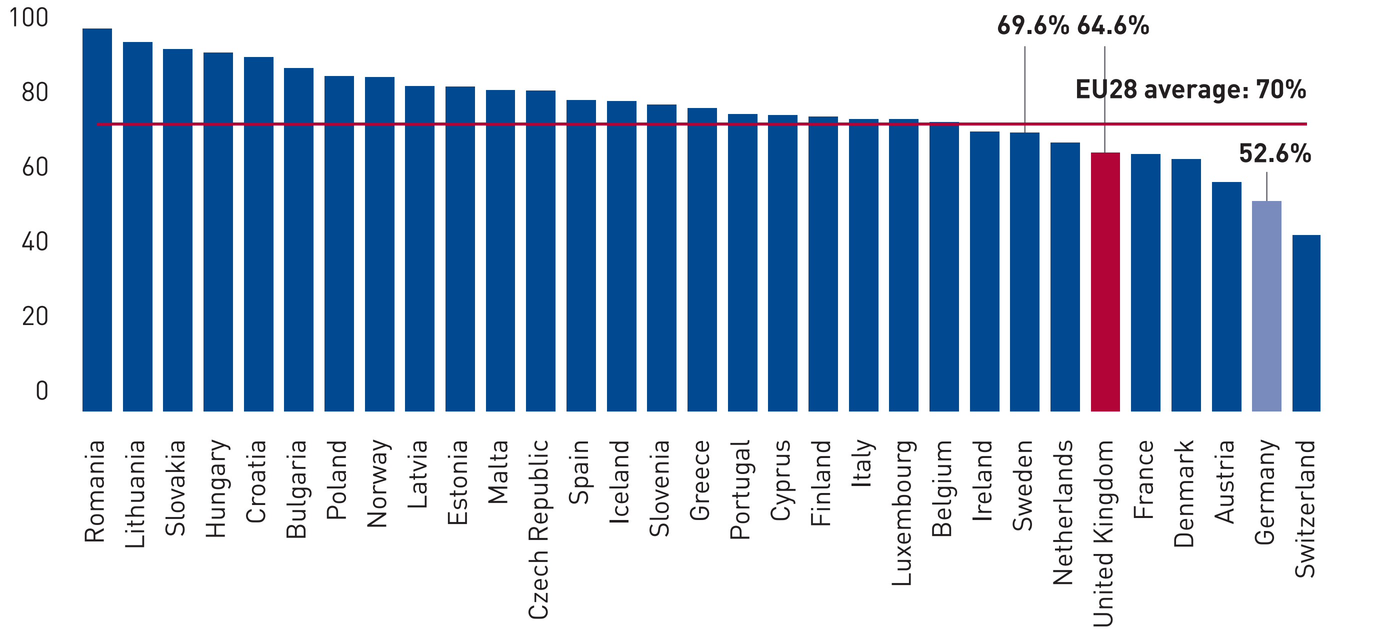
In this section, by examining the examples of the property markets of five different countries, we consider how market interventions have functioned in practice, and whether such interventions might address imbalances in the UK housing market.

3.2 How the UK housing market compares with other countries

Germany

Germany's housing market is a unique case as it is characterised by 0% real house price inflation[4] nationally since 1998 and low rates of homeownership (53%, the lowest in the European Union).

Figure 12.
Homeownership rate, 2013, EU28 countries, Switzerland and Turkey



Source: Eurostat

The absence of real house price growth means there is limited investment incentive for Germans to get onto the property ladder, and many are satisfied to continue renting properties well into their 40s. Satisfaction with housing is high in Germany with 93% of the population happy with their housing situation according to the OECD.

Despite this apparently well-balanced picture at the national level, there are localised housing pressures particularly in the major cities of Berlin and Munich, where prices have risen by 41% and 47% respectively between 2010 and 2014. A fear of an overheating rental market has led the German government to introduce rent controls in late 2015 on new leases that prevent landlords from charging rent exceeding 10% of the local average for a comparable property. Such measures are expected to constrain supply of rental properties to the market and limit appetite for investment in the real estate market.

3. AN INTERNATIONAL PERSPECTIVE

Since 2000, average rents in Germany have kept pace with house prices, in stark contrast with the UK where the value of homes has grown much faster than the income that can be achieved from renting them. In Germany, there are several important factors that have resulted in the existence of strong incentives in favour of renting:

A good supply of rentable accommodation in most cities. In Berlin, close to 90% of properties are privately rented;

Well-managed municipal authority strategies for releasing residential land to alleviate housing pressures;

Lenders tend to be more risk-averse and normally require a minimum deposit of 20% for a mortgage;

A debt-averse culture with a preference for equity and fixed income investments rather than real estate;

An annual land tax on owner-occupied homes.

The housing market interventions that Germany has implemented – while certain to have introduced distortions into the market – have had the effect of minimising the difference in financial incentives between renting and buying. As more British households rent, the German example may point the way towards the future. It is important to keep in mind cultural differences, which mean that homeownership may be more valued by Britons that Germans. It is likely that some of these policies will need to be introduced to reduce the difference in financial outcomes between those that can afford to buy their own home and those that cannot (but not rent controls, which tend to create significant negative distortions).

Sweden

Sweden has a long tradition of state intervention in the housing market. Sweden's policy of "Good Housing for All" mandated universal public housing, via tenant-owned co-operatives and municipal-owned building companies. The 1990s banking crisis led to many state-owned properties transferring to private hands.
As in the UK, low levels of new home building have led to a housing shortage which has contributed towards higher house prices. On average, twice as many homes are built per 1,000 inhabitants in Sweden's Nordic neighbours. Sweden also has the third highest construction costs in Europe[5] after Norway and Switzerland. However, unlike the UK, the Swedish housing market is highly regulated with landlords subject to rent controls.

Most apartment blocks are run as co-operatives – owners of apartments also own a share of the entire building. Renting an apartment is normally restricted to two years, after which time the owner must reclaim the property and leave it vacant for a set period. Combined with rent controls, there are limited incentives for small-scale buy-to-let investors in Sweden.

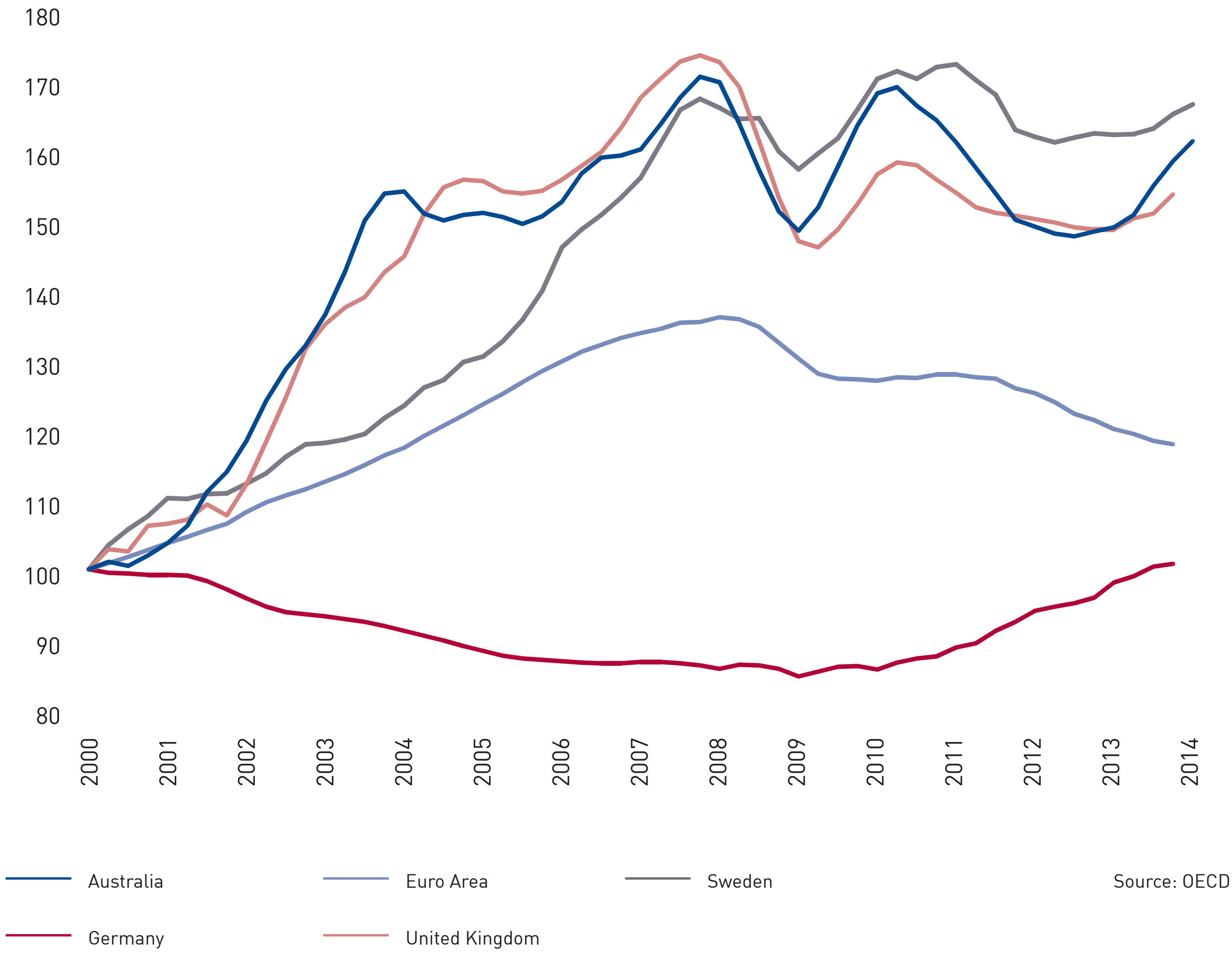
A limited supply of privately rented properties and low rents relative to buying the same property have generated strong demand and long waiting lists for municipally-owned rental housing in most of Sweden's major cities. Individuals who get a standard rental contract tend to stay put or sub-let rather than relinquish the property, because getting a new lease is difficult as the standard waiting list is eight years.

This has led to a large "grey market" for sub-let properties and strong incentives for home-ownership, leading to strong house price growth. The acute lack of housing hits young people, students and migrant workers the hardest, as they often have to remain in temporary accommodation while they wait for an apartment to become available.

Between Q1 1998 and Q4 2014, average house prices in Sweden increased 226% compared with 199% in the UK. These trends combined with rent controls have meant that house prices have far outstripped rental growth as shown in Figure 12. In 2010, the Swedish Central Bank introduced an 85% loan-to-value (LTV) limit on mortgages in order to dampen demand in the market.

The Swedish example points to lessons in terms of the perils of over-regulation of the housing market which limits the availability of rental properties and can cause house price bubbles. There have recently been calls to relax some regulations to improve the functioning of the rental market. This includes freeing up more housing by relaxing some rent controls, improving incentives to build new homes and promoting more efficient usage of existing housing. However, over the long term it is unlikely that Sweden will remove all intervention given the established political consensus aimed at minimising income inequality and promoting social solidarity.

Figure 13.
House price to rent ratio, 2000 to 2014, indexed so that 2000=100



Source: OECD

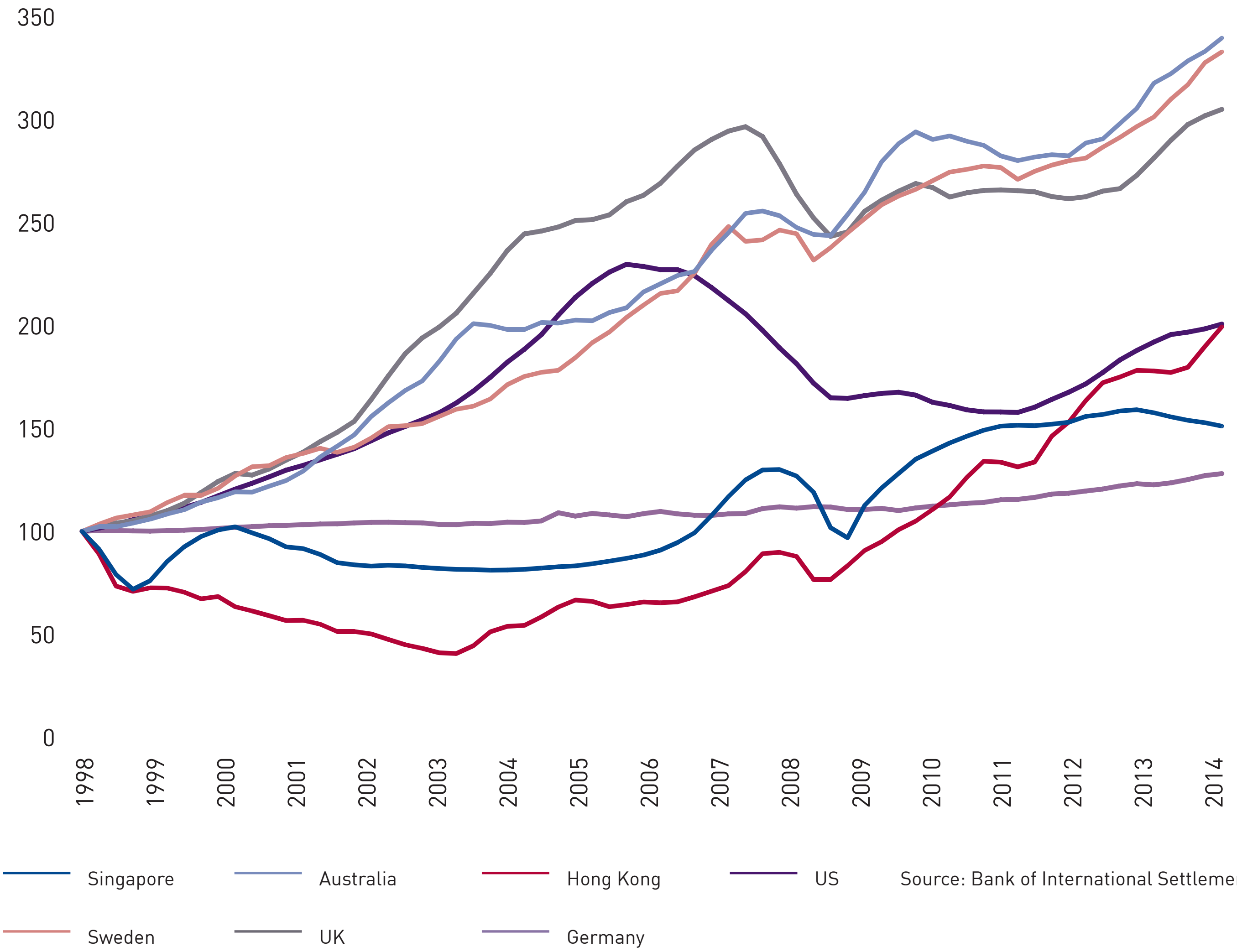
Hong Kong

Hong Kong (HK) has one of the most developed property markets in Asia. A population of 7.2 million living on land covering just 426 square miles makes Hong Kong one of the most densely populated regions in the world. Like other Asian nations but different from the UK, 45.8% of HK residents live in public housing[6].

