FINAL REPORT OF THE LONDON HOUSING COMMISSION

BUILDING A NEW DEAL FOR LONDON

March 2016

London Housing Commission

Institute for Public Policy Research

ABOUT THE COMMISSION

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ABOUT IPPR

IPPR, the Institute for Public Policy Research, is the UK's leading progressive thinktank. We are an independent charitable organisation with more than 40 staff members, paid interns and visiting fellows. Our main office is in London, with IPPR North, IPPR's dedicated thinktank for the North of England, operating out of offices in Manchester and Newcastle, and IPPR Scotland, our dedicated thinktank for Scotland, based in Edinburgh.

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CHAIR'S FOREWORD
LORD BOB KERSLAKE

Our capital city faces unprecedented challenges in housing its citizens. Double-digit annual inflation has resulted in house prices that are now some 45 per cent higher than they were before the financial crisis, pricing Londoners out of buying their first home. Renters are faring little better – while weekly wages have increased some 2 per cent in the past five years, rents are up by around 16 per cent.

Such forces make for damaging consequences: businesses struggling to recruit and retain staff, overcrowding in social and rented homes, stubborn levels of housing-induced poverty, and billions of pounds spent on housing benefit to keep renters afloat and provide temporary accommodation for homeless families.

Providing enough secure, affordable and decent homes is one of the biggest challenges now facing the capital, if not the biggest. London needs at least 50,000 of them each year to keep pace with its growing population. Against this ambition we are falling far short – last year, only 25,000 new homes were built.

In July of last year, IPPR (the Institute for Public Policy Research) established the London Housing Commission, comprised of experts from the worlds of housebuilding, government and academia. Our objective was to review the causes of London's housing crisis and to set out a clear programme for how the next mayor, the 33 London boroughs and central government should work together to tackle it.

We set ourselves the following tests:

- What would it take double the delivery of homes in London every year, and maintain high levels of delivery over the long term?
- What steps can we take to reconnect the costs of home ownership and renting to incomes in London?
- What can be done to provide a high-quality private rented sector?

Our call for evidence last year brought an extraordinary response from major housebuilders, planners, housing associations, London boroughs, homelessness charities and others, who generously provided a huge volume of evidence and ideas.

I would like to place on record my thanks to the panel, the team at IPPR, and all those who contributed evidence.

We concluded that there is no single root cause of London's housing malaise. Rather, this report exposes a great many barriers to building affordable, decent homes in sufficient numbers – from land to planning, investment to skills, subsidy to regulation. In response, we have developed a detailed and coherent package of recommendations.

Our proposals include many actions that the next mayor and boroughs can take immediately – to get more land into the pipeline, to improve the planning process, and to tap new sources of investment.

However, it is abundantly clear that the mayor and boroughs will not be able to address the full extent of the crisis unless they are given new powers by central government.

The new mayor and boroughs should therefore strike a major devolution deal with central government. On their side of the bargain, they should commit to increase supply to 50,000 homes a year by the end of the decade, to ensure that London has sufficient housing offered at submarket rents, and to eliminate poor conditions in the rented market by 2025. In return, the government should give London significant new freedoms to control its own planning, borrowing and tax.

The London Housing Commission does not claim to have all of the answers, but it is clear that the status quo will not do. The housing crisis will not solve itself, and radical measures of the sort we outline in this report will go a long way to delivering the volume of quality, affordable homes that London desperately needs.

SUMMARY

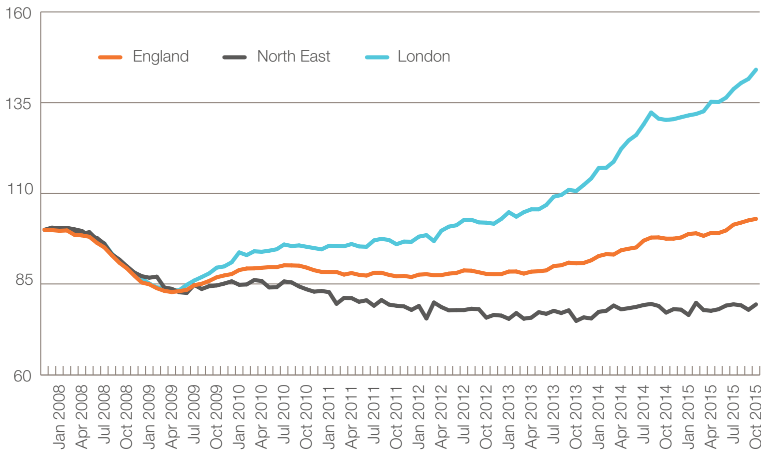
We have a housing crisis in London of a different order to the past

London has always been a relatively expensive city to live in, but the current crisis is of a different order to the past. The average house now costs half a million pounds, more than 12 times the median income: the highest the ratio has been since records began. House prices are now 45 per cent above where they were before the financial crisis hit.

Figure S1

House prices in London are now almost 50 per cent higher than they were before the financial crisis hit

House price inflation since pre-crash peak (index 100 = November 2007 prices)



Source: Land Registry 2016

This is reducing homeownership: the rate of mortgaged homeownership has been falling by around one percentage point a year for the last decade, and fewer than half of Londoners now own their own home.

The growing number of renters in the capital are faring little better. Rents in London, already twice the English average, are rising more quickly than earnings, meaning an ever-larger share of tenants' income is spent on rent.

Even though London's wages are the highest in the country, around a quarter of households are living in poverty, compared with a fifth across the country as a whole – a difference that is almost entirely explained by the high cost of housing. Changes to housing benefit and other aspects of the benefits system are yet to feed through to the poverty figures, meaning they are likely to get worse still.

As we have seen with the financial crisis and its aftermath, we cannot expect a 'market correction' or downturn to fix affordability in the capital. London's problems are now too entrenched – indeed the dramatically reduced supply that will result from any downturn will be a further barrier to fixing the capital's housing problems.

Measures to reduce demand, such as by achieving more balanced economic growth across the UK, can form only part of the solution

Population and income growth are keys drivers of the strong demand for homes in London. On current projections, London will be home to an additional 1.5 million people by 2030. High inward migration – both from elsewhere in the UK, and from abroad – is a driver as well as a consequence of London's success, and not something we should want to discourage.

In the long-run, an economic policy that encourages a more even distribution of business activity across the country – thus making London a relatively less attractive place to live – might help to alleviate London's housing crisis. However, even if such a policy were put in place today, it would take many years to achieve the sort of rebalancing we would need in order to see a significant improvement in the affordability of homes in the capital.

Some of the rise in house prices (and thus also rental prices) stems from buyers treating property as an easily financed and tax-friendly investment. The government has taken some steps to dampen this – for example, by increasing stamp duty on buy-to-let and second home purchases, and by imposing an annual levy on non-domiciled (non-dom) owners. But this will not solve the affordability problem in London or the shortage of supply: the basic problem remains that the population is growing while housing supply is not keeping up.

Increasing supply through conversions or more efficient use of existing stock will not be enough

Building new homes is not the only way to boost housing supply: returning empty homes to the market or converting non-residential properties such as shops or offices for residential use can also play a role. However, the potential for either of these options to make a significant difference to London's housing shortage is limited. London has an estimated 21,000 long-term empty homes, versus an annual new homes requirement of at least 50,000. And large-scale conversion of office or retail space to new homes on the scale required would risk creating a new problem, by significantly reducing London's space for work and employment.[1]

Building more homes is therefore the only way to create the step-change in supply needed to improve affordability in the capital for the long term

The only way to solve the housing crisis is by building far more homes. On current population projections, we need to build 500,000 homes over the next decade if we are to match the expected growth in the number of households in the capital. This will not be easy: in the last decade, we built only 194,000. And these need to be of all types and tenures.

Recent government policies may help with supply – but nowhere near enough

The government's renewed commitment to delivering 1 million homes by the end of the decade is a welcome step, and it has taken measures to increase housing supply by changing planning rules, investing in infrastructure, and

1 Conversions of offices to homes also do not provide additional funding for community infrastructure and services, unlike new homes.

supporting buyers to access new-build properties through its equity loans scheme. However, despite these changes, new orders to build homes in London appear to have peaked in 2015, and shifting the dial from delivering 25,000 new homes in the capital last year to delivering 50,000 a year by the end of the decade will require many more effective interventions to keep the capital and the country building. The current array of government policies are not, on their own, sufficient to address this substantial shortfall.

It will take some time for supply to catch up – in the meantime, we must keep intervening to ensure that workers can afford to live in the city, in decent conditions

Even in the best possible scenario, it will take time for housing supply to catch up fully with population growth. In the meantime, market prices will continue to rise – which, other things being equal, means a further squeeze on household finances, rising homelessness, and growing complaints from businesses that their workers cannot afford to live in London. We also risk continuing to see many private renters living in substandard conditions.

To mitigate these consequences, we need continued intervention by government – at national, city and borough level – to ensure that a significant proportion of housing is genuinely affordable and that the standard of rental property is improved.

The government's focus on promoting homeownership through initiatives such as Starter Homes may move people from renting to ownership but not, by itself, have much impact on supply. Indeed, by putting all of our eggs in the homeownership basket, we risk making new supply vulnerable to a future economic downturn, when demand dries up and mortgage lending falls. Promoting homeownership, if it comes at the price of fewer affordable rented properties, will add to London's housing challenges.

The nature of London and Londoners' incomes means that we need to deliver more homes across all tenures in London, for people with a wide range of means and expectations. Of the 50,000 new homes London needs every year, 25,000 will need to be at market price (whether for sale or rent) and 25,000 will need to be 'affordable' (at submarket prices).

Within the 25,000 new homes needed at market price, experience shows that the market will not absorb more than 10,000 for owner occupation – so the remaining 15,000 will need to be for private rent. This target of 15,000 'build-to-rent' homes is well above London's performance last year, which saw the completion of only 5,000.

Within the 25,000 affordable homes needed, 15,000 will need to be social or affordable rent (compared to delivery last year of only 8,000) and 10,000 will need to be 'intermediate' homes (also well above current delivery levels).

Thus, across all tenures, London is falling short of its needs – and while increased homeownership is one answer, it is far from the whole solution.

Through strong leadership and increased placemaking capacity, it is possible to deliver the quantity and quality of required new housing supply

The housing challenge that London faces is huge but not intractable. The response must be led by London and draw in all of the public and private capacity that London possesses. The mayor and the London boroughs will need to combine their efforts and invest in new placemaking capacity at a city-wide and borough level, and local communities will need to be fully engaged in the growth and development of their own areas. By this approach it will be possible to deliver both increased quantity and better quality of new supply.

The terms of a new housing deal with central government

The mayor and London boroughs would be significantly better able to address the housing crisis if they were given new powers by central government. So they should come together to ask government for a new devolution deal, in return for a commitment that they will, by 2020, double the annual supply of homes.

The mayor and boroughs will only be able to deliver on that commitment if they work very closely together. To do that, they should form a joint London Housing Committee to coordinate housing policy across the capital, and to negotiate this new deal with central government.

