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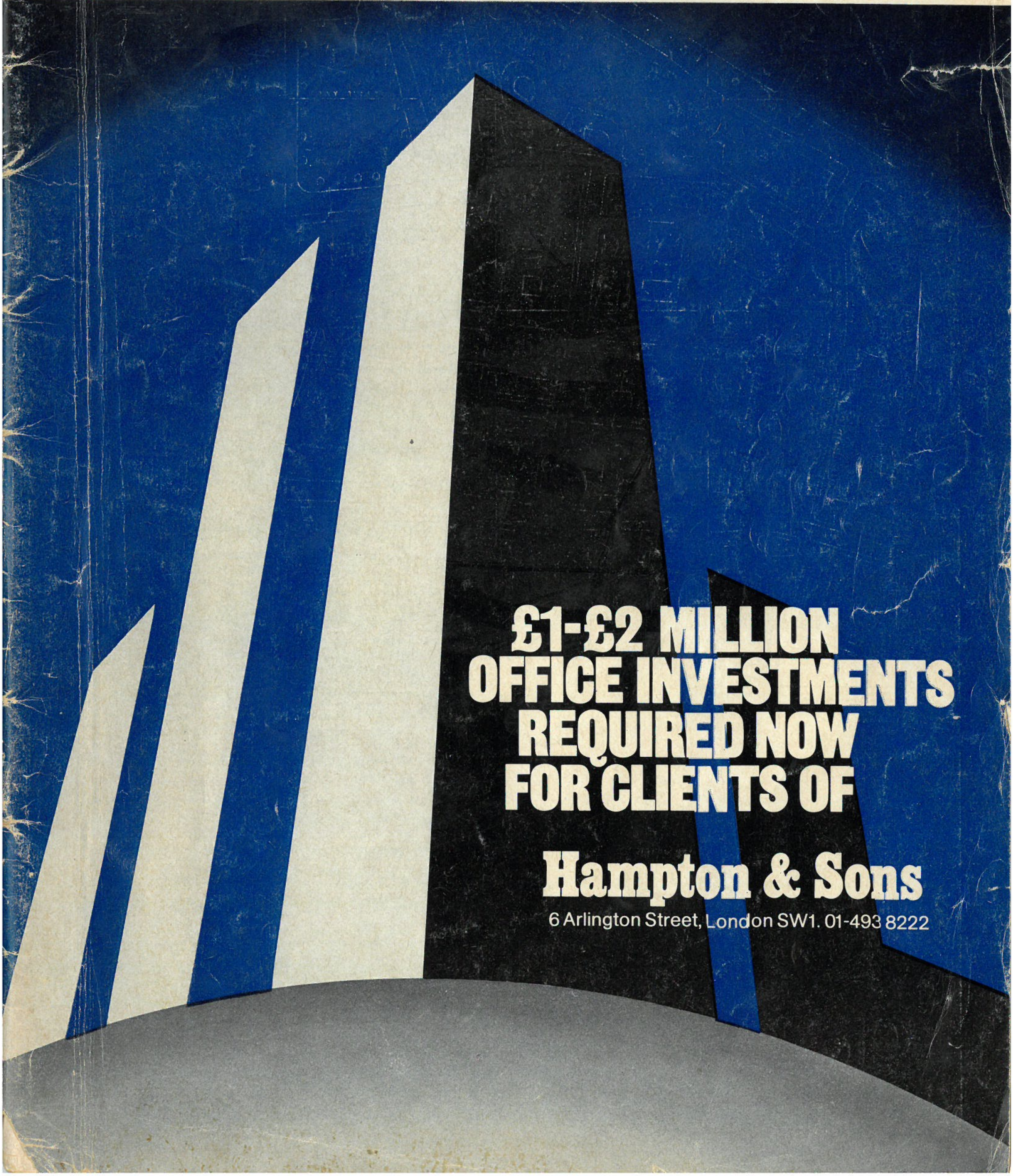


# Housing Policy: Some Alternative Views

*A commentary in the light of the Government's Green Paper "Housing Policy: A Consultative Document" by Michael Oxley BSc (Econ) MSc, lecturer in urban land economics at Leicester Polytechnic.*

"The brutal fact of the matter is that for all this weight of law and money, no government in my view has ever had a consistent housing policy" (Anthony Crosland, 1974). Whether Crosland's successor at the DOE has moved towards consistency with the Green Paper published on June 28 1977 is as open to question as whether consistency will ever be possible in this confusing, complex, and illogical field.