As in the UK, housing shortages are an important political issue in Hong Kong. The average waiting time for public rental housing is currently 3.3 years. Only 33,000 new homes were built in 2013 while 248,000 applicants remained on the social housing waiting list. In some instances, this has led to social unrest.

The constrained HK property market generated one of the world's largest property bubbles - between 1995 and the peak in 1997, prices rose nearly 51%. The Asian Financial Crisis precipitated a real estate crash that led to a 65% peak to trough decline between 1997 and 2003. Large increases in demand have caused Hong Kong's house prices to more than double since 2009, after a long period of stagnation (see Figure 13). This has raised fears of a new property bubble.

Figure 14.
Quarterly house price indices (Q1 1998 = 100), selected countries and the UK, Q1 1998 – Q4 2014



Source: Bank of International Settlements

The HK Government has responded to these new demand pressures by introducing a range of measures to rein in the property market:

In October 2012, a 15% stamp duty tax was imposed on foreigners buying property, aimed at curbing speculation in an overheating market;

A transaction tax of as much as 20% on properties sold within three years of their purchase was introduced;

Boosting the amount of land available for housing development has been made a priority; and

Maximum mortgage loan to value ratios of between 50% and 60% have been introduced, depending on whether the income is derived from within or outside HK.

The resurgence of the HK real estate market has been partially driven by foreign buyers' demands, particularly from mainland China - also a factor in the London housing market. The Chinese government implemented a stimulus package amounting to USD 585 billion in November 2008 aimed at reviving the Chinese housing market, but this had the unintentional effect of generating a surge of mainland buying in Hong Kong. It is estimated that Chinese buyers have since accounted for about 37% of the total demand for newly built apartments in Hong Kong – many of which are investment properties chasing higher returns in a booming market.

In London there is also a high concentration of foreign buyers, with Savills estimating that in 2013/14 32% of all prime London residential market buyers were non-UK nationals. It is likely as interest in the HK market wanes, that some of the investment originally intended for HK could end up in other prime property markets including Singapore and London. There are concerns that if these trends in foreign investment continue, and British buyers are crowded out even more, there will be calls in the UK for even more draconian measures to reduce demand from non-national buyers, as has been done in HK.

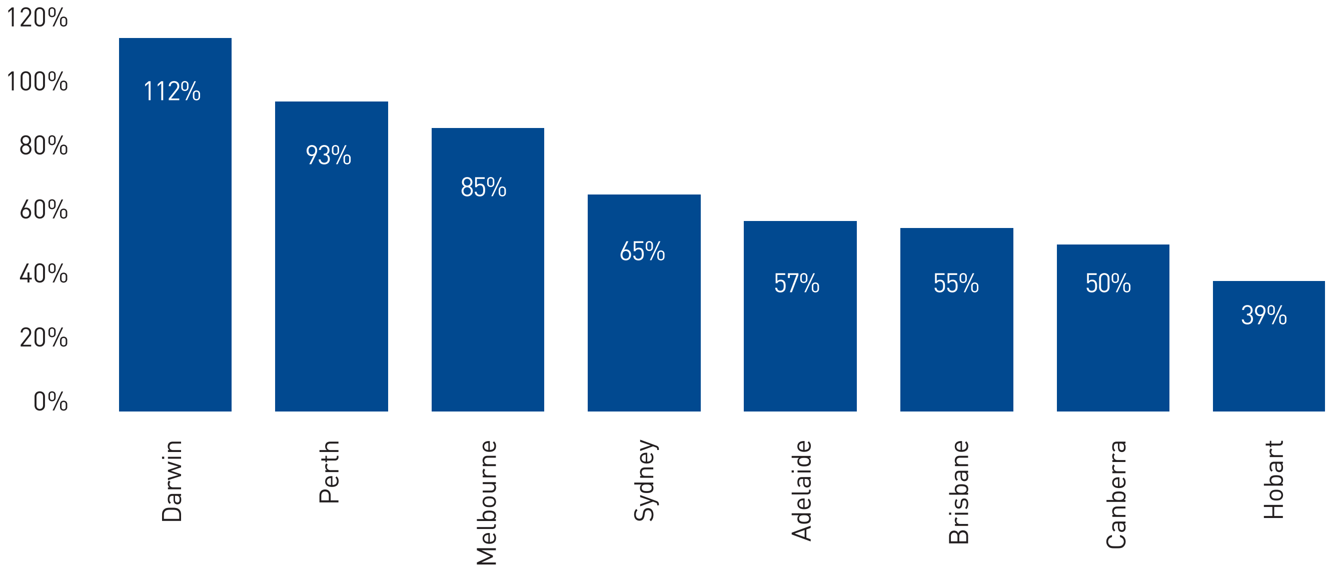
It is also important to keep in mind that although foreign investment in property does limit the supply of homes available to residents, it is not in itself something that the UK should necessarily try to discourage. Foreign property investment can lead to other types of investment inflows into the country. Maintaining London's status as a city open for global business involves avoiding placing punitive restrictions on foreign investment. Furthermore, the country needs to prepare for a rising number of renters. Often, foreign buyers who purchase investment properties around the UK put the properties on the private rental market, thereby boosting rental supply.

There is a rising concern that some buyers purchase residential properties solely as investment vehicles and leave the space unoccupied. If this happens to a great enough extent, it can decrease the appeal of an area. This phenomenon has led to parts of central London e.g. Knightsbridge and Mayfair being called 'ghost towns'. However, this is not an issue that is necessarily linked only to foreign ownership and treating it as such could discourage overseas investment in a punitive manner. Rather this is a matter that concerns all unoccupied dwellings (regardless of the owner's nationality) and that should be tackled through taxation, as described in section 5.4 of this report.

Australia

Australia's property market has seen remarkable growth since 1998 with prices increasing 238%, exceeding even the UK property market's extraordinary performance over that period. Cities influenced by the 2000s commodity boom – Darwin and Perth - saw the largest increases.

Figure 15.
House price % growth 2005 – 2015, city real estate markets



Source: Australia Bureau of Statistics

Since 2010, the property boom has been confined to Sydney, and to a lesser extent Melbourne, where prices have risen 39% and 12% respectively.

Contributing to this growth have been numerous factors which have restricted supply of new housing and incentivised investment in the property market.

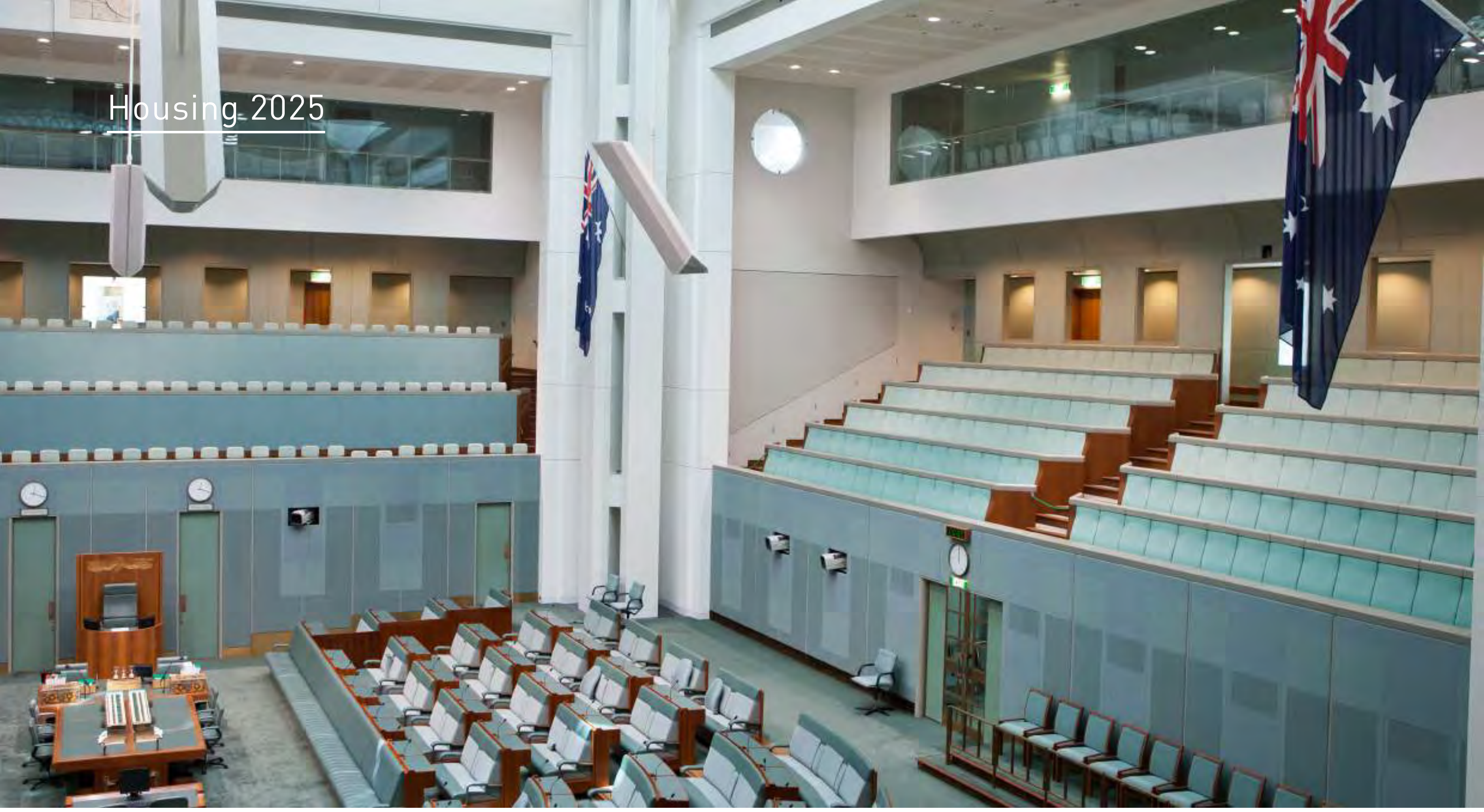
These include:

Limited release of land for new housing development

Restrictions on high density development

Favourable tax treatment for individuals who use their superannuation (a type of retirement savings account) to invest in the property market

High land price inflation



As in Hong Kong, Australia places restrictions on foreign investment in the real estate market. Foreign investors are mostly not permitted to buy existing residential real estate but, subject to approval, can buy new residential property, on the basis that this drives demand for housing. Foreign buyers of Australian residential property must pay an AUS$5,000 registration fee for properties worth less than AUS$1m, and AUS$10,000 for those worth more than AUS$1m.

In 2010, the Government introduced restrictions aimed at ensuring that foreign investors purchasing Australian property were adding to the overall housing stock and not solely benefiting from capital value growth. These restrictions include:

- Foreign buyers are screened by the Foreign Investment Review Board to determine if they will be allowed to buy a property;
- Foreign buyers are forced to sell property when they leave Australia;
- Foreign buyers are fined if they do not sell by a government-ordered sale order and any capital gain is confiscated;
- There is a requirement to build on vacant land within two years of purchase to stop “land banking”.

At present, the UK has no specific restrictions on foreign property buyers. The argument has been made that strong price growth, especially in London, is a result of foreigners taking advantage of the country’s safe haven status and using British property ‘to park their cash’. Others claim that foreign investment in UK property generates other types of spending that benefit the economy and thus should not be limited. Furthermore, the additional source of demand may encourage further housebuilding.

Singapore

Singapore has a long history of Government intervention in the housing market. The Singapore Housing and Development Board (HDB), provides public housing and support for Singapore residents to purchase a home. This has allowed the city nation to achieve one of the highest homeownership rates amongst residents in the world.

Singapore has a population of 5.5 million with a total land area of just 277 square miles – a higher population density than that of Hong Kong. Due to land constraints, housing tends to be in high-density high-rise apartment developments. Singapore is unique in terms of the high numbers of non-nationals living and working in the country. Approximately half a million are permanent resident non-nationals while 1.5 million are foreign workers.

After the housing crash in 2008-2009, house prices in Singapore recovered, and there was a continual rise in house prices along with living costs, helped by low interest rates and rising population. Prices peaked in 2013, spurred by low interest rates and demand from foreign buyers.