They should ask central government for the following:

- To exempt London from the National Planning Policy Framework (NPPF) and instead give the mayor's **London Plan** the same status as the NPPF – and give the mayor the power to force boroughs to change their plans if they are not identifying enough land for housing. This will mean that local authorities outside London have a duty to cooperate with the mayor to help solve London's housing crisis.
- To allow the London Housing Committee to set **planning fees** for London.
- To allow both the GLA and the boroughs to **borrow** more for housebuilding and infrastructure.
- To devolve **stamp duty** on the same model as the government's recent devolution of business rates to local authorities, allowing London to retain a substantial proportion of its stamp duty income, in return for an equivalent reduction in grants from central government, and to adjust stamp duty rates in consultation with the business community, such as via the London Chamber of Commerce and Industry and London First.
- To allow the boroughs to levy, at their discretion, **council tax on developments that fail to meet agreed building targets.**
- To allow boroughs to create their own **landlord licensing schemes.**

In return, the mayor and boroughs should commit to central government:

- To double the supply of new homes to London to 50,000 per year by 2020, and to maintain this for at least the following five years.
- To ensure that London has sufficient housing at submarket rents.
- To eliminate non-decent housing in the private rented sector by 2025.

To lend credibility to those commitments, the mayor and boroughs should also commit to take a number of specific actions, including:

- To identify sufficient land to deliver 50,000 homes per year for the next decade.
- To significantly increase the volume and speed of planning approvals, by increasing the capacity of boroughs' planning departments and creating a London planning inspectorate.
- To earmark a significant proportion of public land for affordable housing and new privately rented housing.
- To take an active lead in the nurturing of housing and planning skills in the private and public sector.

Immediate actions for the mayor and boroughs

Even if central government does not rapidly give London the extra powers described above, there is much the mayor and boroughs can do right now to address the housing crisis and to prepare the ground for a future devolution deal.

Find more land

- **Speed up the release and development of public land** identified as not in use by the London Land Commission for building homes.
- **Lend planning expertise to Transport for London** for it to review the potential for higher-density development around tube, rail and bus stations.
- **Support communities to conduct their own neighbourhood planning** to identify opportunities for regeneration and small sites not currently in the London Plan.
- **Review greenbelt** land near public transport sites, in exchange for improved community amenities and the extension of greenbelt protections in other places.

Turn land into homes

- The boroughs should conduct and publish an **annual audit** of the progress of local planning applications in their areas, and the progress of large sites in particular. The sites identified by the audit as needing extra support to be developed, either from the boroughs, the mayor's office or central government, should be given that support.
- Offer public landowners the support of the **London Development Panel** to turn public land sites into new homes, on condition that a proportion of the public land is used exclusively for privately rented housing (for a limited period of time).
- Where it is appropriate for the site, or if a developer cannot be found, the combined resources of the mayor and boroughs should be used to **directly commission** housing on sites through housing associations and private developers.

- **Support smaller developers** by offering them first refusal on a proportion of small public sites identified for development through communities conducting their own neighbourhood planning, at no initial charge. The public landowner should take a stake in the sale or rental value of the homes created.

Improve planning

- Boroughs should publish an **annual review** of their progress against national and local targets for development.

Provide more affordable homes

- The mayor should immediately **issue London-wide guidance on negotiating affordable housing with developers**, and commit not to call in planning applications that demand a specified proportion of affordable housing.
- The mayor and boroughs should do a deal with **housing associations** to double their housebuilding in exchange for a pipeline of new sites.
- **Consult on simplifying the affordable housing requirement of planning negotiations** between boroughs and developers through the establishment of a London-wide affordable housing tariff.

Improve substandard rented homes

- Launch a **London lettings hub** to link up tenants directly with good-quality, accredited landlords, and to offer discounted lettings fees to landlords offering longer tenancies.

Timeline of major reforms over the next mayoral term		
	Year 1	Year 2
Negotiating with central government	Establish a joint London Housing Committee and propose devolution deal with government	Conclude devolution deal
Planning	Mayor to recruit multidisciplinary place-making team of planners, architects, surveyors and developers	
	Mayor to recruit a London planning inspectorate	
	Mayor and boroughs to launch consultation on planning conditions	New planning system launched with government consent
	Boroughs to conduct an annual audit of local planning applications and progress on large sites	
		Sites identified by annual review as needing support to receive help from boroughs, GLA and national programmes
	Boroughs to publish an annual review of their performance against housing and planning targets	
Land	Mayor to provide permanent status and resources to the London Land Commission to identify all private and public land that could be used for housing	Mayor to offer owners of non-operational public sites support of London Development Panel
	GLA place-making team to offer support to TfL to establish housing potential on TfL land	GLA place-making team to review density criteria and guidance
	Boroughs to launch campaign to support community-led neighbourhood planning	Boroughs to offer proportion of public small sites to SMEs
	Mayor and boroughs to review greenbelt land close to transport connections	
Investment	Mayor and boroughs to consult with pooled pension fund providers on London housing investment opportunities	
Affordable housing	Mayor to commission new affordable housing needs assessment	
	Mayor and boroughs to issue single set of guidance on affordable housing negotiations	
	Mayor and boroughs to begin consultation on housing tariff	Mayor to pilot tariff to assess risk and performance
		Mayor and boroughs to make a deal with housing associations to increase supply in exchange for bringing forward more land
Rented housing	Mayor to issue planning guidance to allocate proportion of housing zones land and London Development Panel sites for build-to-rent	
	Mayor to consult with boroughs, landlords, tenant groups and potential developers on launching a lettings hub for private renters	Mayor to launch London lettings hub

Year 3 (including new devolved powers)	Year 4 (including new devolved powers)
	Mayor to review borough plans and to call in boroughs who have not completed plans or met land targets
Launch consultation on changing planning fees in return for more efficient planning service Boroughs to begin to levy discretionary charge on sites that have missed housing delivery deadlines	Begin applying new fees
Mayor to work with DCLG secretary of state to release further government-owned land	
Boroughs to use additional borrowing capacity to build homes	
Mayor to use additional borrowing capacity to build infrastructure and homes	
GLA to retain portion of stamp duty	Review and consult on adjustments to stamp duty
Open bidding to new affordable housing investment programme, based on previous assessment of need	
Mayor to launch tariff and identify new housing zones	
	Mayor to review the case for a time-limited use class for build-to-rent
	Mayor to connect up licensing data with lettings hub
Boroughs to launch borough-wide licences	Licences to be made conditional on meeting decent homes standard by 2025

1. RECOMMENDATIONS: A NEW DEAL FOR HOUSING IN LONDON

It is clear that under the current settlement between London and central government, there is neither the power nor the resources in the capital to address the full extent of its housing crisis. Unlocking the additional homes that London needs (and that England needs) therefore requires a new deal between central and London governments, to steer London's housing market towards providing more good-quality, affordable housing.

This new deal for London must forge a collective commitment between the boroughs and the mayor to double the annual supply of homes across all tenures by 2020 – in support of the government's commitment to deliver 1 million homes by 2020.

Only working together can they ensure that the land, planning consents and capacity to bring forward London's new homes are in place. So, in exchange for additional powers and responsibility for housing policy, new working arrangements should be instituted through a stronger, joint London Housing Committee, bringing together the mayor and the 33 boroughs to determine housing and planning policy, and to make a comprehensive offer to government.

This offer should be:

- to double the supply of new homes to London to 50,000 per year by 2020, and to maintain this for at least the following five years
- to ensure that London has sufficient housing at submarket rents
- to eliminate non-decent housing in the private rented sector by 2025.

The mayor and the boroughs will need to demonstrate that, if and when a devolution deal is reached, they have the plans in place to ensure that these commitments can be delivered. To do so they should also commit to take a number of specific actions, including:

- to identify sufficient land to deliver at least 50,000 homes per year for the next decade
- to significantly increase the volume and speed of planning approvals, by increasing the capacity of boroughs' planning departments and creating a London planning inspectorate
- to earmark a significant proportion of public land for new privately rented housing
- to take an active lead in the nurturing of housing and planning skills in the private and public sector.

In exchange for these commitments, the government would need to unlock the following set of powers to ensure that the mayor and the boroughs can support homebuilding on the scale that London needs.

Powers and responsibilities: agreeing new devolved powers for London

Improving planning

Core to the devolution deal should be to improve planning. The commission has found much evidence that the conflict between national and city planning policies is an unhelpful barrier to achieving both London-wide and local objectives. To address this, the government should agree to provide full status to the London Plan, and ensure that local authorities, which benefit from London's growth, themselves support an increase in housing provision. Government should:

> **Exempt London from the National Planning Policy Framework (NPPF), and instead give the mayor's London Plan the same status as the NPPF – and give the mayor the power to force boroughs to change their plans if they are not identifying enough land for housing. This will mean that local authorities outside London have a duty to cooperate with the mayor to find land and build homes to help solve London's housing crisis.**

London's planning capability is constrained by the fact that planning departments and the key staff who are critical to planning – such as surveyors and legal advisors – are under-resourced, having had their budgets cut by 46 per cent over the last parliament. Charging planning applicants on a cost-recovery basis could help to ensure departments can process applications more swiftly and save developers valuable time and money in what are often lengthy processes. The government should therefore:

> **Allow the London Housing Committee to set planning fees, following consultation with the development industry, in exchange for reducing planning timelines and planning conditions.**

Increasing investment in affordable housing

A further key strand of devolution must be to increase the financial capacity of the Greater London Authority (GLA) and boroughs to build new housing, and the infrastructure needed to support that housing. Building the 50,000 homes a year that London needs will require total investment (both public and private) of around £16 billion per year – in 2015, total investment was around £8 billion. The government should therefore:

> **Allow both the GLA and the boroughs to borrow more for housebuilding and infrastructure.**

This additional borrowing capacity should come with more autonomy over and responsibility for property taxes. In the broader context of a deal with government that includes a commitment to specific development targets, the government should:

> **Devolve stamp duty on the same model as the government's recent devolution of business rates to local authorities, allowing London to retain a substantial proportion of its stamp duty income, in return for an equivalent reduction in grants from central government, and to adjust stamp duty rates in consultation with the business community, such as via the London Chamber of Commerce and Industry and London First.**

Boroughs should also be able to set higher council taxes for empty homes and second homes, in order to maximise the number of homes that are being lived in and to fund related public services, such as housing and homelessness support.

> **Boroughs should be free to change council tax premiums on empty properties and second homes.**

In the long term, London must have more responsibility for raising its own capital expenditure through fiscal devolution. However, there remains a shortfall in the mayor's capital funding programme that should be urgently addressed.