Why do we have a housing policy? Presumably because market forces have been deemed to have failed to produce and allocate housing services satisfactorily. What is "satisfactory" is a judgment which implies the setting of standards. It is frequently claimed that the prime purpose of policy is to secure a decent home for all families within their means. Why are some households unable to obtain "decent" accommodation? Possibly because they do not have sufficient income or wealth to attain the standard, or because there is an insufficient supply of accommodation of the required standard.

F G Pennance[1] argued that we have not examined logically the question of why the market is not producing the desired results, and that the most serious impediments are those raised by government intervention. Real housing problems, he claimed, were obscured by polemic and sentimentality. "The solution is in increased supply or higher real income, or both." Economists have frequently argued that housing policy has evolved piecemeal, with an almost complete disregard for the realities of market forces.

It might be argued that subsidies are necessary because housing costs are too high for some households to buy "desirable" quantities of housing; because imperfections in the capital market restrict the flow of funds to housing or push up the costs of such funds; because other imperfections restrict supply; or because macro-economic changes produce fluctuations in building activity which may waste resources. It can thus be reasoned that the requirement is a transformation of "need" into effective demand. But this must be matched by an increased supply if the need is to be satisfied. If one accepts the thesis that the problem is to increase supply and improve allocation, then policy should aim for more houses being built or an improved supply being obtained from the existing stock by more efficient allocation and/or physical upgrading.

Much discussion loses sight of the supply problem and concentrates on demand. The Green Paper shows no inclination to reverse policies which have both indiscriminately subsidised the demand for a scarce commodity—so pushing up the price and forcing it further away from low-income families—and perpetuated controls which have kept back supply and exacerbated shortages.

Increased supply requires increased or redirected investment. Any sensible policy must have due regard for the difference between costs and returns, for this is the main determinant of housing investment. An important distinction must be made between housing *expenditure* and housing *investment*. Increased expenditure will not necessarily result in a proportionate change in real investment. It might merely increase prices, or the economic rents received by the current owners of real property, though in the long run some increased real investment might be a consequence.

The Green Paper tends to treat expenditure as investment. A definition states that "investment includes, in the public sector, capital expenditure on new building (including land), acquisition of houses in Housing Revenue Accounts; and in the private sector, expenditure by home-owners on the purchase of new homes and grant-aided improvements." Expenditure, *per se*, contributes nothing to solving housing problems.

Much of government policy has diverted attention from investment. Indeed it has been positively discouraged by policies which arbitrarily allocate much of the existing stock, thereby failing to make the best use of what investment there has been. Policy was once geared to "disinvestment," in the name of slum clearance.

The debate can be pursued by taking the traditional "three sub-sectors" approach—owner-occupation, the public sector, and private-rented accommodation.

### Owner-Occupation

The Government does much to encourage demand in this sector. The extent to which tax relief on mortgage interest payments and the absence of both capital gains tax and a tax on imputed rental income are truly subsidies has produced considerable debate; much of it semantic. These three measures clearly encourage rather than discourage expenditure. The extent to which they increase investment is less certain. There may be more efficient and direct means of achieving that objective. That they redistribute income and wealth in ways which many people find objectionable is undeniable, but they are to continue and indeed be reinforced by extra measures to help first-time buyers.

### Mortgage Interest Tax Relief

The relief of mortgage interest payments from tax has been one of the more controversial policy measures, and it was envisaged that modifications might confine the benefits to lower income groups or basic-rate taxpayers. But there are to be no such changes. The £25,000 upper limit is to be "kept under review," says the Green Paper, probably with a view to raising it.