To dampen demand, the government introduced a range of measures which have precipitated falling rents and home prices, and rising vacancy rates:

- Borrowers' total debt repayments have been capped at 60% of their income, making it harder for Singaporeans to refinance loans;
- Additional buyer's stamp duty was increased for non-Singaporeans from 10% to 15%;
- Limits on maximum mortgage tenure to 35 years;
- A 5 to 7 percentage point rate hike in Additional Buyer's Stamp Duty (ABSD) for Singaporeans, tighter loan-to-value (LTV) limits and a 10% to 15% increase in the minimum cash down payments for potential buyers with at least one existing housing loan.

A number of these measures focus on limiting demand, which would not necessarily be as appropriate in the UK's case, where a chronic lack of supply has driven house price growth.

Chapter notes

[4] Adjusted for general consumer price inflation in those years.

[5] Eurostat, 2014, Construction Price Indices

[6] Hong Kong Housing Authority, 2015, 'Housing in Figures – 2014'.

4. THE HOUSING MIX

4.1 First time buyers

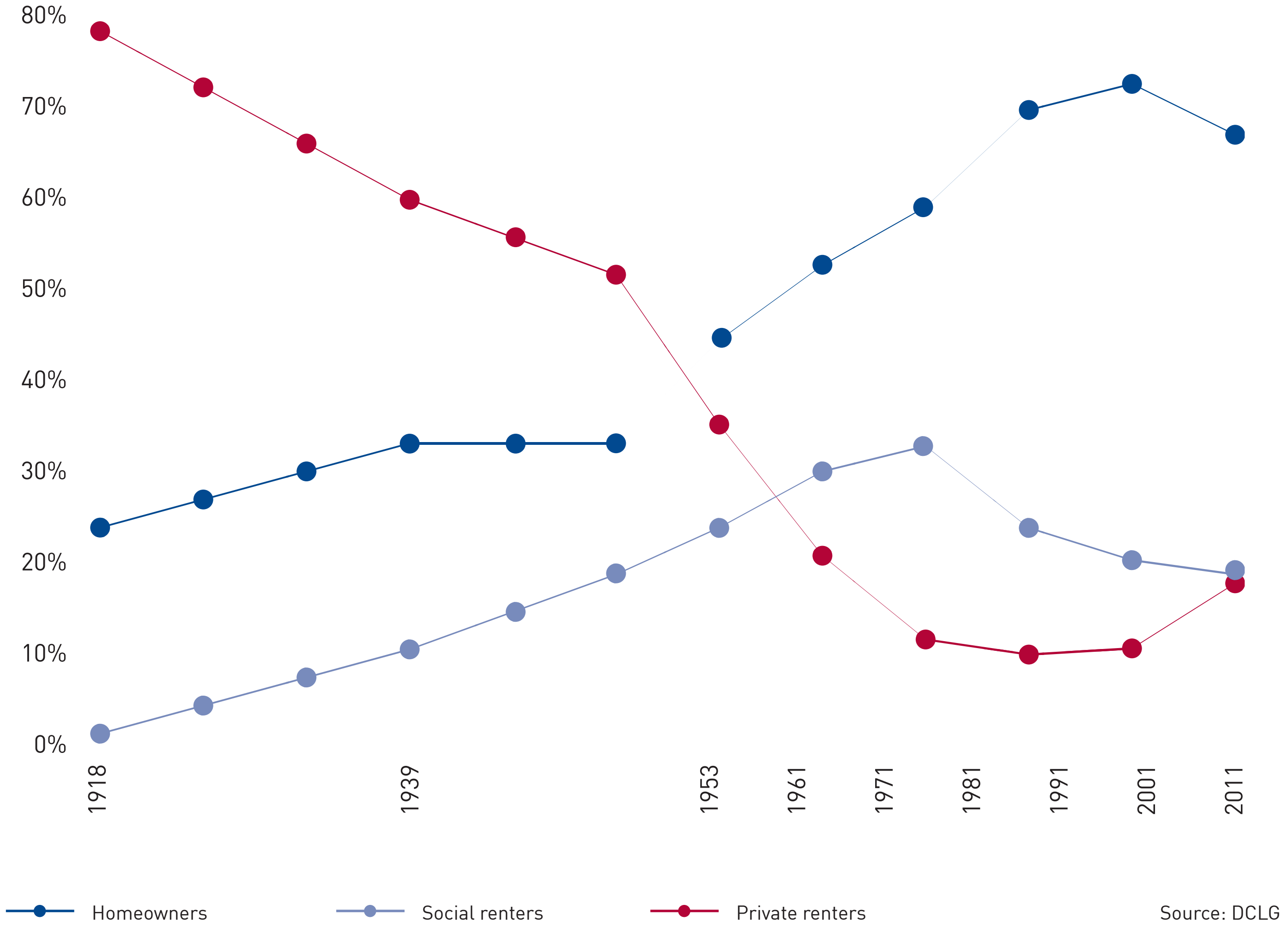
Home ownership has long been an aspiration of the British people. In the UK, the majority of households are owner-occupiers: over 60% of households live in properties which they either mortgage or own outright. However since 2001, the home ownership rate has been declining as affordability has decreased. The current homeownership rate in the UK (63.6% in 2013) is the lowest it has been in a generation and has fallen substantially below the EU average (70% in 2013).Homeownership rates are likely to fall further over the coming years.

Being able to buy one's own home has not always been so commonplace. Before World War Two, the majority of UK households rented their homes from private or social landlords – in 1939, only 32% of households owned their own home (see Figure 15).

Starting with the 1945 pledge by Clement Attlee's Labour government to rebuild Britain's war-damaged housing stock, there was an unprecedented housebuilding boom in the post-war period. At the peak of housebuilding in the single year 1972, 364,000 new homes were built. This pace of construction supported a rapid rise in homeownership – from 32% of households in 1953, to 70% in 2001.

This trend towards owner-occupation was further-encouraged by the 'Right to Buy' programme. Introduced by Margaret Thatcher's Conservative government in 1979, this ultimately led to the sale of 1.8 million council homes to private households, creating a new generation of property owners.

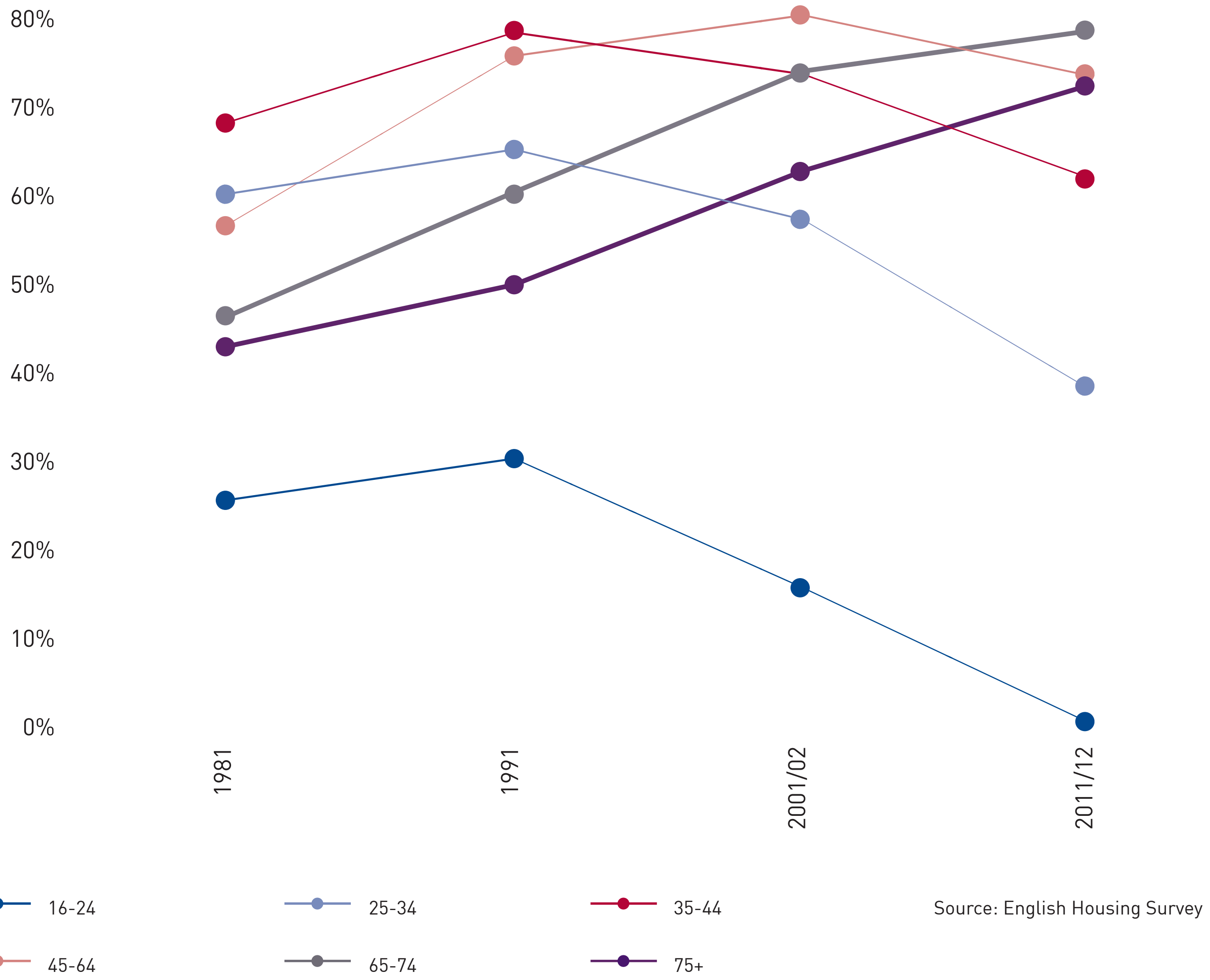
Figure 16.
Trends in housing tenure, % of households, UK, 1918 - 2011



Source: DCLG

The so-called 'baby-boomer' generation (i.e. those born 1946-1964) benefited hugely from the boom in homebuilding in the post-war period, and the relative shortage of housing supply that has followed in more recent decades. As described in Figure 16, homeownership rates among over-65s have increased consistently over the past few decades, while younger age groups are less and less likely to be homeowners. As of 2011/12, only 43% of those aged 25 to 34 owned their own home, compared to 66% in 1991.

Figure 17.
Homeownership rate by age group, England, 1981 to 2012

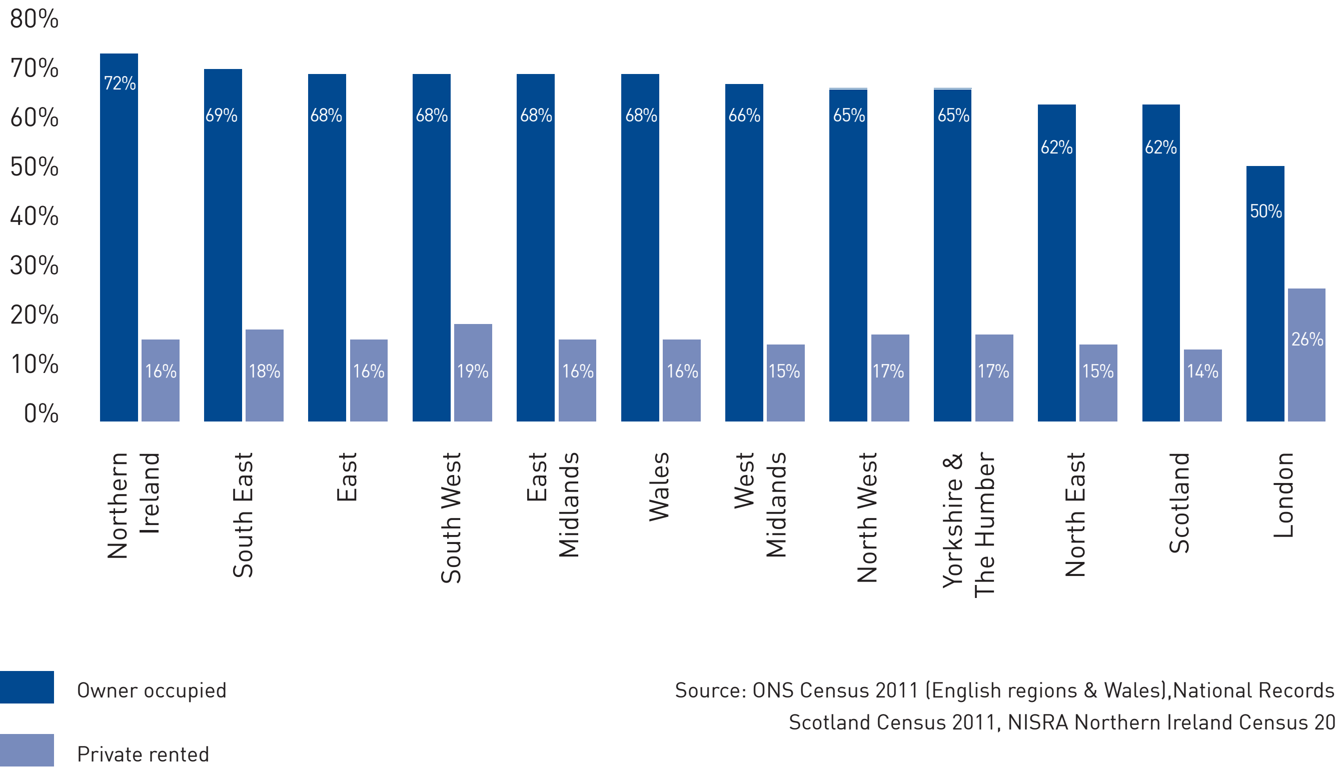


Source: English Housing Survey

4. THE HOUSING MIX

At the regional level, there is substantial variation in the proportion of households that own their home. Northern Ireland has the highest level of homeownership in the UK (71.9%) followed by the South East (68.9%). The endemic shortage of affordable homes and restrictive planning frameworks in London, coupled with its relatively young population, mean that the homeownership rate (49.5%) is the lowest in the UK, and the private rented sector is the largest.