> **To help meet its own target of delivering 1 million homes by 2020, the government should increase the capital subsidy to the mayor's housing covenant by at least £350 million per annum.**

Some of the government's national policies for increasing affordable housing are not well suited to the London market. The government should work with the mayor and boroughs to adjust them as necessary. In particular:

> **The government should not impose a Starter Homes quota as part of local authority affordable housing negotiations, but instead leave it to local discretion.**

> **The government should consider maintaining the Starter Homes 20 per cent market discount in perpetuity, or at a minimum extend the period for which the 20 per cent discount applies to at least 10 years.**

As well as ensuring that affordable homes are genuinely affordable, it is critical that social rented homes in the capital are not sold without being replaced, and that replacements are fully funded by government.

> **The extension of Right to Buy to housing association properties in London should be fully funded through general government revenue in order to allow for the full replacement of social rented homes. It should not be funded through the sale of high-value local authority homes.**

Those delivering affordable housing need to operate with a degree of certainty that their development plans will not be dramatically changed by shifts in public policy. Therefore:

The government should conduct an independent evaluation of the impact of social rent reductions on both household incomes and housing supply, and move towards greater flexibility on rent-setting when the four-year rent cut period concludes.

If the government will not offer more flexibility in rent-setting, it should commit to a long-term rent settlement of at least 10 years, to provide some stability.

Accelerating delivery

The government should help boroughs to provide both support and incentives to speed up the delivery of housing – especially on sites where planning permission has been granted. To support this objective, the government should:

Devolve responsibility for London's share of the Large Sites Infrastructure Programme, allowing London to use the resources to support stalled sites and fund regeneration.

Allow the boroughs to levy, at their discretion, council tax on developers who have failed to meet agreed building targets.

Addressing construction capacity

Key to increasing delivery is to ensure that the construction industry has the labour power it needs. With an estimated 400,000 construction workers set to retire over the next five to 10 years, London needs to grow its skilled housebuilding workforce.

As and when adult skills funding is devolved to London, the mayor should use these new powers to ensure that a central component of the adult skills programme will be devoted to increasing the number of skilled workers for the construction sector.

Improving the private rented sector

The secretary of state should make minor changes to the regulation of the private rented sector, to allow for landlord licensing to be introduced across the capital and a guarantee of housing quality in the growing rental market. The secretary of state for DCLG should therefore:

Allow boroughs to:

- **create their own licensing schemes for private landlords**
- **apply a condition that no property failing to meet the Decent Homes standard should be able to be let from 2025**
- **use licensing fee discounts and, where appropriate, licensing conditions to drive longer tenancies in their areas.**

The ultimate goal should be to achieve London-wide coverage by 2025 under a single, simple London-wide rental licence.

Finally, the government, GLA and boroughs will need to work together to improve affordability in the private rented sector. Building more private and affordable homes will help to reduce pressure on household budgets in the long run, but steps are needed in the short term to address immediate concerns. For too many years rents have been increasing out of step with rent subsidies, creating an acute affordability pressure on some London households as housing benefit increasingly fails to meet the costs of rent.

The government should relink local housing allowance to local rent levels to ensure that low-income households can continue to rent in the capital.

Laying the foundations for a devolution deal: what the mayor and boroughs can do right now

The next mayor can and must make a start. Even if central government does not rapidly give London the extra powers described above, there is much the mayor and boroughs can do right now to address the housing crisis and to prepare the ground for a future devolution deal.

The first priority must be to establish the joint London Housing Committee, made up of the mayor's office and the 33 London boroughs, to establish joint-working arrangements, to put together a clear and coherent strategy for delivering the homes that London needs, and to present an offer to government to demonstrate their commitment.

Identify more land

There is an urgent need to increase the supply of land in the capital. Our research finds that the London Plan only identifies land for 425,000 of the 490,000 homes London needs – meaning a shortfall of 65,000 homes over the period to 2025. By the end of the first year of the new mayoral term, the mayor and boroughs must collectively have filled in the housing land shortfall in the London Plan. To do this, the following steps will need to be taken:

The London Land Commission should be given permanent status and resources to identify all brownfield land opportunities in London, private and public.

The mayor, working with outer London boroughs, should review the scope for housing development on greenbelt land near public transport sites, in exchange for offering improved community amenities and greenbelt protections in other places.

The mayor should create an enhanced and multidisciplinary 'placemaking team' within the GLA, with expertise in planning, design, finance and delivery. Its key tasks should be (1) to offer its technical expertise to TfL to review the potential for increasing housing density around key transport sites across London; and (2) to revise London's policy on housing density in order to encourage better densification and to avoid the creation of new developments that are too dense for local infrastructure to cope.

Boroughs should support communities to conduct their own neighbourhood planning locally, to identify both small sites for development and opportunities for regeneration.

We estimate that, taken together, these measures will be able to provide sites and capacity for at least a further 6,500 new homes each year – sufficient to close the gap between land currently identified for the London plan, and the need for 50,000 homes a year.

Turn land into homes

We have also identified that the majority of sites currently in the London Plan are large, and larger sites tend to be more difficult to turn into homes. From May 2016:

> **The boroughs should publish an annual audit of the progress of planning applications in their area, and of the progress of large sites in particular.**

> **Sites needing support should be offered planning assistance from the mayor's new placemaking team, and support in applying for city and national funding programmes where financing is an issue.**

For public land without a clear plan for getting it back into use or turning it into homes:

> **The mayor should offer public landowners the support of the London Development Panel to turn public land sites into new homes, on condition that a proportion of the public land is used for new affordable housing and privately rented housing (for a limited period of time).**

Where the landowner wishes to retain a stake in the development, the land should be brought forward through joint venture partnerships with housing associations or private developers, with the public landowner keeping either an equity stake or some portion of the resulting rental income from the development.

> **Where appropriate for the site, or if a developer cannot be found, the combined resources of the mayor and boroughs should be used to directly commission housing on sites through housing associations and private developers.**

There are also a number of measures London can take to support certain sections of the London housing market to maximise their output. Throughout the next mayoral term:

> **A proportion of small publicly owned sites should be offered to smaller developers for first refusal, at no initial charge. The public landowner should take a stake in the sale of rental value of the homes created.**

The mayor's London Housing Bank should be available to boroughs to finance the infrastructure required to prepare small sites for smaller developers.

Increasing the capacity of housebuilders, whether public or private, can only be achieved with the necessary supply of skilled workers. With an estimated 400,000 construction workers set to retire over the next five to 10 years, London needs to grow its skilled housebuilding workforce.

As and when adult skills funding is devolved to London, the mayor should use these new powers to ensure that a central component of the adult skills programme will be devoted to increasing the number of skilled workers for the construction sector.

Improve planning

The greatest improvement in planning outcomes will follow the additional resources that would come from allowing boroughs more flexibility over the setting of planning fees. Nonetheless, there are improvements that can be made in the meantime in order to ensure that local plans are up to date, and that planning departments can prioritise their work effectively. By the end of 2016:

The London Housing Committee should establish a London planning inspectorate, charged with supporting and monitoring borough planning departments.

The boroughs should publish an annual review of their progress against national and local targets for housing delivery and planning performance.

Provide more affordable homes

The provision of affordable homes is central to the ongoing vibrancy and economic success of the capital. However, the capital is currently providing only 60 per cent of the affordable housing that it needs. The additional land identified by the mayor and boroughs will be critical to unlocking more development from both private housebuilders and housing associations. Thus by the end of their first year in office:

The mayor and boroughs should offer London's housing associations a deal to double their building by 2020 in exchange for a major increase in land opportunities.

However, offering land on its own will not be enough to close the gap between the 25,000 affordable homes London needs and the 15,000 we built last year. London needs more investment: it cannot rely only on affordable housing contributions from developers and the current capital budget of £550 million. It will be necessary to seek out other sources of funds, such as:

The mayor and boroughs should work with pooled public-sector pension funds to identify investment opportunities in building new homes.

The mayor can also support the boroughs to secure affordable housing as part of private developments, in particular through the careful application of a fixed planning requirement to deliver affordable homes.

The mayor should immediately issue London-wide guidance on negotiating affordable housing with developers, and commit not to call in planning applications that demand a specified proportion of affordable housing.

Providing London-wide guidance and a degree of certainty over appeals will help to improve the negotiation process. However, the next mayor and boroughs could go much further to add certainty to the system by removing the negotiable element of affordable housing contributions in the planning system altogether:

The GLA and boroughs should begin consultation on simplifying affordable housing contributions through a 'tariff' system of fixed developer contributions to affordable housing.

This could simplify the process of agreeing affordable housing contributions and speed up the agreement of planning applications. The GLA and boroughs should work together to determine the level of the tariff, and use borough plans to estimate the viability of the tariff in different areas. The consultation on the tariff must ensure that its introduction would not have the effect of reducing overall levels of housing supply or affordable housing supply.

The tariff could differ by travel zones, or between inner and outer London, to recognise differences in land values. The default position of the tariff could be that homes are delivered on site, or at least within the borough where this is not possible.

At the point a tariff is launched, boroughs could identify any exceptional sites or areas that they consider to require a higher tariff. Where a developer believes that a site cannot viably be developed if the London-wide tariff is imposed, they should be able to appeal to the GLA for exceptional permission, but only with the backing of the relevant borough. An expert team should be established within the GLA to consider such appeals. Large sites that are not viable under any tariff should be given housing zone status.

If it is introduced, the tariff should be reviewed after several years to assess risks and effectiveness.

Improve substandard rented homes

Government reforms to improve enforcement of standards in the private rented sector are welcome, but with one in three homes not meeting modern standards of decency, and tenancies increasingly likely to be short, more action is needed to help the boroughs guarantee a higher degree of quality, transparency and stability in the sector. Therefore:

The mayor should launch a London lettings hub to link up tenants directly with good-quality, accredited landlords.

The hub should offer discounted fees to landlords offering longer-term tenancies, and tenants should be able to search the online platform for properties by tenancy length.

It should also allow tenants to leave feedback on the quality of properties and property management, and provide borough data on enforcement activity to highlight problem properties and landlords to prospective tenants.

Addressing London's housing crisis, collectively

Confronting the London housing crisis will not be easy. Getting delivery moving and affordability back on track will demand not one measure but many, across land, planning, investment and developer capacity.

But it is in our mutual interests to act together – the next mayor, boroughs and the government all have a stake in securing London's economic success and maintaining its social fabric. The changes we have outlined, large and small, to how homes are delivered in the capital can help each layer of government to work towards our shared objective of seeing more good-quality, affordable homes of all tenures for households across London.