The Building Societies Association[2] claims that tax relief is not a straightforward subsidy since it varies with the rate of interest and the tax rate. These items, however, merely alter its value: it is still a subsidy. The association argues that if housing is treated as an "investment good," tax relief should be allowed on the loan to acquire this asset; if treated as a "consumption good" one cannot ask for a tax on imputed rental income while none exists for other consumption goods, and thus "owner-occupiers can be regarded as being subsidised by having tax relief on mortgage interest or by being exempt from tax on imputed rental income, but not both."

The curious reality is that housing is both a consumption *and* investment good and those who chose to purchase a house get substantial advantages over those in other tenure groups and those who have put their funds into other investment outlets. Mortgage interest tax relief can be viewed as an income-regressive subsidy. Those with higher incomes have larger mortgages, larger interest payments and larger subsidies than those with lower incomes. For higher-rate taxpayers the relief is greater still. It has thus been argued that this measure redistributes resources towards the better-off and runs counter to the idea of concentrating effort on ensuring better basic housing for those who need greatest help.

The consultative document argues that any change in the system would upset the planned budgets of millions of households. So it would if tax relief were suddenly completely abandoned—any substantial change of policy is bound to hurt considerable numbers of people. The continuation of the measure is also defended in its context as part of "general assistance," meaning aid, "which meets some part of housing costs without regard to an individual householder's ability to pay," despite the acknowledgement that "some households therefore get more help than they strictly 'need' to enable them to afford a home of a decent basic standard." It is further claimed that a reduction in general assistance would probably lead to a reduction in effective demand and therefore lower investment in housing. Or would there merely be lower expenditure?

It has alternatively been claimed that such measures lead to over-consumption of housing by higher-income groups and possibly divert resources away from productive investment elsewhere—in manufacturing, say—and so contribute something to the UK's poor economic performance. A slightly different argument suggests that although expenditure is increased by the subsidy system actual consumption may not be increased, and the net effect is merely an increase in economic rents.

The real effects on housing investment of such measures as mortgage interest tax relief are difficult to quantify. An intuitive approach suggests that a major consequence is a level of demand above what it would otherwise be; and that increases in such demand will produce, with an inelastic supply, increases in prices. In flexible and efficient capital and construction markets the expected long-term consequence would be an increase in supply. But the investment response may not occur. In a United Nations study of *The Relationship of Financing to Housing Production in Europe and the United States,*[3] D Jaffe argued that mortgage subsidies may result simply in an increase in the ratio of mortgage loans to the housing stock without any significant increments to this stock, and that there can be no assurance that subsidised mortgage loans will not be used to replace non-subsidised loans or to decrease the equity proportion of housing investment. Such responses might be most significant for higher-income groups. For the United States several empirical studies have indicated that such substitution is significant and that the efficiency of mortgage subsidy schemes is low.

### Savings Bonus and Loans Schemes

The Government intend to reinforce demand subsidies with their " savings bonus and loans " schemes for first-time buyers. Those who had saved would obtain a bonus which might, at an interest rate of 7 per cent net of tax, be worth about £100 on top of the normal £260 interest to a couple putting aside £20 a month to save over £1,000 in five years; or about £30 to those saving £40 a month for just over two years. " A £500 loan would be available to each first-time buyer who had saved at least a matching sum under the savings bonus scheme, had been saving for not less than two years, and who was buying a house within a specified house price limit (with variations by geographical area); the loan would be interest-free for the first five years and repayable with subsequent interest over the remaining duration of the mortgage or upon redemption of that mortgage." The waiver of interest would be worth £200.

One doubts whether we really know if such a scheme would result in more people wishing to buy houses. An extra £230 over five years may not sway the balance one way or another for those who have saved £40 a month for two years. The hope is that a lump-sum payment would facilitate a smaller mortgage loan or be used to meet loan payments in the early years. It might alternatively have the effect of increasing offer prices to the advantage of existing property owners. Some gains for those able to save and those wishing to sell a house may thus occur. This could be seen as a further indiscriminate distribution of income and wealth. Are these really the people in greatest housing need? It is by no means certain that any increased construction or renovation will result.