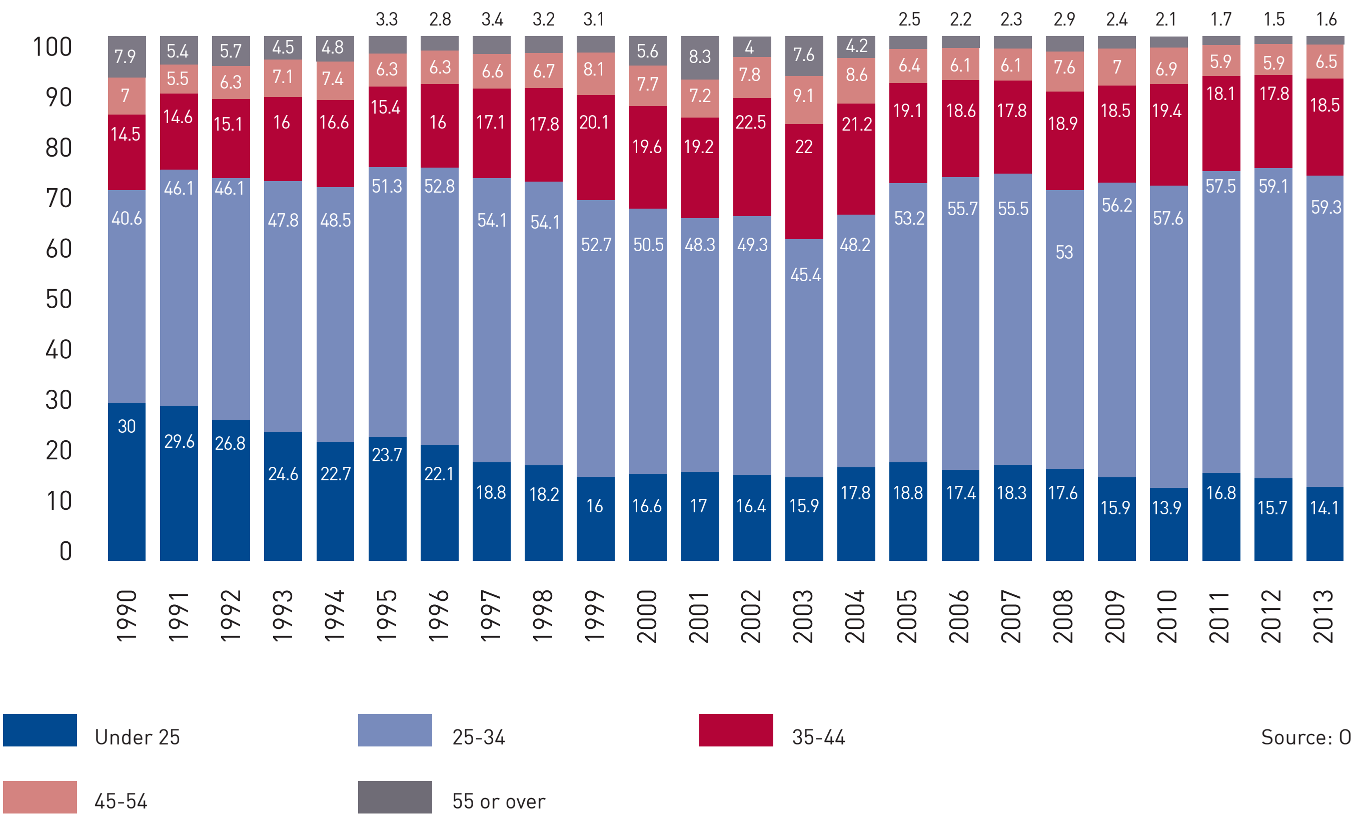
Figure 18.
Homeownership and private rental rate (%) by region, 2011



Source: ONS Census 2011 (English regions & Wales),National Records of Scotland Census 2011, NISRA Northern Ireland Census 2011

When individuals are in a position to buy their own property, they are now doing so later in life. The average age of people borrowing for first home purchase has increased from 34 in 1990 to 37 in 2013. This is a trend which is expected to continue, as homeownership slips further out of reach for more of the population.

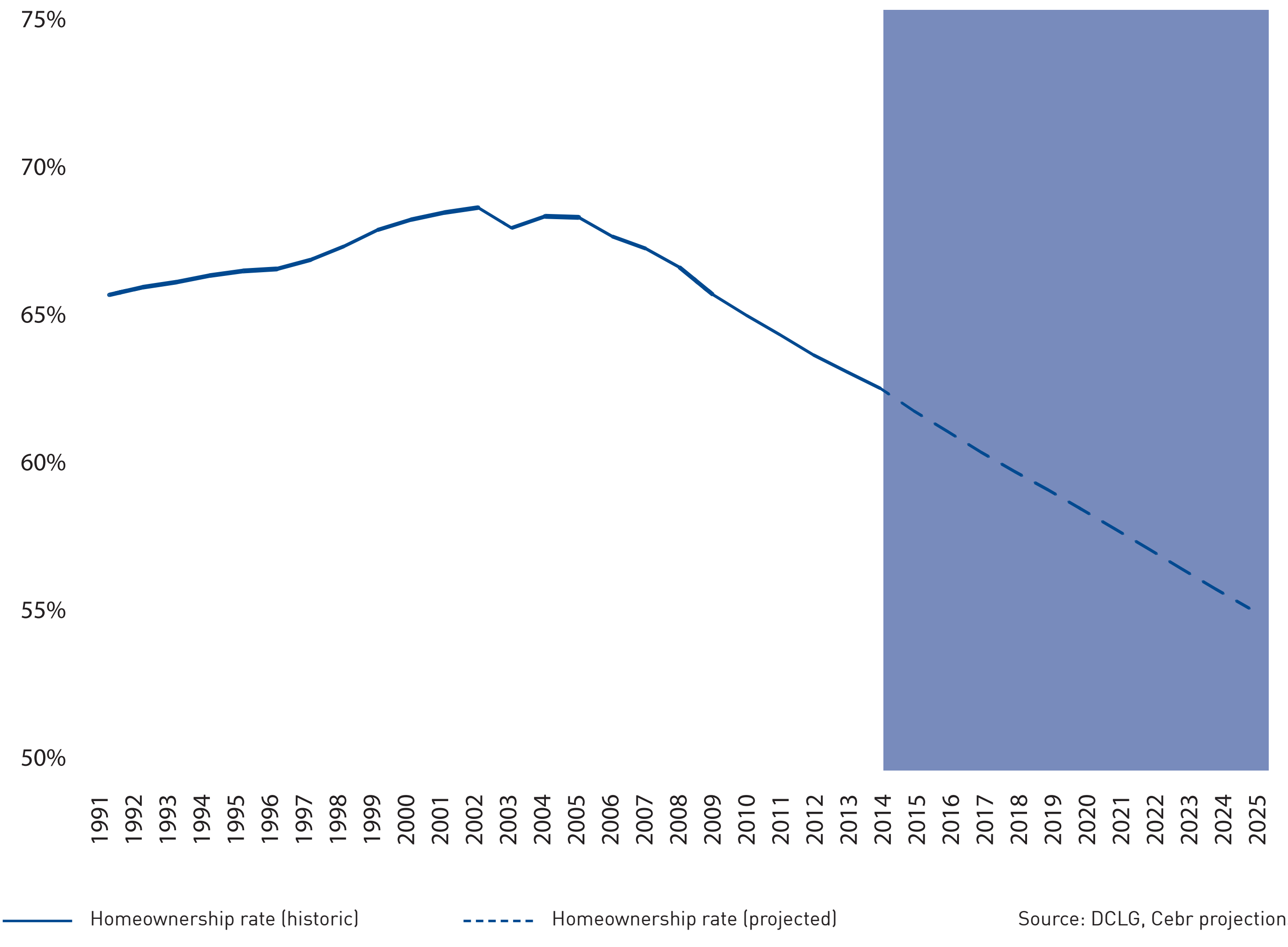
Figure 19.
Distribution of borrowers' ages, % of first time buyers, UK



Source: ONS

Lower homeownership rates amongst the working-age population (age 16 to 64) and the ageing of the baby-boomer generation, will drive a continued decline in the proportion of UK households that own their primary residence. The homeownership rate in 2015 is estimated to stand at approximately 62% of households – we forecast this proportion to fall to 55% by 2025. Over the same period, the number of households renting in the private sector is projected to grow by 46% over the next ten years – driving the proportion of private renters from 20% of households in 2015, to nearly 29% by 2025.

Figure 20.
Homeownership rate, historic and projected, UK



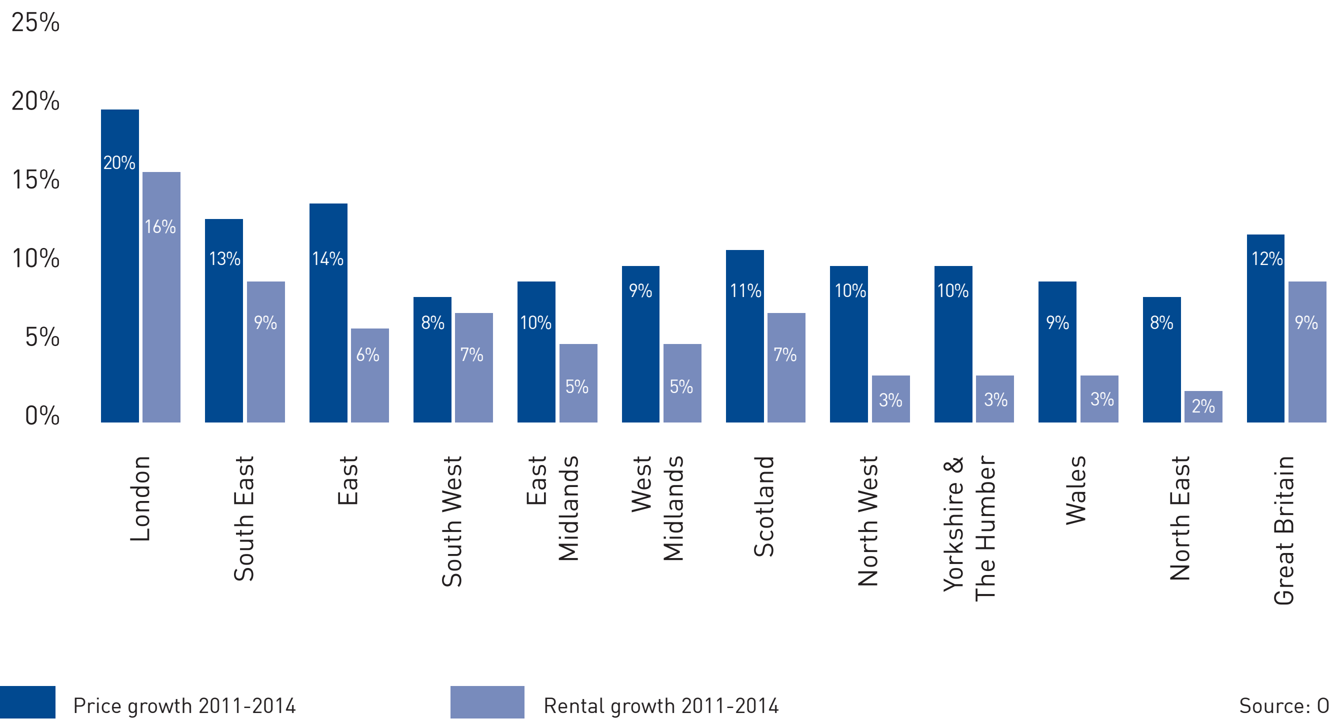
Source: DCLG, Cebr projections

This profound decline in homeownership can be expected to have substantial impacts on the UK housing market. For one, it is inevitable that greater numbers of households will remain in the private rental market for their entire lifetimes. This is likely to have the effect of narrowing the gap between growth in house prices and growth in average rents (such as has happened in London, see Figure 21) – particularly in regions which have seen the largest declines in homeownership.

In addition, strong demand for private rental properties will attract more investment into the buy-to-let (B2L) market. Rising rental values will offset some of the income loss associated with the Budget 2015 announcement to scale back tax relief for B2L landlords.

Ultimately, failure to address planning constraints in order to correct the under-supply of homes (including rental properties) in many areas, will lead to continued upward pressure on both rents and house prices.