2.
LONDON'S HOUSING CRISIS

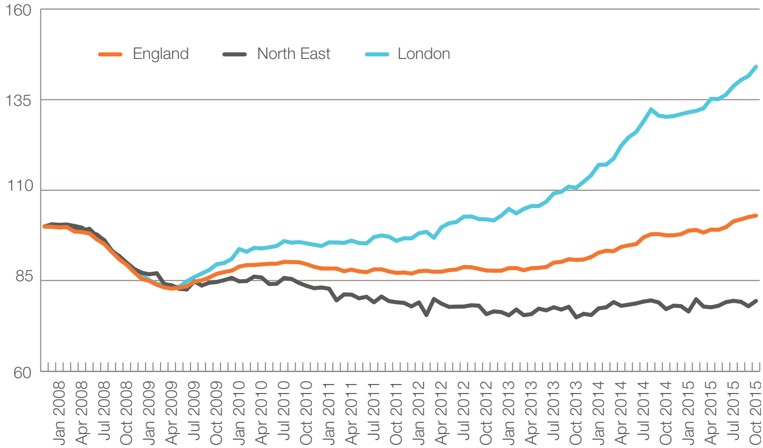
London is suffering from an urgent lack of good-quality, affordable homes. The average Londoner may not notice the difference between a supply of 10,000 new homes a year or 50,000 a year. What they do notice, however, is the unaffordability of housing, whether in the struggle of trying to buy a house or find somewhere to rent, in the size and quality of what they can get for their money, or in the number of homeless people they see on London's streets. Principally, the London housing crisis is a crisis of affordability, and one that will only get worse without concerted action.

London is expensive and the cost of a home is rising quickly

London's housing situation is different to the rest of the UK. As far back as the data takes us, London has always been, relatively, an expensive place to live. It is a vibrant, attractive place that creates a significant proportion of all UK wealth, and offers current and prospective residents a plentiful supply of job opportunities. However, the cost of making a home in London has never been as high as it is today, and demand for the homes it has is greater than in any other region of the country.

Average house prices in London were recently recorded at £525,000 in Land Registry data (Land Registry 2015), and while buying a home in London has consistently been more expensive than other parts of England, the data shows that the London market is moving at a very different speed to other parts of the country. For instance, average prices in the capital are now some 50 per cent higher than at their pre-crisis peak, compared to the North East, where losses since the financial crisis have barely been recouped, nearly a decade on.

Figure 2.1
House prices have recovered from the financial crisis more quickly in London than anywhere else in the UK
House price inflation since pre-crash peak (index 100 = November 2007 prices)



Source: Land Registry 2016

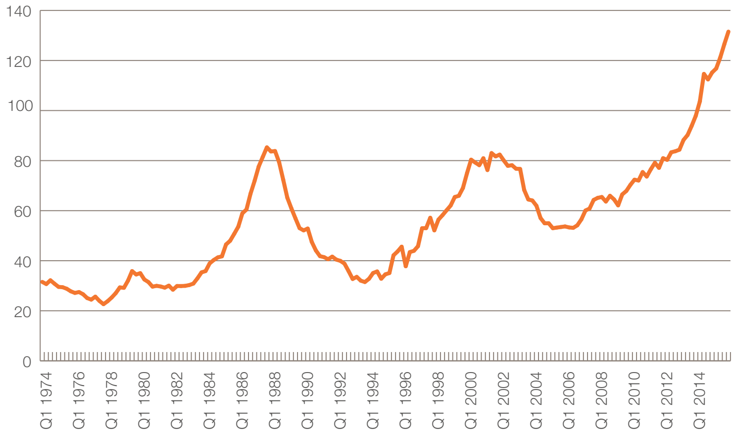
Equally, the gap between average house prices in London and in other parts of the UK has never been so wide. As figure 2.2 shows in proportional terms, the average price of a London property is racing away from the UK average: in 1973, the average London house was just a third more expensive than the national average; by 2015, this had ballooned to almost two-and-a-half times.

The effect of this surge in house prices has been compounded by wages, which over recent years have failed to keep pace. As figure 2.3 shows, the ratio of house prices to earnings in London is now higher than at any point in the last three decades.

Figure 2.2

Average London prices are outstripping national average prices by a record margin

Additional cost of average London prices compared to national average prices (%), 1973–2015

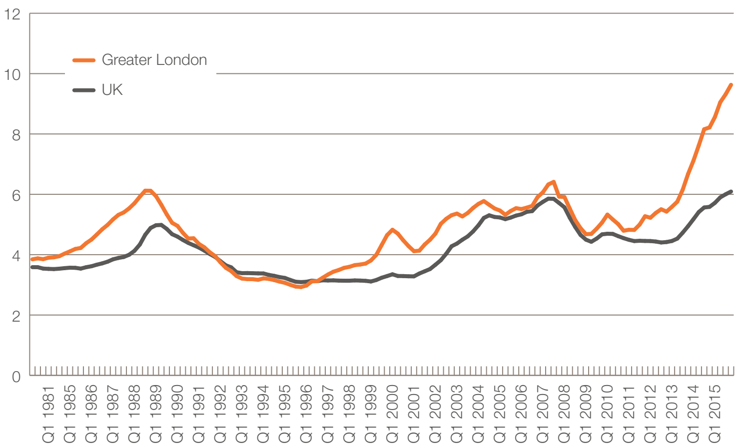


Source: Nationwide 2015

Figure 2.3

The average London house price is now nearly 10 times median earnings

Ratio of house prices to median male full-time earnings, 1983–2015



Source: Halifax 2016

Rising prices appear to be hitting levels of owner-occupation. Despite the government's commitment to stemming the fall in homeownership, the share of households who own their own home fell some 12 percentage points in the last decade alone (DCLG 2015a). This is hardly surprising: for first-time buyers, the average deposit in the capital is now around £74,000 (Hudson 2015a), and is feeding pessimism about future ownership prospects, particularly among younger groups. A recent survey found that 82 per cent of 20–45-year-olds felt that they would never be able to afford to own their own home (Halifax 2015).

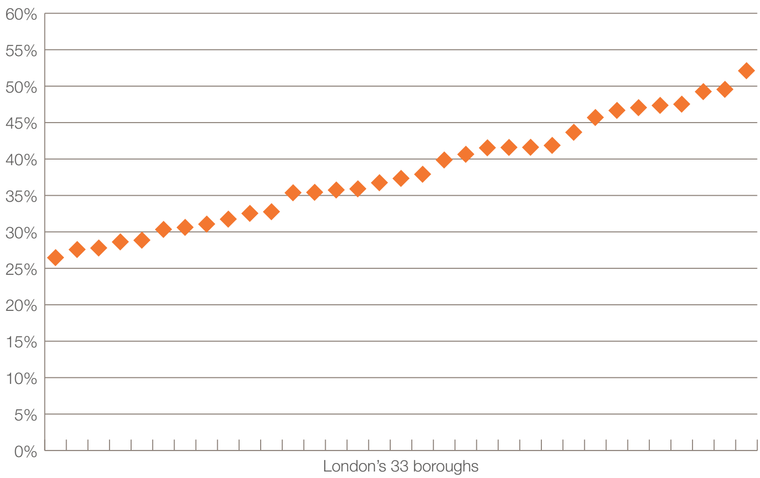
The rental market is growing, and with it rents are rising too

As fewer people become homeowners, pressure is growing in the rental market, stoking an affordability crisis for renters. The number of households renting privately in London has doubled in less than a decade (CLG 2015a), and households are spending longer renting, as other housing options are closed off. This is compounding pressure on a sector already subject to overcrowding (LPP 2015), and in which rents are already double the English average: the median rental cost of a property in London is now £1,400 a month – or £16,800 per year (VOA 2015).

The gap between what people earn and what they pay in rent has been narrowing in the past five years. While rents have traditionally tracked earnings more closely than house prices, this relationship appears to be changing in the capital: since 2011, London wages have increased by 2 per cent but rents are up by 16 per cent (ONS 2015).

The costs of renting in the capital compare unfavourably to the rest of England: in 2013 median London rents were 40 per cent of median monthly household incomes, compared with the second most unaffordable region – the South West – where median monthly rents were 26 per cent of household incomes (VOA 2013, GLA 2015a). Although the cost of renting varies widely across London, rents are now more than one-third of household incomes in 27 of 33 boroughs. In Bexley (where median rent is around £950 per month) affordability is much less of a constraint than it is in either Kensington and Chelsea or Westminster, where median rents are around £2,300 per month and the least affordable in London, by the standard of incomes in either borough (VOA 2015).

Figure 2.4
In 2013 rents were between one-quarter and half of income across London's 33 boroughs
Median rents as a percentage of gross median household incomes, by borough, 2013



Sources: GLA 2015a, VOA 2013

While people are clearly willing to pay more for their housing In London, it is less clear that it is economically or socially desirable that such a high proportion of income should be spent on accommodation costs. In any case, the high cost of housing in the capital has a slew of undesirable social and economic effects.

Rising housing costs are driving up poverty and hurting living standards

Families do not have a choice about whether they 'consume' housing or not, and therefore the amount they pay for their homes directly impacts on the amount of money they have for other purchases, such as food, clothing and travel.

Research by the New Policy Institute (NPI) shows that while London has the highest average pay in the country, once housing costs are accounted for, it also has the highest rates of poverty nationally (Aldridge et al 2015). Table 2.1 shows how dramatic this impact is: while London's household poverty rates are roughly equal to England's before housing costs, once these are accounted for, more than a quarter of London's working-age households are in poverty – that is, as a result of their housing costs.

Table 2.1
Percentage of working-age households living in poverty, before and after housing costs, 2011/12–2013/14

	England	London
Before housing costs	15%	15%
After housing costs	21%	27%

Source: Aldridge et al 2015

On this point, the NPI concludes that 'the extent of this problem seems to be getting worse rather than better and there appears to be no progress' (ibid 2015).

In the short term at least, these problems are likely to get worse. Reforms to welfare, and in particular to housing benefit (which is intended to support rental costs in both social and private housing), are yet to feed through fully into the data. So over the coming years, successive rounds of poverty indicators are likely to markedly worsen.

Income lost to housing has a significant impact on living standards. While various poverty-based measures of affordability suggest a household should not be spending more than one-third of its income on housing costs, recent analysis by the Resolution Foundation has identified that a quarter of households in the private rented sector are spending more than half of their income on their rent (Resolution Foundation 2016).

As households struggle to meet the growing costs of housing, many compensate by living in shared accommodation, and in an increasing number of cases, living in overcrowded accommodation.[2] The NPI estimates that, in 2012/13, there were around 250,000 overcrowded households in London. In particular, overcrowding has risen most sharply in the private rented sector, where some 13 per cent of households live in overcrowded accommodation, roughly three times higher than the English average for private renting (LPP 2015). Overcrowding is also high in the social sector, where the problem affects 14 per cent of social renting households, compared to 5 per cent across England (ibid).

Homelessness is rising, as is the number of people living in temporary accommodation

Amid a shortage of housing and rising accommodation costs, data also shows that homelessness is rising again – there are now around 7,500 individuals rough-sleeping, up by around 3,500 since 2010, and 5,000 since 2005 (Aldridge et al 2015). It is evident that those with limited access to public funds are particularly struggling, as non-UK nationals account for around half of these figures (ibid).

The official figures also show alarming trends. In the capital, the number of households going to their local authority to register as homeless is around twice the English average (five per 1,000 households, compared to 2.5 per 1,000 across England), and that the number of homeless households is rising again to levels last seen a decade ago, in 2006 (DCLG 2015b).