### Supply Subsidies

A radical alternative to the demand subsidies pursued in Britain is to subsidise supply directly. This means starting with the question " How can the production of housing services be increased?" An answer can be given only after careful consideration of the determinants of construction and maintenance output, including the specific problems of the house-building industry. The tone of the Green Paper in parts shows an appreciation of the industry's fluctuating demand problems, but nothing by way of direct assistance to builders is offered. In fact there is very little about the industry and its possible contributions to housing policy—imagine a Green Paper on food which had so little on the problems of farmers! Construction, which has a vital role to play, has the highest bankruptcy rate of any industry. No measures to subsidise private-sector output directly are considered. Other European countries have such measures.

The question of increased output might be answered by reference to the organisation and productivity of the industry, and measures which improve internal efficiency are desirable, but the major problems for housebuilders centre on the demand for their product and their costs, together with the future prospects for each. A prime determinant in both cases is the prevailing level of interest rates. Consider a policy which subsidised builders', rather than purchasers', borrowing costs. Lower costs, increased profitability and increased production would be the expected market response.

The most elementary market analysis suggests that measures which directly subsidise costs are likely to be more efficient in producing output increases than are demand subsidies. Supply subsidies could reduce interest costs or involve a payment for each house or conversion made. We have masses of comparable measures for manufacturing industry. It might be claimed that the capital market is not well geared to meet the financing requirements of small building firms. The Government needs to consider the flow of funds to builders much more thoroughly. There may be a case for establishing some sort of " Finance for Building " agency which would channel funds at subsidised rates of interest, if necessary for medium or long terms.

The Green Paper's request that building societies earmark more of their funds for new houses by increasing their " quotas " to builders is hardly a significant alternative. It leaves too much to chance. The proposals to maintain a stable supply of mortgage funds by persuading the building societies to contine accumulating liquid funds when the inflow is high, and run them down when the inflow is lower, will similarly operate in a much more indirect and uncertain manner even if reinforced by the fresh sources of funds that might be tapped by the mooted new financial intermediary which would raise funds from institutions—in particular life and pension funds—and " on-lend " them to building societies. It might be better to have a co-ordinated attack on the problems of the availability and cost of finance for both purchasers and builders.

Minimum lending rate and the money supply is the key to instability in construction demand and output, to bankruptcies, to booms and slumps in house prices, and to changes in the expenditure that households have to devote to housing. Changes in monetary controls are not designed to have such consequences for housing. They are, given the present structure of the capital and money markets and the accepted wisdom on macro-economic policy, unfortunate but inevitable consequences of attempts to deal with inflation, balance of payments, or unemployment problems. High interest rates and reductions in the supply of credit increase builders' costs and reduce the demand for their product while low interest rates and increases in the supply of credit produce rapid increases in house prices. The last seven years provide ample empirical evidence.

### A Protective Buffer

It might be reasoned that the need is to isolate housing from some of the consequences of macro policy by means of some sort of buffer. The detailed form and *modus operandi* of this could only be concluded after a detailed examination of the UK capital market, but a finance-for-building agency which provided funds both for builders and borrowers might provide such a buffer, stabilise the flows of funds to each, and provide a means of subsidising the supply—and, if it still be deemed necessary, the demand for housing.

The low rates of interest which builders were charged need not be uniform. Positive discrimination in favour of particular types of dwelling and particular localities could be tried. The agency might lend at more stable rates for longer periods than are currently available, and thus improve certainty. The agency need not lend directly to house purchasers. It could " on-lend " to building societies (as the Government has envisaged) and lend to local authorities. These mortgage lenders could lend directly to house-buyers at low rates of interest. Mortgage interest tax relief would no longer be necessary. The mortgage lenders would be persuaded to offer an escalating scale of interest charges—larger rates for larger loans. The effect would still be a mortgage subsidy—possibly subject to some of the objections raised previously against mortgage interest tax relief—but certain major defects would be removed. This subsidy would not be income regressive. The better-off would be helped less than those on lower incomes, and the system need apply only to new borrowers—initially at least.