Figure 21.
FTB price growth and average private rental growth 2011 – 2014, by region and country (excl. NI)

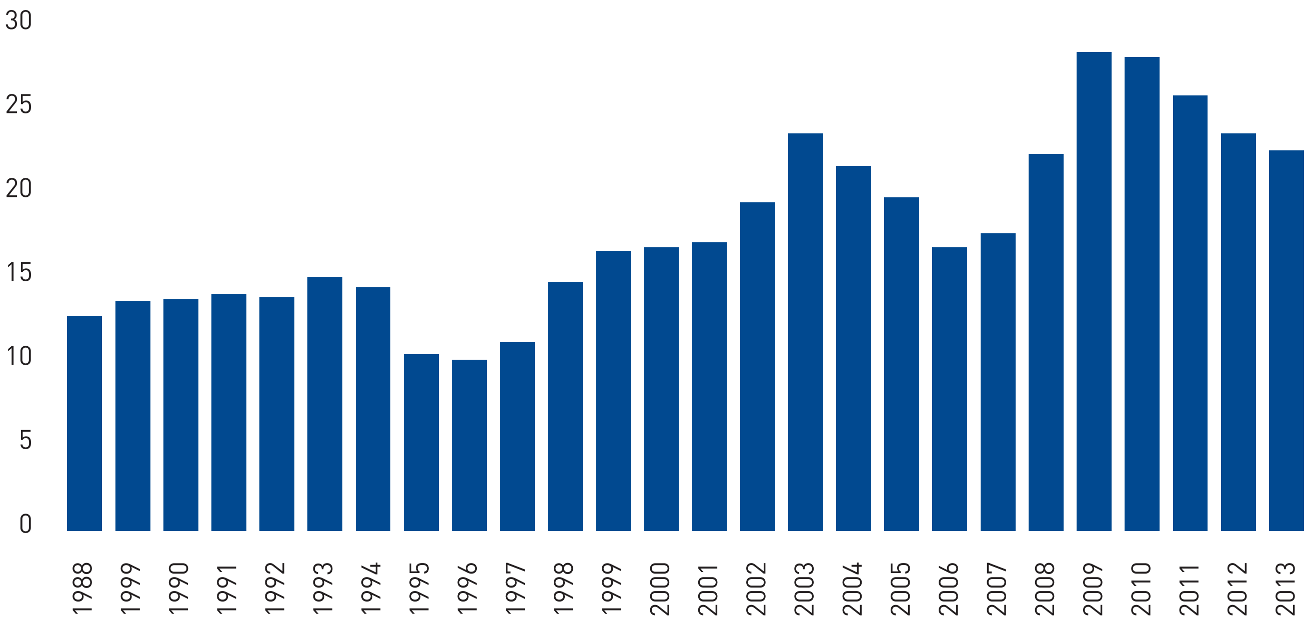


Source: ONS

As described in section 2.7, one of several hurdles encountered by first-time buyers (FTBs) when purchasing their first home is the tightness of lending criteria – including average deposits required by mortgage lenders. Since the 2008 financial crisis and subsequent collapse of the housing market, the average deposit paid by FTBs has grown from 17.2% of the property value in 2007, to 22% in 2013.

Several schemes have been introduced by Government to assist FTBs with putting together a deposit – most notably the 'Help to Buy' initiative. However, the fact remains that many prospective FTBs rely on their parents or relatives to come up with a sufficiently large deposit. Research carried out by Cebr for HSBC in 2012 showed that almost one in five (19%) FTBs depended upon financial support from their family to buy their first home.

Figure 22.
Average deposit as a percentage of average purchase price - first time buyers, UK, 2014

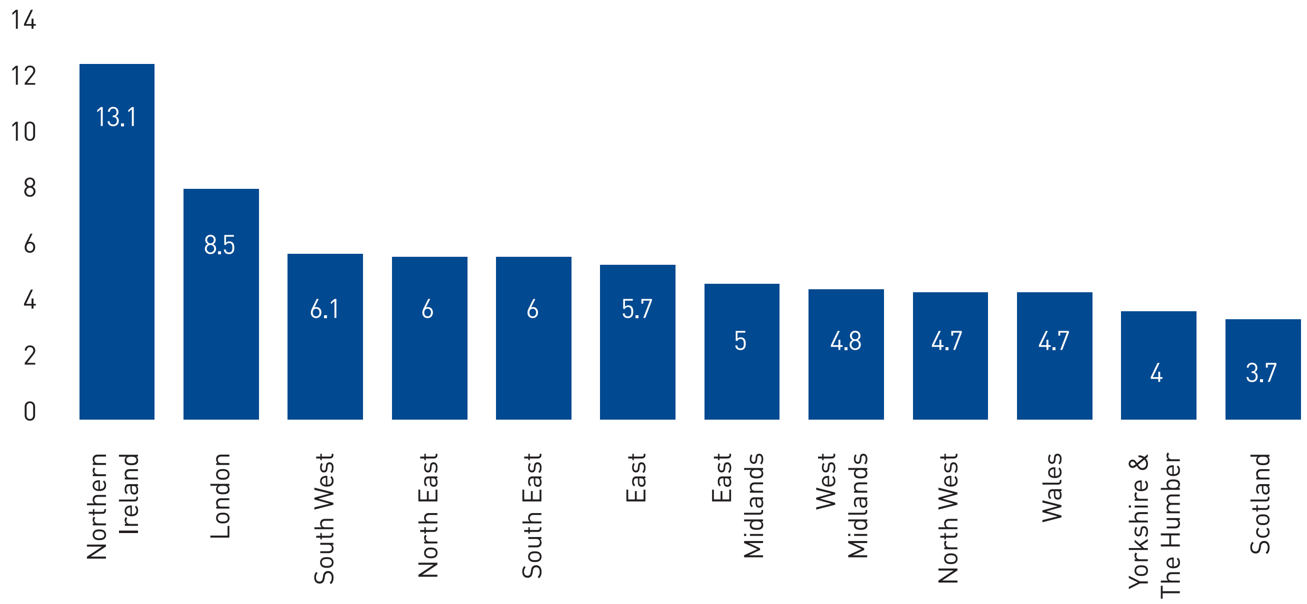


Source: ONS HPI supporting tables April 2015 – table 38

Without the financial support of relatives, FTBs are left with no alternative but to attempt to save for a deposit, the requirements for which are ever-rising. In London, a standard 10% deposit required to purchase an average-price FTB home now amounts to £36,000. Based on the savings rate of the average London household, it would take around 8 years to save a deposit of this size (see Figure 23).

As a result, home ownership has become infeasible for the average household in London, meaning families need to move outside the capital to find a property they can afford. The other choice is to privately-rent properties for their lifetime – a choice which is more common in some other European countries, such as Germany and Austria.

Figure 23.
Number of years needed to save a deposit for an average first time buyer home, by region, 2014



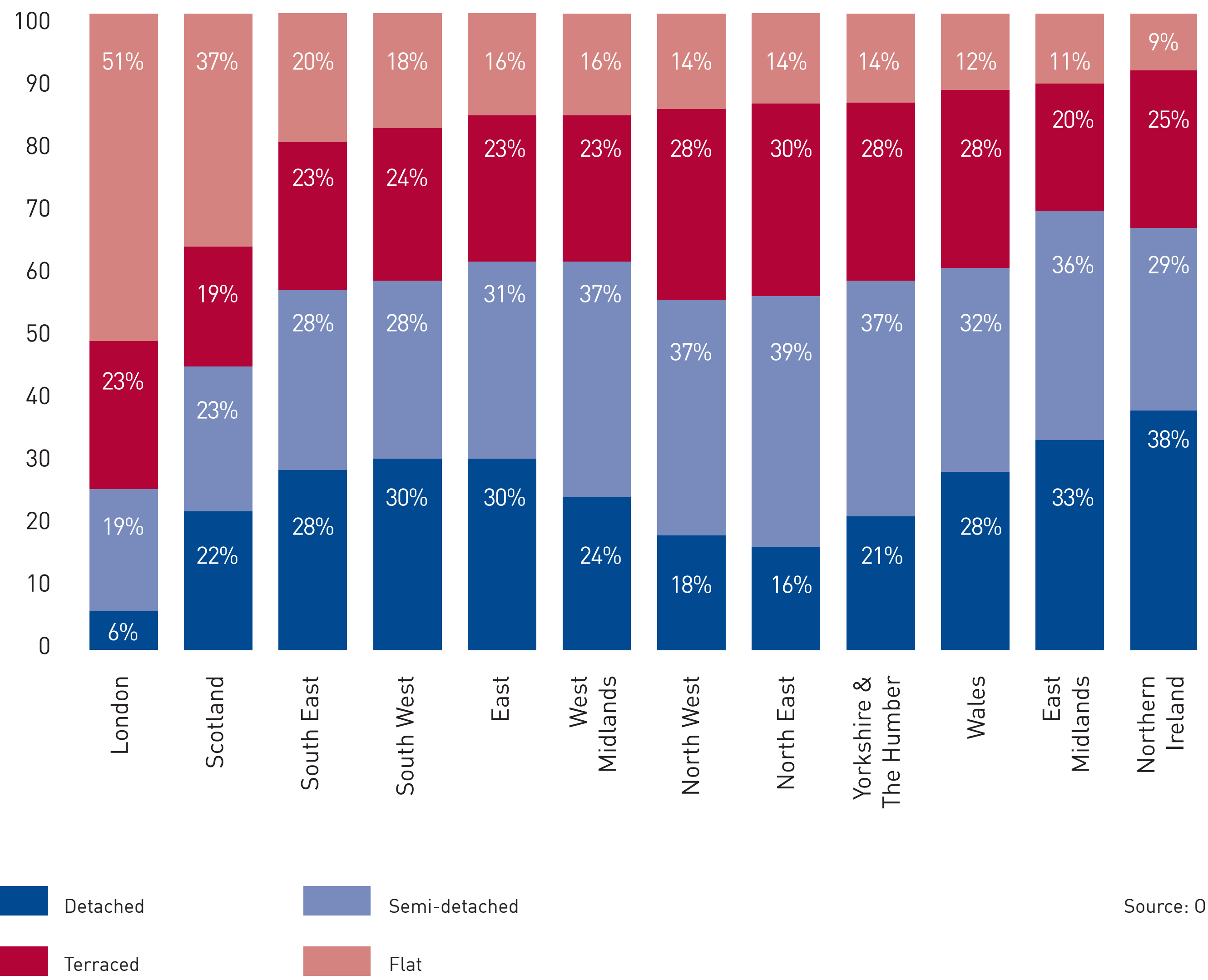
Source: ONS, Cebr analysis and calculations

4.2 Rental demand and available stock

Approximately 81% of UK households live in urban areas. However, unlike our mainland European counterparts, the majority of Brits live in houses – not apartments or flats. The semi-detached house is the most common type of home in the UK: this is an enduring symbol of 20th century suburbanisation, and a property type which houses 8 million UK households.

A wide variation in the housing mix can be observed across the nations and regions of the UK. In London, the majority of households live in purpose-built flats or sub-divided houses, while in comparatively-rural Northern Ireland nearly two in five households live in a detached home (see Figure 23).

Figure 24.
Households by accommodation type, by region



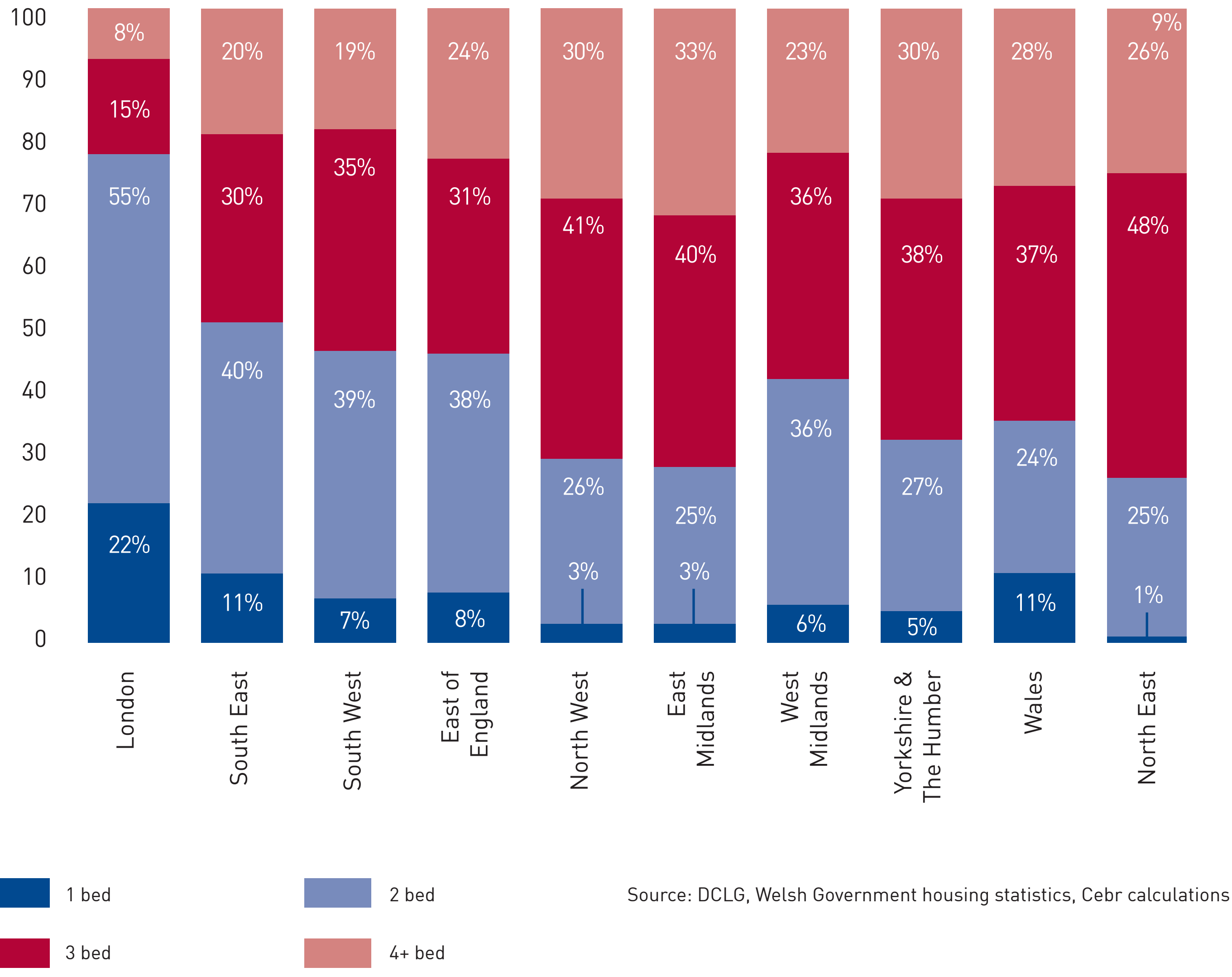
Source: ONS

The housing mix in the UK's regions and nations reflects the historic pattern of settlement in towns and cities, the level of urbanisation and population density, and the housing pressures in each area. In the UK's major cities and particularly London, millions of homes suffered damage as a result of bombing during World War Two. In many urban areas, terraced homes were replaced by medium and high rise apartment developments. In other towns and cities, suburban housing estates were built to provide replacement housing.