There are also around 49,000 households living in temporary accommodation (DCLG 2015c), among which there are around 78,000 children, despite the often dire, cramped and inappropriate conditions associated with hostels, B&Bs and the worst corners of the private rented sector (see Rose and Davies 2014). Despite these poor conditions, however, the cost of keeping families in emergency housing is substantial. The most recent estimates suggest that London boroughs collectively spent around £650 million over the four years to

2 That is, according to the Housing Act 1985, 'wherever there are so many people in a house that any two or more of those persons, being 10 or more years old, and of opposite sexes, not being persons living together as husband and wife, have to sleep in the same room'.

2014; Westminster alone spent more than 10 times what Leeds spent over the same period (Twinch 2014).

In addition to these social concerns, there is also an economic imperative to fixing London's housing crisis.

The capital provides both jobs and taxes that the UK needs

London is central to the UK's economic success. Research by the Greater London Authority (GLA) has shown that typically when London does economically well, the rest of the UK does, and vice versa (GLA 2014a). While economic growth has occurred in every region of the UK over the past decade, London's contribution to the UK's economy is around 50 per cent higher than the next biggest region, the South East, and gross value-added (GVA) growth in London has been 20–25 percentage points higher than any other region of the UK (Cox and Raikes 2014).

Figure 2.5
Economic growth in London is roughly 50 per cent greater than in any other UK region
GVA, 2002 vs 2012 (left) and percentage change (right), by region

Source: Cox and Raikes 2014

The capital's reach beyond the boundaries of the GLA is important: around 870,000 people work in London but live outside its boundaries, predominantly in the south east of England (McKinsey 2015).

London's success is also a cornerstone of the UK's tax base, which is vital both to fund UK public services and enable the redistribution of resources to weaker economic areas. A report by McKinsey estimates that London's average net tax contribution was around £12.7 billion a year over the decade to 2015 (ibid).

The housing market in particular provides a significant fiscal contribution via property taxes. London contributes around one-third of total UK stamp duty revenues, and despite claiming only around one-tenth of all homes, it contributes around one in every £4 of property tax raised. Indeed, the borough of Westminster alone is responsible for around 6.5 per cent of England's whole residential stamp duty receipts (HMRC 2015).

Failing to fix the housing market threatens UK stability and London's growth

While a more geographically balanced economy and tax base is desirable in the long term, in order to spread wealth and opportunity more equally around the country, we need at the same time to fix the London housing market to ensure that London continues to grow its economy too.

A failure to do so poses significant risks to London's capacity to grow, and to the wider UK economy. Both the European Commission and the IMF have issued warnings about the threat of house price inflation to London's economy (see Chan 2014, BBC 2014). Estimates from the University of Reading has suggest that 'the likely loss of employment arising from housing shortages [means] £1 billion will be lost in potential extra economic output from professional workers in the London economy' (Ball 2013).

Business representatives have also been pressing for urgent action on supply and affordability. In their response to the commission's call for evidence,[3] the CBI noted:

> *'The lack of housing supply poses a growing challenge to London's pre-eminence domestically and abroad as a destination for top talent. More than three-quarters of CBI/CBRE survey respondents do not believe that the current mayor's target of 42,000 homes built per year will be met. Without a significant change to the status quo, there will be a continued drain on London's workforce as the affordability gap between incomes and housing prices widens further.'*
> CBI 2015

The London Chamber of Commerce and Industry (LCCI) has also warned of the threats to London's competiveness from a failure to tackle the housing crisis, highlighting concerns across recruitment, productivity and punctuality linked to lengthy commuting times, and rising pressure on employers to increase wages in line with spiraling housing costs (LCCI 2014).

All the while, the costs of inaction are adding up. Until recently, the government has been largely willing to bear a large share of the costs that fall on employees (and the unemployed) through housing benefit transfers, which in the capital cost an estimated £6.5 billion a year – this is equivalent to around 25 per cent of England's total housing benefit expenditure, despite London having only 16 per cent of England's claimants (DWP 2016). While this is not a new phenomenon, improving employment levels have not drastically cut the number of claimants – in 2010 only 17 per cent of London's housing benefit claimants were in work; by 2015 the proportion was as high as 33 per cent (ibid).

Left alone, the London housing crisis will only get worse

Without urgent action from the government, the mayor and the boroughs, there is a little to suggest that the crisis in the capital will fix itself.

3 See LHC 2015a.

House prices will continue to rise. Forecasts by Savills show house prices rising by 15.3 per cent by 2020 (Savills 2016), which would put the average price of a property in the capital at £605,000, outpacing inflation and wage projections throughout the next mayor's term. Estimates by PwC put 2020 prices at an even higher level, at an average of £670,000 (PwC 2015), with average prices equivalent to 14.5 times average full-time household earnings.[4]

This inexorable rise is down to four crucial factors. First, without intervention, housebuilding and property conversions will likely continue at around 25,000 a year, which is around half of the volume needed in the capital to keep pace with growing demand (DCLG 2015d).

Second, the mix of people who are buying houses is changing, which in turn changes the dynamics of housing costs. While first-time buyers are struggling, they are being replaced in the market by growing numbers of buy-to-let investors and investors from overseas seeking a safe haven, at a time when other investments are making weaker returns, and amid uncertainty in major economies in Europe and the far east.

Third, while lending has largely recovered in the London housing market, interest rates remain at record low levels. When these rise, house price inflation may slow, but this will not improve affordability among current owner occupiers. At the same time, the growing number of buy-to-let landlords in the capital may simply choose to pass on these rate rises to tenants chasing a scarce number of rental homes, exacerbating pressures in the renting sector.

Fourth, even in the event that London's house prices do 'correct' in the coming years, the correction is unlikely to produce a lengthy period of greater affordability. In the last downturn, house prices fell by some 19 per cent at first, only to return to their pre-crisis peak within 18 months – and since reaching these pre-crisis levels have continued to rise by some 10 per cent a year (Land Registry 2016).

4 Over the same period, the OBR projects average incomes across the UK to rise by roughly 6 per cent (OBR 2015).

The only part of London's housing stock that is somewhat insulated from these pressures – affordable housing, such as social rented homes – cannot take the strain of what is demanded of it, and therefore a growing number of people will be competing for whatever private rents are available once other options are exhausted.

There is no alternative to building more homes

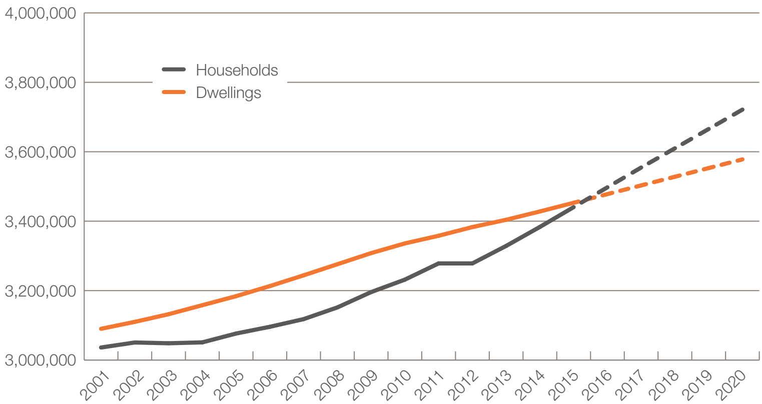
The fix for London's housing crisis is complex, and must target problems across housing, planning, tax and investment policies. Nonetheless, the first priority for the next mayor is 'simply' to build more houses.

The capital has long failed to build enough homes for its growing population, but as a submission from the Highbury Group showed, for the first time in recent records, the total number of households living in London will exceed the total number of homes by 2017, as figure 2.6 shows.

Figure 2.6

The number of households living in London is set to exceed the number of homes in London for the first time in 2017

Total households vs total number of homes, 2001–2020 (actual and forecast)



Source: Highbury Group 2015

Simply looking to reallocate where people live in the capital will not solve the problem. The English Housing Survey shows that of all regions, London's housing is used the most efficiently[5] (DCLG 2015a). As we have noted already, a growing proportion of homes are overcrowded and thus a growing proportion of London homes are being 'overconsumed'.

Nor are there enough empty homes to address housing supply issues. Compared to the total number of homes in each region, London has the smallest proportion of homes left empty (see Davies 2014), and there are simply too few empty properties in the capital to make a major difference. In 2015 there were only 21,000 long-term empty homes in London, against an annual need of at least 50,000 new homes (DCLG 2015e).

For London's crisis to be solved, fundamentals must change

The housing crisis in London has been a long time in the making and will take a long time to turn around. Building up momentum on new supply, through changes to public policy and the broader framework through which homes are delivered, will take time to bear fruit – and any resulting gains would not change the relative attractiveness and therefore cost of London as a place to live.

However, the crisis has now reached unprecedented levels across a range of measures. More worryingly, there are signs that London's housing dilemma is not cyclical – that is, that a correction in the cycle of the housing market or wider economy may to do little to address the crisis of affordability in the capital. Rather, London – and UK public policy more widely – has built up a problem in the capital's housing market over decades of imbalanced economic growth and undersupply of new homes.

Without major action to address some of the fundamentals driving London's housing problems, the risks to households – poverty, overcrowding, overexposure to the debt, and

5 In terms of matching the number of people to the number of bedrooms.

homelessness – will only continue to grow, and with them the economic risks to the health and stability of the capital and national economies. The following chapters, therefore, explore the challenges of confronting the London housing crisis, across crucial issues of housing supply, housing affordability, and London's growing private rented sector.

3. WHY IS LONDON NOT DELIVERING THE HOMES THAT IT NEEDS?

Tackling the housing crisis in London needs first to focus on the supply of new homes. While 'building more' will not by itself address every issue in the capital's housing market, failing to do so will only make addressing the deeper problems of affordability and housing quality more difficult in the future.

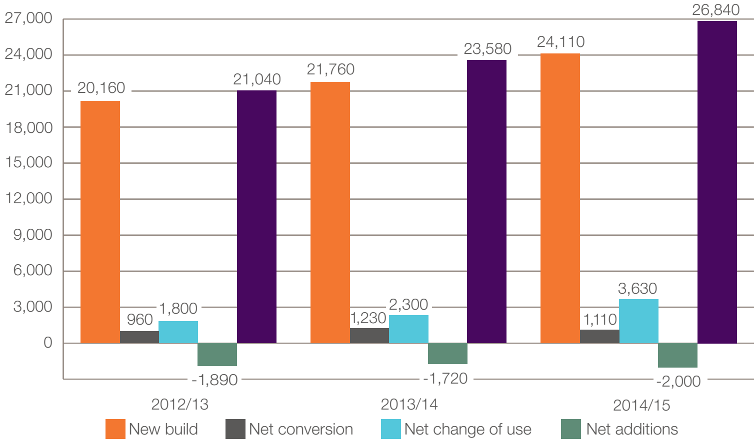
The scale of housing demand in the capital is significant. The mayor's review of housing need, the Strategic Housing Market Assessment, estimates a minimum need for 48,841 (for the purposes of this report, rounded to 50,000) new homes a year simply to keep up with London's population growth and backlog of need, or up to 62,000 homes a year in order to clear the backlog more quickly (GLA 2013a).[6]

Measured against these targets, London is falling well short, delivering an average of around 20,000 new dwellings a year over the last decade. While building has grown in more recent years, it remains far below the levels required: taken together, total new supply in 2015 was roughly 27,000 homes – including 24,000 new-build homes, 1,000 conversions and 3,500 changes of use – which is still 22,000 homes short even of the mayor's lower target.