Some longer-term gradual transfer to the new scheme for existing borrowers could ease the cries of pain from those with existing large mortgages. The scheme might be used to achieve the objective of stabilising household budgets more effectively than the existing arrangements or Green Paper proposals. The interest rate could be fixed or repayments indexed to prices or incomes. The agency could monitor and influence both housing demand and supply, thus mitigating some of the inflationary effects of demand subsidies.

The activities of the agency need not be confined to the owner-occupied sector. It could be the means whereby funds are channelled to local authorities and housing associations at low rates of interest, and so become a major means of subsidising the public sector. It might even be used to encourage private-sector landlords by lending at low rates of interest for the purchase of property to rent or for improvements. The cost reductions and supply increases could provide a very effective means of helping tenants. This is not a detailed proposal but merely an example of an approach that can be suggested by giving more emphasis to supply problems.

**The Public Sector**

Three major issues are apparent in relation to public sector housing—investment, rent determination, and the allocation of accommodation.

Investment is largely a matter for the local authorities. How much investment should occur in a given area must, in the absence of market criteria, be determined by some estimate of need, for which new (as yet unspecified) guidelines, are to be issued. The local authority will also have regard to its sources of finance—rents, rates and Exchequer subsidies. The major cost is interest, and again changes in minimum lending rate have inevitable, although partially cushioned, effects on investment programmes. The Green Paper proposes measures to alter the complicated basis of the existing Exchequer contribution to one based on broadly meeting the difference between costs and a "reasonable" local contribution (from rents and the General Rate Fund).

But what is reasonable is by no means clear. The subsidy would be determined annually after discussion with the local authorities of their housing investment programmes, which will set out a strategy for local public-sector housing over the next four years. It is impossible to make clear judgments about the level and nature of investment without knowledge of how local needs and contributions are to be determined.

An aspect of the new system would be that both the balance between rents and the General Rate Fund contributions and the fixing of individual rents would remain matters for local discretion. There are thus to be no general principles governing rent levels, and local-authority tenants are to be subsidised to different extents according to where they happen to live. The wide variations in rent levels which result were highlighted in Chapter IV of *Housing: the Chartered Surveyors Report,*[4] which recommended a return to the fair rent principle and the continuation of the rent rebate system with the total costs being met by the Exchequer. Such a system would relate rents both to the accommodation and the income of the household. There would, however, be no reason to have the "accommodation element" in a system where tenants are allocated housing on the basis of need. The principal function of prices is to allocate. Why retain prices if allocation is to be by non-price methods? An income-related payment would be sufficient to ensure that payments for housing were according to means—council house rents would not be necessary if no real choice over accommodation existed.

The Green Paper makes the welcome suggestions that allocation procedures should be made public and the practice of imposing residential or other qualifications for inclusion on a housing list be ended. It does not, however, propose national guidelines for deciding who gets what. Thus, clear principles and procedures for determining what is supplied, who occupies housing, and what they pay are to be sacrificed to some vague notion of local autonomy.

There is already plenty of scope for local discretion in the design and quality of accommodation. Parker-Morris standards have concentrated on internal arrangements, and the application of their criteria can lead to too smug a satisfaction with the quality of local-authority accommodation. A much more imaginative view of housing quality which relates not just to basic amenities but also to the quality of the housing environment is called for. This implies better design of new stock and better management of that which exists with reference both to what people like and dislike about their dwellings and their neighbourhood.

**Private Rented Sector**

There are those who consider it morally unacceptable that profit be made from owning houses in which other people live. There are also those who believe that free-market principles applied to rented accommodation could improve the quantity and quality of accommodation. Rent controls have survived principally in the name of protection of tenants from "exploitation." This word is usually used to mean high rents. Rents can rise only to the extent that supply fails to meet demand. The problem can be seen as one of deficient supply. One does not require a Marshallian grasp of economic analysis to realise that rent controls ensure that supply must always be less than demand.