These historic patterns of development have left some parts of the UK with housing stock that is not well-fitted for the demographic profile of these areas. For example, in England the number of over-65s is projected to increase by 20-25% in all regions by mid-2022, compared to general population growth of just 7.2% overall. This shifting demographic profile, combined with England's legacy housing stock, will mean that more and more old people will be living in homes which are too large for their needs. Moreover, suitable properties for downsizing are unlikely to be available in sufficient quantities.

When we consider the types of new homes that are being built in each region, we can see that the majority of homes have three or more bedrooms (with the exception of London). This reflects market demand in those areas and the underlying cost of building new homes, which remains sufficiently low in many of the UK's regions to permit the building of larger properties. In London, however, in 2013/14 four out of every five new homes had either one or two bedrooms, reflecting the specific demographic profile of the capital, and the unique demand pressures that exist.

Figure 25.
Housing completions by number of bedrooms, by region, 2013/14

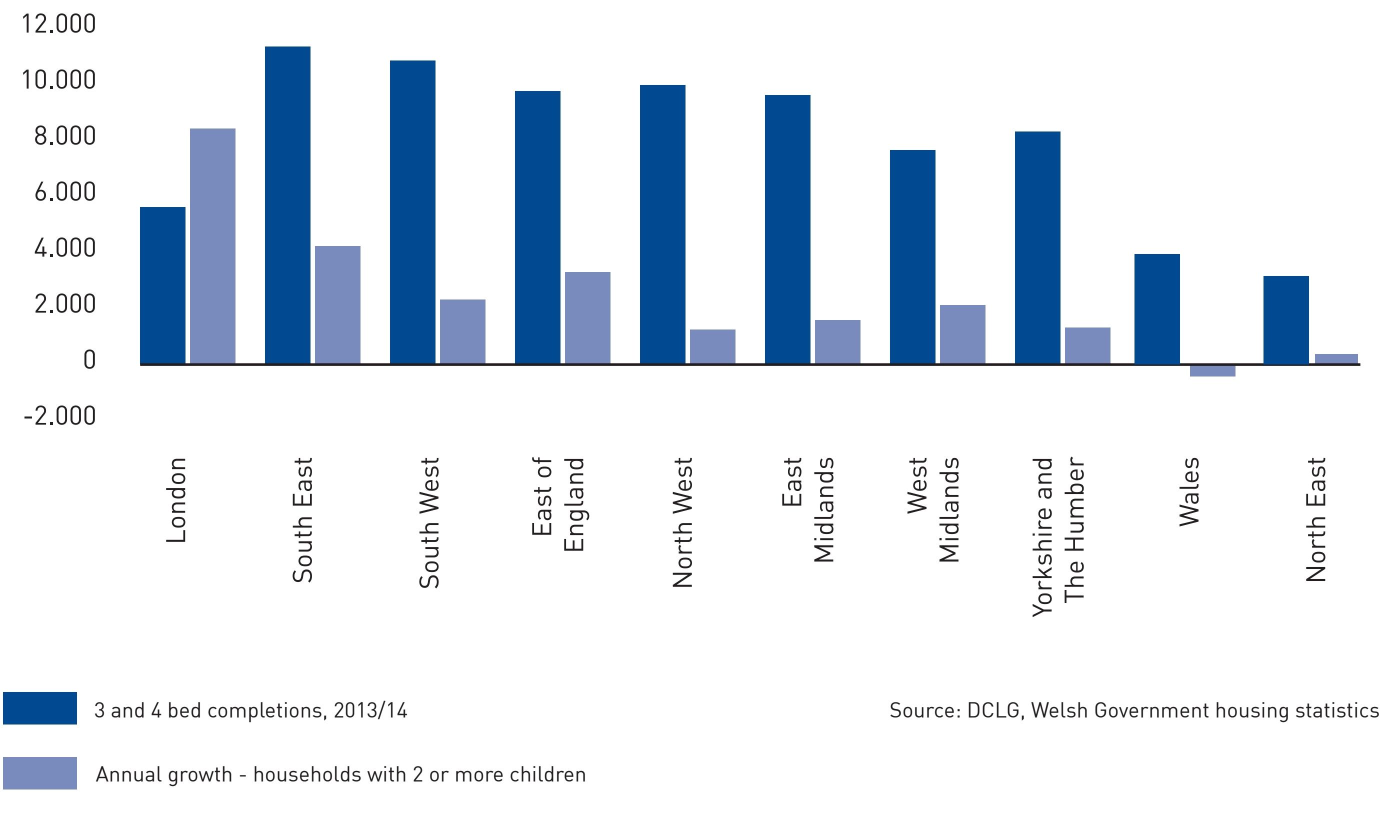


Source: DCLG, Welsh Government housing statistics, Cebr calculations

While the differences in housing mix across the UK's regions and countries are clear, the important question is whether we are building the right types and sizes of homes for the estimated 2.5 million new UK households which will be formed between 2015 and 2025.

To investigate this question, we compare the number of new homes built by size (number of bedrooms), with the projected annual growth in households - this provides an indication of underlying demand for housing. The analysis, summarised in Figure 26 below, gives an indication of whether, and to what extent, the new homes being built in each region meet the requirements of new households in those regions.

Figure 26.
3 and 4 bedroom housing completions 2013/14 and projected annual growth in households with 2 or more dependent children 2011 - 2021, by region



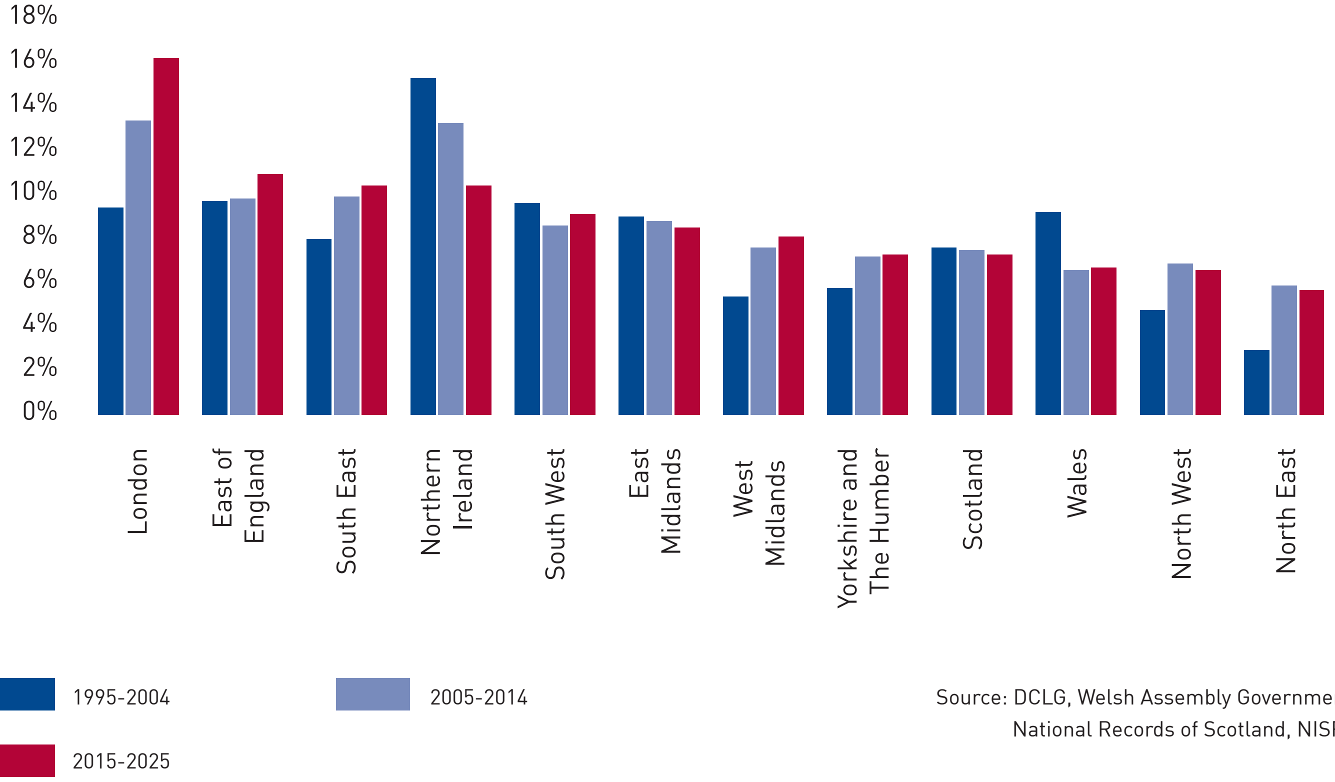
Source: DCLG, Welsh Government housing statistics

The analysis reveals that in most regions, the number of larger homes (i.e. those with 3 or more bedrooms) being built far exceeds projected growth in households with two or more dependent children. The sole exception is London, where projected growth in larger households exceeds the number of larger homes built during 2013/14 by 50%. High prices and the lack of suitably-sized properties in London will mean that unmet demand in the capital is likely to continue to be satisfied in the Home Counties around London. In these areas, completions of 3- and 4-bedroom homes is more than sufficient to meet demand generated by the local population.

Overall, the epicentre of the UK's housing shortage is likely to continue to lie firmly in London. The number of households in London is projected to grow 16% between 2015 and 2025, while those in the East and South East regions will grow by 10.8% and 10.3% respectively (see Figure 26).

Ideas on how to address some of these imbalances and the housing affordability crisis are among the topics discussed in the next section of this report.

Figure 27.
Household growth by region, historic and projected



Source: DCLG, Welsh Assembly Government, National Records of Scotland, NISRA

5. ROLE OF POLICYMAKERS

5.1 Achievability of current housing targets

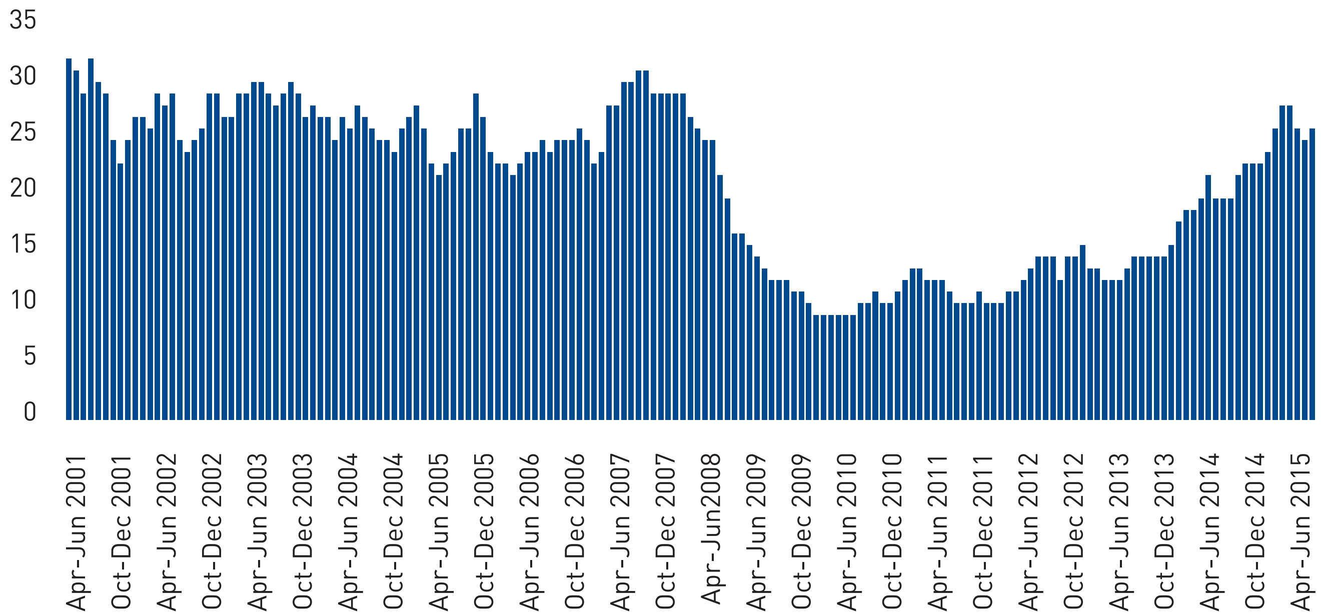
The last Labour Government under Gordon Brown's leadership made use of specific housing targets. They were calculated based on projected demand at the national level and set for each regional planning authority. The regional target would then be allocated between the local planning authorities. As part of the 2011 Localism Act, the Conservative and Liberal Democrats Coalition government discontinued the use of nationally set housing targets. The Conservative Government elected in May 2015 has acknowledged the need to boost house building and requires councils to present plans for new homes by 2017. If this is not done, the government will produce the plans for them. Furthermore, the Housing and Panning Bill was announced in the May 2015 Queen's Speech. In order to boost housing supply a statutory register for brownfield land will be introduced with the aim of developing suitable brownfield sites more quickly. Additionally, the neighbourhood planning system will be simplified, also with the aim of speeding up house building.

While the Housing Bill may prove to be a good first step, further government action is needed to ensure sustainable levels of housebuilding, especially in the medium and long term. In order to consider necessary policy revisions, it is crucial to first understand the existing and potential barriers to boosting housebuilding levels.

The primary obstacles explored in this section are skill shortages, supply shortages, and plateauing productivity in the building sector.

The number of vacancies in the construction industry has been rising almost constantly since late 2012.