There are multiple factors preventing development from proceeding; if these could be unlocked, housing supply could be increased significantly. These factors include land availability and disposal, planning resources and powers, investment constraints, and development sector capacity. In this chapter, we will address each of these constraints in turn.

6 See chapter 4 for a more detailed discussion of the nature of this housing demand.

Figure 3.1
Total new housing supply (net additions) has increased slightly in recent years but lags far behind the mayor's targets
Components of net new supply, London, 2012/13–2014/15



Source: DCLG 2015f

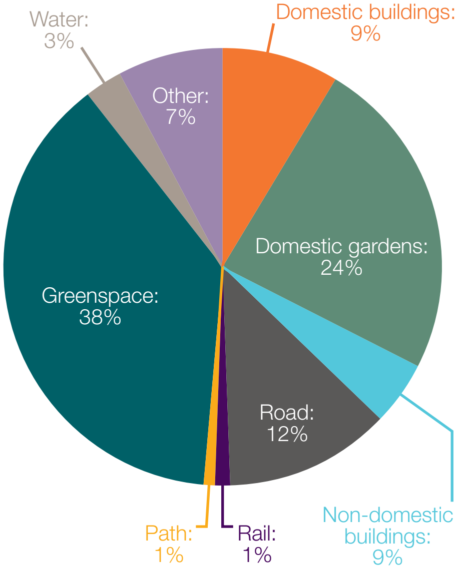
Land: availability, cost and use

There is not enough land in the London Plan

The lack of availability of developable land is a primary constraint on new housing supply in London. While its use of land for homes is perhaps the most efficient in the country, only 9 per cent of London's total land area is used for housing its citizens, as figure 3.2 shows.

The London Plan and the borough plans determine what land is in scope for development over the plan period (2015–2025), via the mayor's Strategic Housing Land Availability Assessment. The assessment currently identifies land enough for nearly 424,000 new homes, predominantly through large sites.

Figure 3.2
Only 9 per cent of London's land is used for homes (domestic buildings)
Components of London's land use, 2005



Source: GLA 2014b

The land assessment illustrates a critical constraint on delivering the homes that London needs. First and foremost, the plan does not identify enough land to keep pace with London's population growth: in order to deliver 490,000 new homes over the next decade, the boroughs and mayor will collectively need to find sites for at least 65,000 homes on top of what has already been earmarked. If we are going to tackle the housing supply problem, there needs to be a hierarchy for how we allocate land in the capital, and within this hierarchy land for housing must be prioritised.

Table 3.1
Potential for homes on land identified within London (2015–2025)

	Large site capacity	Small site capacity	Capacity from long-term vacants	Student non-self-contained accommodation pipeline	Total
Total dwellings	290,244	106,476	7,550	19,617	**423,887**
Proportion of total	68%	25%	2%	5%	**100%**
Estimated housing requirement					**488,410**
London Plan land as a percentage of requirement					**87%**
Shortfall in capacity					**64,523**

Source: GLA 2013b

The London Plan relies too heavily on large sites

The second challenge is that 68 per cent of the land identified for housing consists of 'large sites'. While small sites can and usually are delivered quickly, large sites are much harder to develop: they are often more complex, requiring significant upfront investment in infrastructure (such as transport, water, electricity and broadband) and possibly additional preparation of the land to ensure it is fit for housing. The resources and time required can mean that major sites can take years if not decades to come to fruition. One review for the mayor explained that:

> *'[Planned sites] with capacity of more than 500 units per site are misleading. Very, very few schemes commence over 500 units in any five-year period. This is because selling more than 100 units per year is very difficult.'*
> Molior 2014

In spite of this problem, the commission heard evidence of an institutional bias in favour of larger sites. Because (as is discussed in more detail below) the resources of local planners, valuers and surveyors are so thinly stretched, local authorities have focused their housing plans on the larger sites that make it easier to reach the number of homes required in their local plans, thus overlooking the smaller sites that are so vital to actually delivering new homes quickly (and to supporting smaller developers) (LSE 2016).

> To unblock development on large sites, the GLA should offer planning and technical support to landowners, and assist struggling sites to access public funding, such as the Large Site Infrastructure Programme.[7]

There is also a significant opportunity to use the Neighbourhood Planning[8] initiative to bring a greater number of smaller development opportunities into the scope of local plans. Small sums could be provided by boroughs to support this process, on the basis of future New Homes Bonus receipts.[9]

> Boroughs should support communities to conduct their own neighbourhood planning to identify new opportunities for regeneration opportunities and small sites not currently in the London Plan.

Land use restrictions prevent new land coming to market

The third is that public policy constrains – often for sensible reasons – land availability and capacity in a number of ways.

The first such constraint concerns potential sites that are excluded from the scope of local plans on account of their designation as industrial, greenbelt or 'metropolitan open land'.

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7 The Large Sites Infrastructure Programme is a national programme to provide capital funding and other support to help unlock and accelerate large-scale housing development.

8 Neighbourhood Planning is a tool introduced by the 2011 Localism Act that enables communities to identify and shape development opportunities in their area, in addition to those already idenitified in wider local plans.

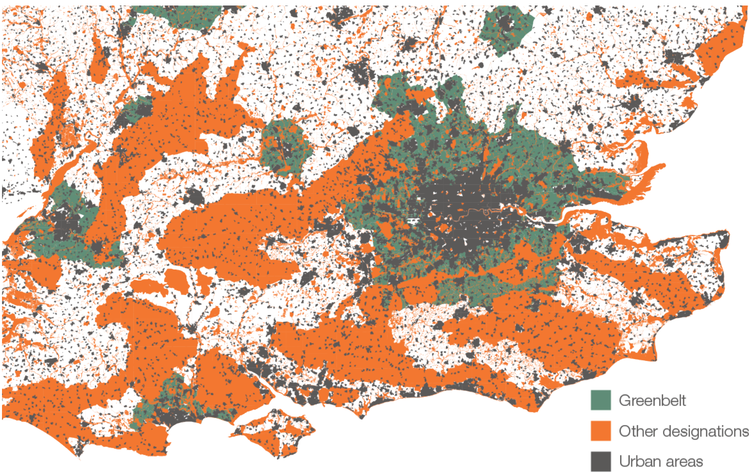
9 The New Homes Bonus is an incentive for local authorities to agree new housing developments by paying a fee from central government to local government for every new home built in their area.

Together, these designations cover a substantial amount of potentially developable land:

> *'[DCLG data] indicates that ~11 per cent of England is developed. In terms of land with development constraints: ~13 per cent is covered by Green Belt while National Parks, Areas of Outstanding Natural Beauty and Sites of Special Scientific Interest cover 29 per cent. Adding them together while allowing for overlaps indicates that ~40 per cent of England is covered by these restrictions.'*
>
> Hudson 2015b

The impact of these restrictions is particularly clear when mapped across London and the greater south east.

Figure 3.3
Much of the south east of England is covered by restrictive designations, including greenbelt
Land designation in the south east of England



Source: Hudson 2015b

Estimates suggest that using only 1 per cent of greenbelt land within the greater London borders could release enough land to make up a quarter of the capacity shortfall in the London Plan. Building homes at average densities on this 1 per cent could provide 17,500 homes over the decade covered by the plan (IPPR analysis based on DCLG 2015j).

> Working with outer London boroughs, the mayor should review the scope for housing development on greenbelt land near public transport sites. Any new greenbelt developments should be brought forward in exchange for a commitment to providing improved community amenities and potentially extending greenbelt protections in other areas.

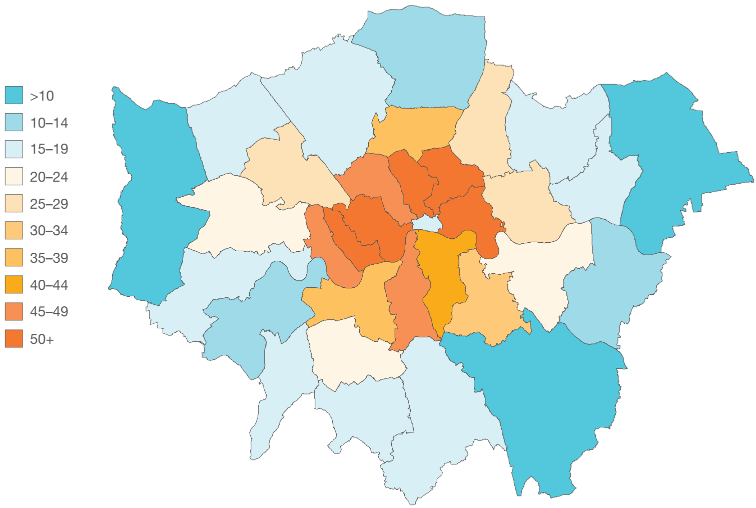
The second policy constraint applies after sites have been identified for development, by limiting the number of homes that can be built, according to density and other restrictions. The density of developments is constrained through planning guidance, which sets guideline densities for different neighbourhood types (central, urban, and suburban) based on a planned site's location and its proximity to public transport networks.

In theory this guidance should constrain the density of developments, but it is not clear that this guidance is being rigidly applied. GLA data shows that the majority of developments are exceeding current density guidelines, and that only around 7 per cent of developments fall below the intended density levels. In inner London, 5 per cent of all approved developments had densities below the desired range, compared to 10 per cent in outer London boroughs (GLA 2015d).

However, increasing density further on land already captured by the London Plan is not necessarily desirable: while the mayor's review of land availability suggests that increasing density could deliver the additional 65,000 homes needed (GLA 2013b), this brings the risk of a significant number of undesirable developments and the overburdening of local infrastructure, such as transport.

Instead, higher densities might better be achieved in locations that are not currently in the London Plan, but are nevertheless relatively low-density – that is, on sites currently not in scope but at lower-than-optimum densities. A number of recent reports have identified that densification of low-density areas could unlock significant additional housing development across the capital, if the scope of the London Plan were to be widened, for instance to low-density town centres with good transport links (London First 2015).

Figure 3.4
Housing density in outer London is roughly one-third what it is in inner London
Homes per hectare, 2014



Source: GLA 2015c

Equally, there are considerable opportunities to increase housing density in outer London, which has many areas predominated by low-rise semi-detached housing (HTA Design 2015). The population densities in outer London are around one-third those of inner London boroughs, and indeed densities in inner London have risen more quickly over the last decade than in outer London (LHC 2015b). Moreover, a number of reviews of density in London highlight that there are very different types of densification – in addition to high-rise, such as Victorian terraces or mansion blocks – that can deliver good-quality homes in different settings (Create Streets 2015, HTA Design 2015).