Pennance argued that "there is no economic case for rent control in any form and its continuance can be regarded as a ritual sacrifice to an obsessive and blinkered view of distributive justice linked with a curious disregard of elementary market analysis."[5] An opponent might argue that the sudden abolition of rent controls would indicate "an obsessive and blinkered view" of the efficiency and equity of market forces.

The Labour Party in its evidence to the Government in response to the consultation paper on the Review of the Rent Acts[6] claims that private landlordism "has outlived its usefulness," and suggests that the interests of landlords and tenants are irreconcilable. The Green Paper does not take this view. It acknowledges that "the needs of many people . . . will only be satisfactorily met by renting, and under present arrangements most of them would not have a very high priority in public sector waiting lists," and furthermore "the terms on which new private investment might be attracted into a publicly accountable letting agency should be explored."

Beyond this there is little of significance concerning this sector: "It would be premature to reach conclusions about the long-term future of private renting before the Review of the Rent Acts is completed." The Green Paper is thus by no means a complete review of housing policy. A comprehensive strategy can be formulated only by means of a co-ordinated approach to the three main tenure groups.

Rent controls can be viewed as promoting a redistribution of income from landlord to tenant. In their contribution to housing shortages they may make matters worse for those looking for property to rent. The shortage can also be seen as a reflection of the failure of local authorities to provide accommodation of the right type on the right terms for certain groups. If the public sector is not to relieve the shortage, private sector supply will need to be encouraged. This means increasing the return to landlords. This does not mean that tenants need suffer or necessarily pay any more, for rent allowances related to income could continue. The inelasticity of supply would ensure that in the short term a sudden increase in rents resulted only in increased economic rents for owners. Any change in housing policy would need to take account of the problems of adjustment to that change. Only in the long run might supply increase. A pre-announced phased increase in landlords' returns over a long period might help to produce a better relationship between return and supply. The essential information needed to determine the merits of a change is not so much dogma or prejudice but indications of the likely supply response to increases in return.

### Renovation and Improvement

As the Government has acknowledged, an increased supply of housing services need not come from new construction, and a new emphasis on improvement is proposed. Subsidies in this area are supply- rather than demand-orientated, and are thus potentially one of the more valuable aspects of housing policy. Proposals to counteract the tendency over the last few years "for a growing proportion of resources devoted to renovation to go into relatively high-quality improvements in both sectors, rather than into an attack on the most serious problems—the large number of houses mainly in the private sector, which are either unfit or without basic amenities" may serve to increase the effectiveness of such aids.

The economist's "externality" argument suggests that a major reason for market forces failing to promote large amounts of improvement is the "atomistic" nature of the decision-taking. One man improving his property does not get a satisfactory return because rental and capital values are related to the state of repair and appearance of adjacent properties and the local infrastructure. This argues for still greater emphasis on the local authorities' role in improving the quality of neighbourhoods and the exterior as well as the interior of properties.

The Green Paper does not consider the ability of the building industry to carry out efficiently the renovation and repair work of the type and in the locations required. This is another example of a case where a full consideration of supply problems is lacking.

### A Final Comment

In a moment of elementary enlightenment the Green Paper notes: "In the last analysis, the effectiveness of any national housing policy and local housing strategy is likely to be judged by how far it helps those facing the most pressing housing problems." There is a danger, however, that the "middle-way"—the lack of radicalism, the attempt at consensus—which the paper goes for will result in the continuation of a system which will be judged harshly against this criterion. We shall continue to tax most of the people in order to help most of the people meet the costs of their dwellings. As long as market forces are not completely rejected, effective policy must concentrate on turning need to effective demand and ensuring that the demand is satisfied. If low income is the cause of inadequate demand then the answer would appear to be measures to increase incomes by, for example, higher wages, lower taxes, direct income subsidies, or a more fundamental programme which saps whatever are deemed to be the roots of poverty. In this context, bad housing conditions are merely a reflection of a deeper malaise, and concentrating on the reflection will not alter the reality.