Figure 28.
Number of vacancies in the UK construction industry, seasonally adjusted, 000s



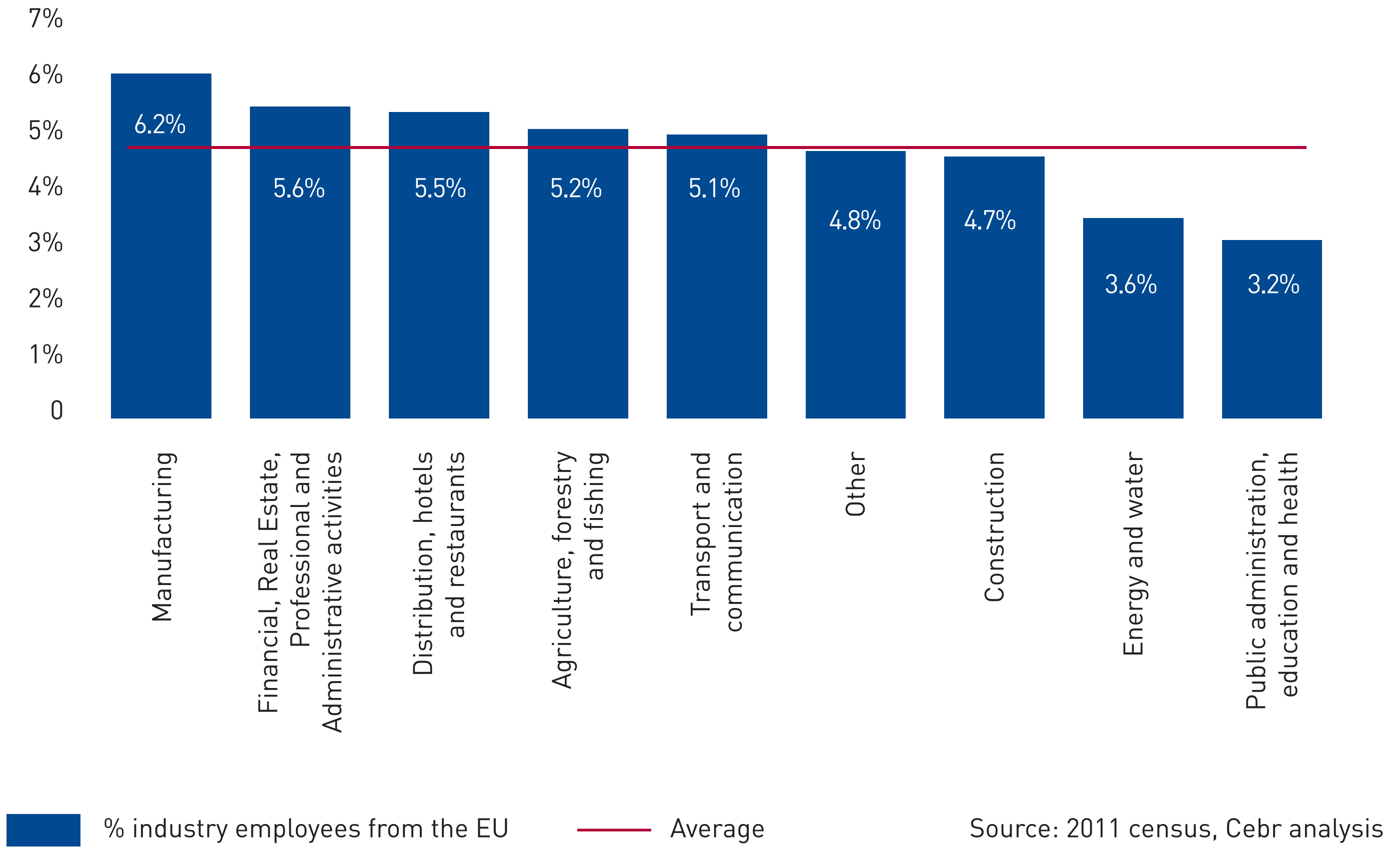
Source: Office for National Statistics

The construction industry contracted during the financial crisis and many UK nationals working in the field found new careers, while a number of foreign builders who lost their jobs returned to their home countries. Another adverse impact of the financial crisis was that, when faced with collapsing revenues, many construction firms cut spending on training programmes, thereby limiting the number of skilled workers for the future.

Extreme shortages of skilled workers in certain occupations, including bricklayers and electricians, have led to an increase in average weekly wages, which may make certain projects less profitable for developers, thereby discouraging building. In order for government policy to address skill shortages it is necessary to provide incentives for firms to offer apprenticeships in the shortage fields. As this process may not increase the labour supply substantially in the short term, it is also necessary to boost the number of non-UK nationals eligible for construction sector jobs.

The Conservative Government has committed to a referendum on EU membership by the end of 2017. Given that a notable number of EU nationals work in the construction industry, should the UK choose to leave the EU and assuming the free flow of labour is not maintained, this will put an additional strain on skill shortages in the construction industry.

Figure 29.
Non-UK nationals born in EU countries as share of total work force, by industry, 2011



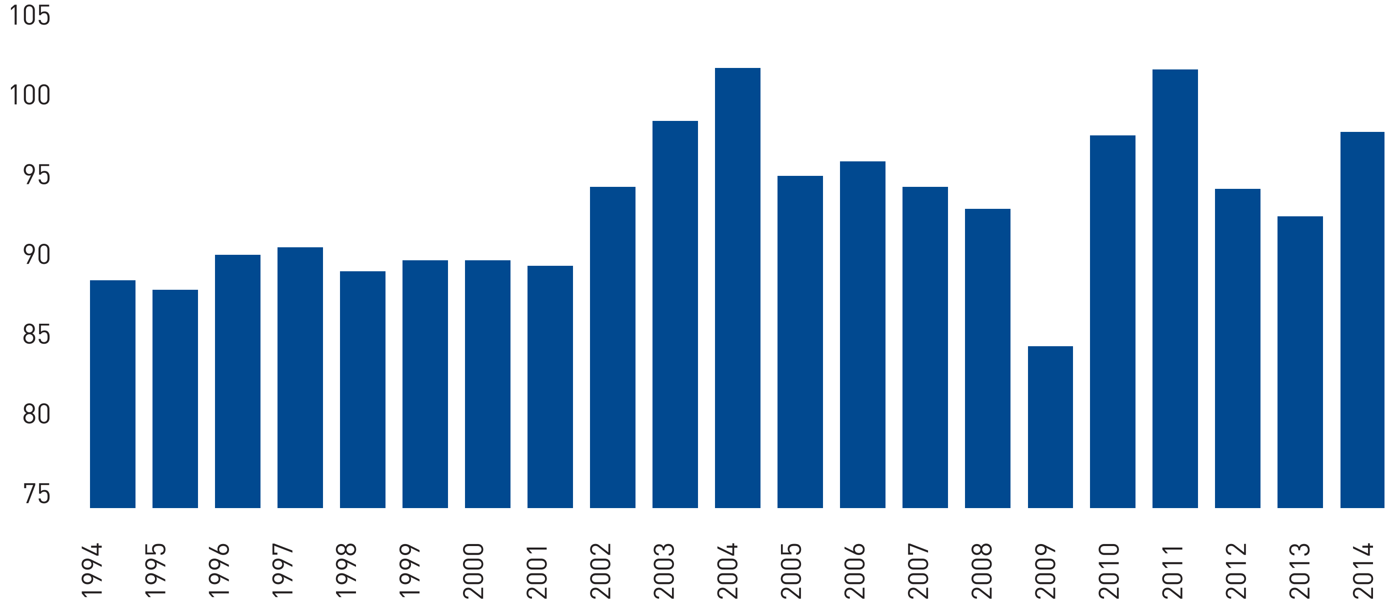
Source: 2011 census, Cebr analysis

Given the extent of skill shortages in the sector it is actually necessary to boost, rather than limit, the number of non-UK nationals working in construction. While EU nationals are already able to move freely to the UK and take on construction jobs, it is virtually impossible for non-EU nationals trained in this field to move to the UK in pursuit of work. The Home Office publishes an annual list of shortage occupations, which specifies occupations for which employers may apply to hire non-EU nationals without fulfilling the Resident Labour Market Test[8]. Currently there are no construction worker occupations on the shortage list despite the shortage crisis in affordable housing. Adding key occupations to this list would enable workers from all over the world to be considered for construction jobs, thereby filling many vacancies and helping boost housing supply.

Supply shortages may also hinder the government's ability to boost housebuilding. The availability of certain construction materials, most notably bricks, has diminished since 2014. This is in part because many brick manufacturers produce only just enough supplies to meet forecast demand and the pick-up in housebuilding has been greater than expected. Also contractors may need to adjust how they obtain their supplies. During the financial crisis and weak recovery that initially followed, so little building was done that those firms that were working became used to acquiring the materials they needed at short notice. Although larger industry participants often forward buy their supplies based on projected requirements - leaving little available for immediate purchases - now that demand is rising, delivery times may be extended, which may impact particularly on smaller builders. Occasional shortages are putting upward pressure on prices, which may attract new entrants into the industry and alleviate the problem.

However, boosting productivity among existing industry participants is also necessary for achieving higher levels of home building. In the UK construction industry, productivity (output per hour worked) in 2014 was lower than a decade ago. Investing more in training or providing incentives for the private sector to boost vocational education may help boost productivity.

Figure 30.
Output per hour worked in the construction industry, UK, indexed so that 2011=100



Source: Office for National Statistics

In summary, in order to address the low level of housebuilding the government must tackle skill and supply shortages. In order to address skill shortages it must provide incentives, such as tax breaks for private sector firms to offer apprenticeships and training programmes for shortage occupations in the construction sector. As this will be a time-consuming process, in the short term it is necessary to allow more non-EU nationals to move to the UK and take up construction jobs. The first step on this front would be adding roles such as brick layers to the Home Office's shortage occupations list. In terms of the supply shortages, housing policy certainty would allow producers to adequately forecast building material demand and thus limit the risk of shortages.

5.2 Depoliticising the housing market

A source of numerous market failures in the housing market is the frequent and often politically motivated changes to the policy area.Given the persistence of the housing affordability crisis, it could be lucrative for policymakers to make changes to housing regulation near election time, in order to please segments of the electorate. What makes housing policy especially susceptible to political influence is that changes in this area can be felt by the population very quickly. For example, lowering Stamp Duty Land Tax charges immediately benefits everyone buying a home.

Hence, the UK housing market often lacks the long term policy certainty needed to reassure developers and investors that it is desirable to start development projects with extended completion dates. An extreme solution would entail the formation of a housing market authority – an independent body of non-elected officials who make decisions on long term housing policy. One shortcoming of such an approach is that, in the UK especially, housing decisions have such a drastic impact on people's lives that it could be perceived as democratically illegitimate not to elect the individuals in charge of making these decisions.

However, the benefits of delegating housing policy decision to a permanent, non-partisan body far outweigh this argument. Policy areas which are highly susceptible to political manoeuvring (i.e. where government policy commitments may be deemed as having low credibility) and where a high level of technical expertise is required to reach optimal decisions are often considered by political economists as areas where power should be delegated to independent bodies. A common example includes central banks handling monetary policy – as is the case with the Bank of England's Monetary Policy Committee (MPC). Although no such precedent exists for housing policy, the current state of the UK housing market is unprecedented as well. Consequently it requires an application of new and innovative ideas.

5.3 Preparing the housing market for an increase in rental demand

Politics impact not only the construction and buying market, but also the rental sector. In the months before the 2015 May general election, the Labour Party suggested that should they be part of the new government they would regulate the private rental market more heavily. Primarily, the Party proposed banning high charges for signing a tenancy agreement and making longer, three year tenancies the standard in the sector. While longer tenancy agreements prevent landlords from increasing rent excessively, they may cause certain externalities or negative consequences. For example, landlords may set higher initial rental charges in anticipation of the fact that they will be unable to change the amount for a number of years. Additionally, more landlords may start requiring costly background checks on prospective tenants, motivated by the fact that it will be more difficult to change occupancy. Political intervention in the rental market may have consequences for the broader economy as well. For example, longer leases may discourage people from moving around the country, thereby reducing labour mobility.

Many of the steps which the government has taken in order to prepare for the growing number of renters across the UK have been moves in the right direction. For example, in April 2013 a Private Rental Sector Taskforce was established in order to facilitate investment in rental properties. The move recognizes the growing need for rental accommodation and the fact that much of this future demand will be met by large scale, institutional investors. Merging this taskforce with an independent housing regulator as described earlier in the section would expand their mandate, thereby giving them greater influence into future sector developments.

Given the losses encountered by many investors and builders in the financial crisis and its aftermath, many are still reluctant to invest in large scale projects. Recognizing this, in February 2013 the government launched a £10bn scheme which provides a guarantee on debt raised to invest in new privately rented homes. This also decreases developers' borrowing costs, allowing more funds to go directly to the private rental market. A continuation of similar incentives under future parliaments will help prepare the country for the coming surge in rental demand.

An issue faced by many prospective tenants is the poor quality of available rental stock or the inability accurately to establish the quality of the properties on offer. Given that the UK is increasingly becoming a country of renters this will become an issue for more and more people. The government can help alleviate this issue by offering a voluntary review process for landlords who wish to have their property classified as 'high quality' or 'kept up to high standards'. In the capital, the London Rental Standard scheme offers such a service providing accreditation for landlords. Extending a similar programme to the rest of the UK could both increase the overall quality of rental properties on the market and enable prospective tenants to easily make well informed decisions.

5.4 Encouraging 'rightsizing'

Analysis conducted in 2014 by the Office for National Statistics suggests that 1.1 million households in England and Wales (4.5% of the total) were overcrowded. On the other hand, 16.1 million households (69.0% of the total) were under-occupied. This suggests that there is scope for targeted policy to encourage those households with spare space to downsize, allowing more families living in overcrowded flats and houses to move into bigger properties.