As well as focusing on a more holistic interpretation of density around key transport sites, more creative approaches to transport infrastructure that focus on mobility (such as walking and cycling) and access to key services may be necessary in higher density developments. Typically, the measures of infrastructure for developments focus on issues such as peak capacity of the road network and rail network, which is invariably more expensive to provide.

However, with higher densities come additional risks, and it is essential that density categories both recognise more sophisticated neighbourhood types – beyond the current central/inner/suburban distinctions – and also recognise and mitigate the risks to community infrastructure that higher density brings, such as pressures on transport and public services.

Therefore the mayor should issue new guidance alongside revised density matrices, setting out the planning conditions for amenities and green spaces that should come with higher density developments.

> The mayor should create an enhanced and multidisciplinary 'placemaking team' within the GLA, with expertise in planning, design, finance and delivery.

A specific opportunity identified by the Outer London Commission (OLC 2015) focuses on increasing housing density around current and future stations and adjacent land owned by TfL, locking in new development around key transport sites.

Therefore, as its first task:

> The new placemaking team should offer its technical expertise to TfL to review the potential for increasing housing density around key transport sites across London.

The second task of the new team should be to improve the current rules around density in the planning system:

> The GLA team should review and revise current density criteria to include broader density categories. These revised categories should be supplemented by new planning guidance around the additional community amenities and infrastructure requirements that will be expected of higher-density developments.

Public land is not being used to its full potential

Public land is a significant asset in the capital, and the London Land Commission (a body established to identify publicly owned development land) states that around a quarter of land across the GLA area is owned by public-sector bodies, and the London boroughs in particular (Sullivan 2016).

A substantial proportion of this land is already used for homes, in the form of local authority housing estates. In a recent piece of work for the Cabinet Office, Savills estimated that borough housing estates covered around 8,500 hectares across London, and that if 20 per cent of these sites were redeveloped to higher densities, an additional 54,000–360,000 homes could be built (Savills 2016b), depending on the density and design ultimately adopted. At the same time, the government is increasingly focused on regeneration as a way to meet a number of goals for housing supply and social policy, and has tasked Lord Heseltine with identifying a further 100 sites across the UK for development (DCLG 2016a). However, the regeneration of housing estates can take many years to achieve, because schemes are often complex and require the consent of residents, who may be opposed to the redevelopment of their homes.

> Communities should be supported by boroughs to develop neighbourhood plans to identify opportunities for regeneration in their area, in preference to a top-down approach.

In a wider review, the London Land Commission has identified enough public land to deliver around 130,000 new homes in the capital. Much of this land is currently operational and therefore unavailable for development. However, there are significant tracts of land owned by various bodies that are not in active use: some 2,200 non-operational sites within London's boundaries, including 19 non-operational Department of Health sites, a further 15 owned by NHS Trusts, and a further five owned by NHS Foundation Trusts (LLC 2016). Some of these sites will return to operation as the landowners' organisational needs change, but some will remain non-operational, and in many cases there will be no plans in place for their disposal. These perpetually non-operational sites could be released for housing development.

The National Audit Office (NAO) has highlighted that public bodies have been slow to dispose of public land, and that disposal has not automatically resulted in increased housing supply (NAO 2015). In particular, it highlights that:

> *'Departments do not routinely track what happens to a site after disposal. There has been no recording of development activity or housing starts and completions. The [Homes and Communities Agency] is not able to establish starts or completions as the programme did not require departments to provide this information to the HCA. Therefore we are not able to say how many homes have been built on the land. Evidence of actual homes built would take many years to identify: for larger sites, it may be up to 20 years before all homes are built.'*
> NAO 2015

A number of submissions to the London Housing Commission have highlighted that simply releasing public land will not, by itself, see homes being built. Instead, once the London Land Commission has completed its mapping of publicly owned land, the release of non-operational land needs to be linked directly to a clear strategy of housing development. For instance, the National Housing Federation comments that:

> *'The [London Land] Commission not only needs to ensure that all public landowners engage in the process, but also set out a coordinated strategy for land release that is explicitly linked to housing delivery. So, having annual targets not only on the land identified and released, but also targets for the number of homes delivered on these sites.'*
> NHF 2015

The NAO has illustrated a range of different options for releasing land from the public sector, including joint ventures, direct development, partnership approaches, and 'clawback' methods (see NAO 2015), and some public landowners in London have been proactive about bringing their land to market. Still, others have struggled, in part because of a lack of capacity and experience in dealing with the disposal or development of surplus land. The commission also heard that there may be an issue of local authorities using European procurement processes (OJEU) to dispose of their land, rather than simple land sales, which due to their complexity can take up to twice as long. Public landowners may therefore need additional support to manage these steps, so that the transformation of unused public land into new homes can be hastened.

> The London Land Commission should be given permanent status and resources to identify all brownfield land opportunities in London, private and public.

> On the basis of the results of the London Land Commission, public land that is not in use should be released to build new homes. Where there are no plans for bringing public sites back into use, the mayor should offer the public owners the support of the London Development Panel,[10] which would be tasked with finding a developer for the site.

Rising land prices discourage land release

A final constraint on land supply is the land market itself. The price of land is closely connected to house prices, and in a rising market there are few incentives for landowners to offload their landholdings today when they could benefit from significant capital growth tomorrow, and no tax disincentives to their holding onto it. In the last decade, residential land prices have closely mirrored house prices: having dropped sharply after the recession they recovered strongly such that, by March 2015, they were some 30 per cent above their pre-crisis peak (Savills 2015a). As Policy Network's submission to the commission makes clear, these rising prices undermine the viability of housing projects and limit competition in the sector by creating such large capital hurdles that only the largest developers can bid for a site (Policy Network 2015; see also HBF 2015).

10 The London Development Panel is responsible for finding developers for public land.

Summary: land

In summary, the constraints on London's land availability are four-fold:

1. There simply isn't enough land identified in the London Plan and borough plans.
2. The plan focuses too heavily on big sites to deliver the number of homes it needs.
3. Public policy restricts the amount of land that is available and the capacity of that land in order to restrict the development of schemes of types or in places that the government deems undesirable.
4. Perhaps most importantly, rapid increases in the value of land act as disincentives for landowners to release their land onto the market quickly.

The mayor's land assessment already includes 'the contribution of all currently identified brownfield sites, infill sites, redeveloped local authority stock and possible urban extensions' (HTA Design 2015). Given this account, then, it falls to the next mayor and boroughs to identify additional capacity for at least 65,000 more homes by bringing more land into scope and increasing density on existing and prospective sites. Finding additional land will require a collective effort within the GLA boundaries, but also a recognition that councils beyond the GLA boundary have a key role to play not only in increasing London's housing supply but also in managing it's affordability (Bramley 2016).

The next mayor will need to provide support, and in some cases actively intervene, to ensure that borough plans are capable of delivering the number of homes that London needs. As such, the government should transfer the following competencies to strengthen plan-making.

> The government should exempt London from the National Planning Policy Framework (NPPF), instead giving the mayor's London Plan the same status as the NPPF – and give the mayor the power to force boroughs to change their plans if they are not identifying enough land for housing.

There is a clear role for local authorities bordering the greater London area to work with both the mayor and outer London boroughs to tackle the shortfalls in housing delivery, land identification, and infrastructure needs across political boundaries, and this role should be enshrined in plan-making processes.

> Giving the London Plan the same status as the NPPF will mean that local authorities outside London have a duty to cooperate with the mayor to find land and build homes to help solve London's housing crisis.

Planning: conversion rates, capacity and performance

Planning is often cited as one of the main constraints on delivering homes across England, and in the capital (see for example Holman et al 2015). On the one hand, of course, planning is intended to be a constraint on housing supply, by ensuring that buildings are legally compliant and meet certain specifications and conditions for the area. However, there are a number of pinch points in the planning system that regularly featured in responses to the commission's call for evidence, including insufficient resources, the burden of negotiations around planning gain, and planning departments' limited ability to ensure applications would turn into actual homes.

There are too few new planning permissions

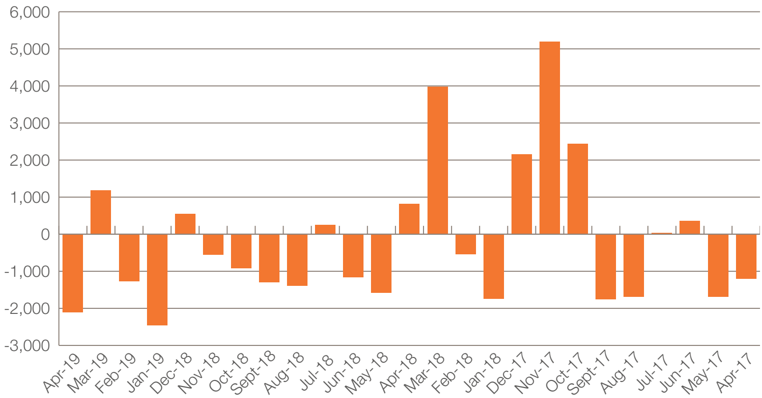
Figure 3.5, based on the London Development Database, shows the number of homes given planning approval in a given month since April 2013, compared to the number of residential approvals needed each month to build 50,000 homes (*if* all approvals turned into starts).

The number of approvals regularly falls short of this crude monthly target, which means that there are not enough planning applications going through the system on a regular basis to deliver the homes that London needs. Providing the capacity to deliver good-quality and efficient planning will be vital to getting housebuilding starts up to desired levels.

Not all planning permissions become homes

While the number of new consents is not keeping pace with the need for new homes, a significant volume of planning approvals already exist. Data from the GLA shows that approved planning consents exist for 240,000 new homes (GLA 2015e), which is enough to meet the housebuilding target for the next half decade or so.

Figure 3.5
Planning approvals in London fall short of homebuilding targets in most months
Planning permissions net of target approvals (4,085 per month) to meet housebuilding target



Source: GLA 2015e

However, it is very likely that not all of these consents will be actually developed. Data produced for the LGA identifies around 111,000 unimplemented planning permissions in London, which represents around one in four of all of England's unused consents and a rise of some 20,000 over the last five years (LGA 2016).

More detailed analysis of the pipeline of planning permissions by Molior offers some insights into why so many consents do not turn into homes. Studying earlier data, Molior's research suggests that of the 172,000 private homes in the pipeline in 2014, only around 105,000 homes were 'realistically deliverable' according to site examinations (Molior 2014).

According to Molior, there are a number of explanations for this poor conversion rate, including that:

- Large sites (over 500 units) are unlikely to commence immediately or evenly, and therefore are unlikely to be built out at a rate commensurate with present housing demand. Molior therefore limited its estimate of realistically deliverable supply to 105,000.