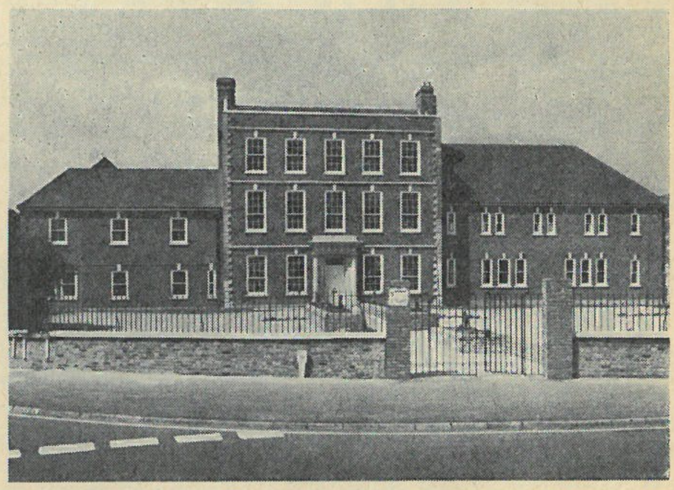
If we redistribute incomes and allow the market to adjust without any supply encouragement the process could be long and painful, with the real value of the income increases being eroded by higher prices. Measures which encourage supply by keeping down costs also increase the real value of incomes. Much of what we do at present, and much that is proposed in the Green Paper, helps those who do not need help, fails to support the most disadvantaged, pushes up housing costs, and hinders rather than helps supply.

### References


1 *Housing Market Analysis and Policy*, Institute of Economic Affairs 1969.
2 *Facts and Figures Bulletin Number 8*, October 1976.
3 In *Financing of Housing* (Proceedings of the Seminar in Geneva, August 1973, United Nations).
4 RICS 1976.
5 op cit.
6 See "The Shape of Things to Come?" ESTATES GAZETTE, July 2 1977, p 31.


## SLOUGH OFFICE REFURBISHMENT LET AND SOLD

The Chantry-Keys Group have let their office refurbishment at Langley Hall, Slough, to Wilkinson Match, through their agents Jones, Lang, Wootton. The building has a floor area of some 28,600 sq ft and the rent equates to just under £5.76 a sq ft. Matthews & Goodman acted for the tenants. The created investment has been sold by JLW and J P Sturge & Sons to the Scottish Equitable Life Assurance



Society for a price in the region of £2.4m. The purchasers were represented by Savills.

In the past two years the property, originally dating from Tudor times with Georgian and Victorian additions, has been substantially rebuilt, retaining only the original walls. A new frame, floors, roof and interior have been installed, together with a new wing at the rear finished in the same architectural style as the main building. Before the last war the building was used as an orphanage for actors' children, and during the war it was used as the headquarters of Bomber Command, afterwards becoming the home of the Road Research Laboratory.

## £5.5m Moore Street, Dublin, Redevelopment

Dublin Corporation have given planning permission for the £5.5m Moore Street redevelopment by Irish Life Assurance Co. The scheme, which has been under discussion since the late 1960s, will have the corporation as 50 per cent equity partners after a minimum yield to Irish Life, who are putting up all the cash and development expertise. The 5-acre site is to be developed with some 80 shop units, a department store, variety store and an extension to Roches department store, plus a market stall area. The covered shopping will extend to some 150,000 sq ft on one level, and there will be multi-storey parking for 650 cars. The shops are expected to be open for trading in 1980.

The architects are David Keane & Partners, the quantity surveyors Austin Reddy & Co. Lisney & Son are the letting agents.

## Bradford Factory Site Sold

Euroway Estates (Northern), represented by Anthony Brown Stewart, have sold 2.5 acres of land on their Bradford estate to Nibb-it International (UK) for £32,500. The purchasers are building a 20,000-sq ft factory for the manufacturing of snack foods. This sale brings the total area sold or under contract on the estate this year to 25 acres.

## The Incorporated Society of Valuers and Auctioneers

### GOLFING SOCIETY

The society played the Chartered Secretaries Golfing Society at West Byfleet on July 18 when the result was a win for CSGS by 10½ to 4½.