Many residents of under-occupied houses are pensioners who have not changed properties since their children moved out of the family home. Encouraging this segment of the population to relocate to smaller properties could boost the supply of family homes in the market, which could in part offset rising demand.

The decision to downsize is a difficult one to make, especially if no suitable properties are available in the same area. Hence government policy which makes the prospect of downsizing more attractive could contribute to boosting house supply. One of the main barriers for pensioners wishing to sell their family home and relocate is the lack of suitable choices. A June 2015 report commissioned by Legal & General and compiled by Cebr found that when last time buyers[9] are looking for a new home, the most common preferences are being close to family and friends (32%), being near their current neighbourhood (18%), having easy access to healthcare (16%) and being located near shops (10%). This suggests that traditional senior living centres which often require residents to move far away from their existing home and may limit access to community facilities do not necessarily offer a great enough incentive to downsize. In order to encourage the development of more suitable properties, the government may offer tax relief on the development of specific properties that are suitable for pensioners looking to downsize.

A barrier for all prospective home buyers, not just pensioners, is the Stamp Duty Land Tax payable on all residential property sales over £125,000. Since it is in the broader interest of all prospective buyers that under-occupied households 'rightsize', a government policy which offers last time buyers a stamp duty exemption might see more family homes come on the market. Such a policy might entail an initial loss for the Exchequer, but as the number of transactions across the market increases (due to more family homes becoming available) any initial decline in stamp duty receipts would be at least partially offset.

The changes to inheritance tax announced in the 2015 Summer Budget may also have an impact on a pensioner's decision to downsize. At present, inheritance

tax is charged at 40% on the value of the estate above £325,000. The Conservative Government has announced their intention to take the family home out of inheritance tax starting from April 2017, except for those whose home is worth over £1 million. This will be done by adding a family home allowance to the existing threshold. In order to ensure that the policy does not discourage downsizing, a tax credit will be offered to those that sell a more expensive property and move into one that better suits their needs. However, the availability of such tax credits will be conditional on several factors, including what is done with the proceeds of the home sale. Hence, making the family home a privileged asset class exempt from inheritance tax could, despite the tax credit policy, encourage pensioners to hang onto more valuable properties. The changes would be especially discouraging for pensioners who are considering selling their home and renting a property. These households would not be able to benefit from the inheritance tax revisions in any way and thus may reconsider their preference to start renting.

As stamp duty is a one off charge that only represents a small portion of the entire home buying process, this alone may not be a great enough incentive for many pensioners to downsize. Hence, the government should also explore additional incentives, such as access to over-65s bonds with market-beating returns for downsizers. The government could permit only funds obtained through property downsizing to be converted into the bonds. Given that it has already been proven that there is a strong appetite among the over-65s for bonds such as these, re-introducing them, but with the added qualification tied to downsizing, would boost the supply of properties on the housing market.

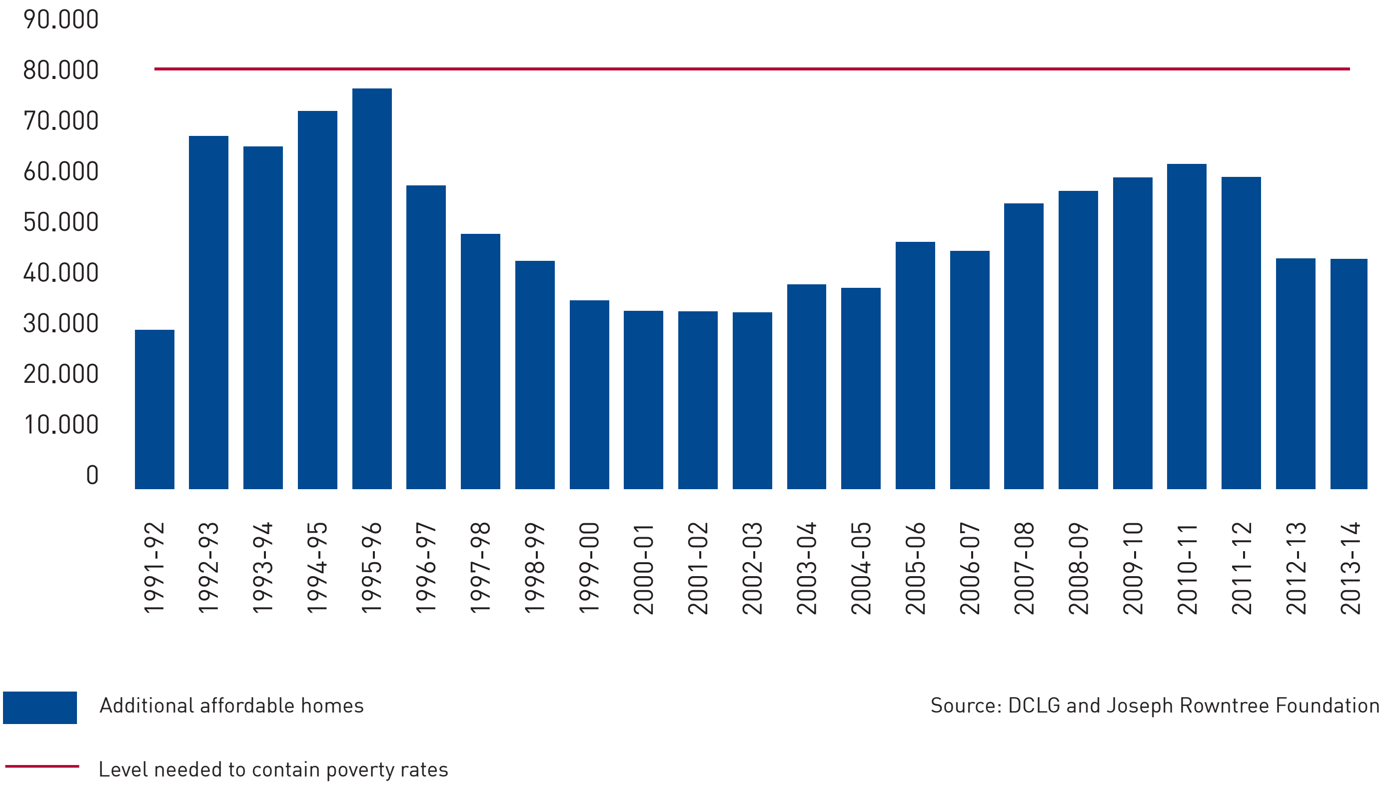
Encouraging people to move out of under-occupied properties would also have an impact on the private rental sector. Given the rising demand for rental accommodation and the fact that Britons are renting later into life, it is common for several single individuals to occupy the separate bedrooms of a larger property. Hence, some properties that come onto the market as a result of downsizing will be bought by individuals who do not intend to use the properties themselves and will end up on the private rental market, thereby boosting supply.

5.5 Extending the Right to Buy and affordable house building

The Right to Buy is a scheme that became popular in the 1980s and over the past four decades has enabled council tenants to purchase at a discount the properties they were previously renting. In the lead-up to the 2015 general election, the Conservative Party pledged to extend the same right to housing association tenants[10]. Although the intention of the policy – to help more people fulfil their home ownership ambitions – may be noble, numerous unintended consequences may arise if the policy is implemented in its current form.

Most concerning is that the policy may reduce the availability of affordable housing. The provision of affordable housing is already at a level below that necessary to contain poverty rates and taking properties off the market without encouraging the provision of additional affordable homes may worsen the situation.

Figure 31.
Additional affordable homes provided annually in England



Source: DCLG and Joseph Rowntree Foundation

Also it is not uncommon for affordable homes purchased at below market prices to end up back on the rental market, but with private landlords and at higher prices.

Housing associations use the existing stock of properties to borrow against. Should the value of their existing assets decline it will become more difficult to obtain financing for further building.

In order to increase the supply of affordable housing, extending the Right to Buy will not be sufficient and may even be counterproductive. Further steps should include revisiting the definition of 'affordable' housing, enforcing affordable housing quotas more strictly, and making use of long term vacant dwellings. Rents and purchase prices of affordable housing are largely set as a share of the market value. A more appropriate approach to ensure that the people who are meant to be helped can actually take advantage of these properties could be to set rent and purchase prices in relation to the average earnings in the region.

There are an estimated 610,000 vacant dwellings in England[11]. Until early 2013 owners of empty properties enjoyed a council tax exemption for the first six months and would get a 50% discount thereafter. Since 2013 this has been abolished and councils can also charge a 50% premium on properties that have been unoccupied for longer than two years. However, a much greater incentive is necessary to discourage property owners from holding onto vacant properties. Even if higher taxation does not put a substantial number of properties on the market, the added revenue could be put towards providing affordable housing.

5.6 Revisiting the green belt debate

The green belt policy was introduced in the UK in the 1940s aiming to make city living more enjoyable by limiting urban growth. Specifically, the policy designates areas of countryside in the proximity of urban regions where development is not permitted. In England, the total green belt area is 1.6 million hectares or 13% of total land area. The metropolitan green belt around London covers 484,000 hectares or 3.7% of the English land area. As home prices around the country have grown strongly in recent years and the building sector has continuously failed to keep up with surging demand, many have called for a reduction in the size of the green belt or further permission to develop on this land.

Supporters of the current green belt policy argue that preserving specified nature areas improves the quality of life in the UK by preventing urban sprawl, stopping neighbouring towns from morphing into larger cities, preserving the natural setting of historic towns, and ensuring that no city dweller is ever too far away from the country's nature escapes. More abstractly, some claim that the green belt is inseparably tied to the British way of life. However, many of these arguments relate to relatively minor quality of life benefits which are enjoyed by only a few at the cost of rising housing costs for many.

Those calling for development of the green belt argue that limiting development of such vast areas of land hinders economic growth and contributes to the ongoing housing shortage and diminishing home price affordability. Furthermore, although the very phrase 'the green belt' brings to mind an image of expansive natural beauty, in reality part of the land not eligible for development is lifeless and barren. It is also a fact that at the time when green belt areas were designated, the UK was not in dire need of land for development as it is now.

As the debate regarding the future of development on the green belt depends so heavily on the value associated with access to nature, it is very difficult to quantify the pros and cons of maintaining the policy as it currently stands. However, it is difficult to argue that any development on the green belt would deteriorate quality of life to a point that justifies allowing the housing affordability crisis to persist. Strong negative feelings among many constituents have too heavily influenced the debate on the matter, leading to political reluctance to discuss various policy options. As addressing the housing affordability crisis would benefit much of the country, shying away from an open debate on the topic favours only the strongly represented interests of the minority. Given the pressing need to create more homes, it is necessary to revisit the idea of reducing the land area of the green belt and to designate a committee which would explore this possibility in detail. Encouragingly, in late 2015 some steps in this direction were taken with the government publishing a consultation outlining plans to allow councils to allocate small sections of the green belt for starter homes.

Chapter notes

[8] The Residential Labour Market Test involves proving that an effort has been made to fill the vacancy with a UK national by, for example, advertising the position within the country.

[9] home-owning households living in under-occupied homes with two or more spare bedrooms, where the head of the household is over-55 and who have expressed a preference to downsize

[10] On July 20, 2015 the House of Lords voted for an amendment to the Charities Bill which may hinder the Right to Buy extension.

[11] Data refers to 2014.

[12] www.cpre.org.uk

6. CONCLUSION

This report has examined the current conditions in the UK housing market and provided forecasts for a number of key variables relating to both the buying and the rental segments. It has also provided an international perspective with a review of select housing markets across the globe. The German, Swedish, and Singaporean cases offer lessons as well as warnings about a greater degree of state intervention in the housing market.

We also examined the housing mix and how it varies across the regions. Across the country, people are waiting until later in life to buy their first home. The problem is especially pronounced in London, where just half of all properties are owner-occupied. Higher deposit requirements, tougher mortgage lending criteria, and rising prices are among the main reasons that many young people are finding themselves unable to buy a home. Unless more drastic measures are taken to boost housebuilding, this trend is set to continue or even worsen. The affordability crisis is turning many into eternal renters, which has placed upward pressure on rental prices, so that even for renters housing expenses will account for an increasing share of disposable income.

Action on numerous fronts is necessary in order to reverse or slow down the trends of rising prices and worsening affordability. Some of the options include depoliticising the housing market and thereby offering greater policy certainty, encouraging 'rightsizing' by various incentives, making use of long term empty properties and revisiting the possibility of developing green belt land.

Britain deserves better.

That was the simple plea Propertymark made in our Housing Manifesto, published ahead of 2015's General Election. Our nation, we reflected, was standing on the precipice of a crisis in housing supply. Our members across the country had witnessed sharp falls in properties for sale, rental price increases and a heavy decline in housebuilding. For too long governments of all persuasions had buried their heads in the sand, rather than face the challenge of matching growing demand with dwindling supply.

The General Election ushered in a new government, and with it fresh pledges to solve the acute problems facing the property industry. The government would, it said, aim to build one million new homes before the end of this Parliament, in 2020.

Fine words. But words are not enough. The housing crisis facing Britain is deep-rooted. If it is to be solved, it will require finance, suitable land, time, new skills and – increasingly – appropriate national regulation of the key stakeholders, not least the estate agents and letting agents that form our membership.

It will also require a degree of political will and industry consensus. Propertymark commissioned the Housing 2025 Report to help contribute to the debate and shape that political will, both at a national and regional level. Its findings and recommendations are both radical and sensible. But if we are to finally confront the fundamental challenges facing our industry, and build a future for Britain where everybody has the opportunity to own or rent a decent home, then we need more than words. We need action.

David Cox
Chief Executive, ARLA Propertymark

Mark Hayward
Chief Executive, NAEA Propertymark

Words are not enough.

The housing crisis facing Britain is deep-rooted.

We need action.