- Within this, the actual supply delivered from these 105,000 consented homes is argued to be much lower, as a significant proportion of developments with planning permissions are not held by developers.
- A significant proportion of sites with permission are on hold for various reasons, including an inability to find a developer, the difficulty of accessing finance and the cost of building materials.

The second point in particular was echoed in research from Savills, who identified that a significant proportion of housing land was in the hands of non-developers, and thus unlikely to be turned into homes at any point in the near future (Savills 2012). There appears to be a specific constraint in London created by landowners being able to make sufficient capital gains from the sale of land with planning consent attached without needing to implement those consents. Thus, simply increasing the number of planning approvals will not be enough.

> The mayor and boroughs should be given responsibility for London's share of the Large Sites Infrastructure Programme, and use the resources to provide a recyclable pot of funding for supporting stalled sites and funding regeneration.

> Boroughs should be able to charge council tax, at their discretion, on planned developments where mutually agreed building milestones for those sites have been missed.

Resources for planning departments are increasingly stretched

Many submissions, not least from the Home Builders' Federation (HBF), various housing associations and other housing delivery organisations, cited weaknesses in the capacity, skills and efficiency of borough planning departments as a key barrier to increasing housing supply in London. This is a reflection of the demands on their resources, funding constraints, and the pace and quality of decision-making required.

The NAO has estimated that, across England, planning department budgets were reduced by almost half (46 per cent) in the last parliament (NAO 2014), which has inevitably reduced the ability of local authorities to provide a good-quality and efficient planning service. In a submission to the commission, London Councils estimates that ‘development control in London has seen a projected net shortfall in funding of around £37–45 million annually between 2012/13 and 2014/15’ (London Councils 2015). Given the limited resources remaining in local authority budgets to cross-subsidise other departments, the resources required to unblock the system may need to come from the planning applicants themselves. London Councils, for one, has argued that this could increase capacity:

> *‘If planning fees for large-scale housing regeneration projects were charged on a full cost recovery system enabling councils to meet all 13-week planning targets, this would save developers up to £486 million per year in delayed development costs, while adding only £65 million in planning fees.’*
> London Councils 2014

> The power to set planning fees should be devolved to the mayor, who should work with boroughs and developers to determine the fee levels and structure. In exchange, there should be guarantees around planning deadlines and reducing planning conditions.

> These changes should be supported by a London-wide planning inspection team established to monitor planning department performance.

Planning negotiations over affordable housing are lengthy and resource-intensive

A core part of the role of planning departments is to negotiate planning gain (or section 106 agreements) with developers. These negotiations provide affordable housing and community infrastructure in exchange for the granting of planning permission for developments. Most private developments comprising 10 units or more are expected to make a financial or in-kind contribution to affordable housing and wider infrastructure requirements.

In a submission to the commission, Brownill et al (2015) provided detailed data showing that, between 2004 and 2014, planning gain supported the delivery of 57 per cent of all affordable homes in London. However, the data also shows that this share is shrinking. A number of submissions argued that this was the result of the increased emphasis on development viability in planning negotiations (ibid, Islington Borough Council 2015).

The negotiations around planning gain are a significant drain on planning resources, precisely because they are negotiable. Local planning authorities have to contest with developers, often for lengthy periods, about whether the affordable housing and community infrastructure that the planners are demanding is appropriate, and whether or not the scheme remains viable and permits a sufficient level of profit for the developer. Ironically, this uncertainty can also drive up the price of land:

> *'There is a lot of consternation out there on both sides (planners and developers) about how hard it is to navigate the planning system when the rules (affordability targets, density, etc) are seen as negotiable elements of planning. This leads to people basing their bid price for land on an assumption that they can get more out of planning than the rules might allow – thus driving up the price.'*
> Holman et al 2015

The contestable nature of the affordable housing requirement allows landowners to speculate that they will be able to increase their profits (by negotiating away affordable housing and other community infrastructure) – but this in turn contributes to pushing up the land price, thus creating a risk that a development becomes unviable.

Brownill et al also identify that local planning authorities are often outgunned by developers in these negotiations. They highlight that (a) there is a lack of skills within planning authorities to interpret and carry out viability assessments and (b) the quality of agents and consultants advising local authorities varies, while wealthier developers can often afford much better legal and technical advice (Brownill et al 2015).

The increased emphasis on 'negotiable viability' – the idea that the planner should take a development's profitability into account – is adding time to the planning process, and thus acts as constraint on good, efficient planning, and therefore in turn on housing development output.

The question of viability may be addressed by applying a tariff in order to set a fixed affordable housing contribution for developments in London. Applying a tariff is not necessarily easy or uncontroversial, on account of differing land values across the capital, which means that in some places a tariff will underprovide for affordable housing in some areas, and in others bring into question the viability of the housing development. A great deal of care needs to be taken therefore to apply a tariff that is fixed, workable and fair, and to ensure that the delivery of affordable housing and market housing is not compromised in the process.

On balance, if these conditions are met, the commission is in favor of applying a planning tariff in London, so long as it is achieved after in-depth consultation.

> The GLA and boroughs should begin consultation on replacing negotiated affordable housing contributions with a tariff system of fixed developer contributions to affordable housing.

Specifically, the GLA should consult on an affordable housing tariff in order to simplify the process of agreeing affordable housing contributions and speed up the agreement of planning applications. The GLA and boroughs should work together to determine the level of the tariff, and use borough plans to estimate the viability of the tariff in different areas. The consultation on the tariff must ensure that its introduction would not have the effect of reducing overall levels of housing supply or affordable housing supply.

The tariff could differ by travel zones, or between inner and outer London, to recognise differences in land values. The default position of the tariff should be that homes are delivered on site, or at least within the borough, where this is not possible.

At the point a tariff is launched, boroughs could identify any exceptional sites or areas that they consider to require a higher tariff. Where a developer believes that a site cannot viably be developed if the London-wide tariff is imposed, they should be able to appeal to the GLA for exceptional permission, but only with the backing of the relevant borough. An expert team should be established within the GLA to consider such appeals.

> Large sites that are not viable under any tariff should be given housing zone status.[11]

If it is introduced, the tariff should be reviewed after several years to assess risks and effectiveness.

Planning department performance varies widely

Some borough planning departments are performing better than others when it comes to delivering the number of planning consents needed to meet their own housing targets and support the delivery of the London Plan.

National planning performance data shows wide variation in the proportion of planning applications being granted approval: across the 33 boroughs, the proportion of applications receiving approval ranges from 61 per cent to 98 per cent (DCLG 2016b). Similarly, there is significant variation in the speed with which planning consents are being processed (ibid). However, as the RTPI noted in its submission to the commission, getting permission is only one step in the process, and other steps are equally important – namely the additional negotiations and conditions that follow initial planning consent (RTPI 2015).

> *'Although the time taken to determine applications is often still good, there are indications that there are increasingly delays in pre-application advice, s106 agreements and discharge of conditions.'*
> RTPI 2015

The use of planning conditions – actions required as a condition of planning consent – can contribute to delays. A report by the University of Cambridge has highlighted a number of cases where planning conditions were considered onerous and unnecessarily detailed. The report also identifies that because planning departments have specific targets for the processing of initial applications, planning conditions are being used after the consent stage to get agreement on more complicated issues that might more logically have been addressed by the original application.

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11 Housing zones are designated areas for housing development and regeneration. These areas are supported by capital spending and planning support to accelerate housebuilding.

> *'Local planning authorities [LPAs] and housebuilders said that in order to meet the targets, some LPAs over-used conditions in order to get decisions through in time, lengthening post-determination processes.'*
> Burgess 2014

Many of those who participated in the commission's evidence-gathering sessions were happy to point out both exemplary and underperforming boroughs. In a recent report, London First summarised how borough planning departments could in some cases constraint development (London First 2014):

- Some boroughs have poorly performing planning departments, and so agreeing all of the necessary permissions can take a long and unpredictable length of time.
- Some boroughs' decision-making processes can be unrealistic, turning down applications where developers are unable to meet the requested level of planning gain, irrespective of the affordability to the developer of such commitments.
- Some boroughs resist any more development – some local planning committees, made up of elected councillors, would rather turn down a planning application than risk upsetting local voters.

> The government should give the mayor the power to call in poorly performing boroughs, and call in their plans, supported by a London-wide planning inspectorate.

> Boroughs should publish an annual review of their progress against national and local targets for delivering housing and identifying land.

Summary: planning

There is a clear need to increase both the sheer volume of approvals and the type and quality of approvals going into the system in order to stock the pipeline with 50,000 housebuilding starts every year. Beyond this, it is a key priority to support large sites to deliver at speed (given how important they are to meeting housing targets), and to reduce the time it takes a developer to move from the granting of planning permission to the housebuilding start to housing completion.

Investment: new build, developers and finance

Building new housing costs a significant amount of money. Estimates for the London Infrastructure Plan 2015 conducted for the mayor are that the capital needs to identify around £16 billion per year in housing investment if it is to meet the need for 50,000 new homes – suggesting a per-home cost of around £320,000 (GLA 2014c), which is roughly consistent with other findings (see for example Savills 2016b). The total investment figure assumes that, in line with the mayor's housing needs assessment (GLA 2013a), half of these units will be available at below-market prices.[12]

London attracts significant amounts of investment, and it has sharply increased in recent years: in the four most recent quarters, £8.1 billion was invested in new housebuilding, comprising private investment of £6.4 billion together with £1.7 billion of public investment (ONS 2015a).[13]

Thus, if £16 billion is needed each year but only £8.1 billion was invested in the last four quarters, a significant level of additional public and private investment is required. Achieving this means addressing the finance constraints facing different property developers in the capital and using public money to unlock further private-sector development.

Private developer funding for larger developers has improved, but varies by type of development

According to successive studies by the GLA, the general financial outlook for development has improved. In 2012, access to debt was considered a priority issue (Molior 2012), but this pressure has since eased, on the back of improving economic conditions, bank liquidity, and growing asset values:

> *'Effectively, there is now an unlimited pool of funding for schemes costing below £40 million as the limiting factor in the market is the number of*

12 Intermediate housing covers a range of housing products, but for renters it occupies a price range between social rent and market rent, and for owner-occupiers, it is a discounted homeownership product, for instance shared ownership homes.

13 While overall output appears to have risen sharply in the last year, new orders for housing appear to have dropped sharply since 2014 (ONS 2015a). On this evidence, the number of new homes likely to be delivered in the coming years is therefore likely to undershoot previous estimates (see Molior 2014).

> *schemes that can be invested in. And there are no real 'no-go' areas for development funding anymore … This was not the case two years ago.'*
> Molior 2014

While the funding environment may have improved for some, the HBF argues that certain lending conditions are preventing development on large sites proceeding more quickly.

> *'A key constraint for housebuilders in London is the lengthy capital lock-up period that is inherent in the development process. Because of time limits on mortgage offers, domestic purchasers can be disadvantaged, especially on schemes for which the developer requires the release of cash to support future phases of development … Opportunities for guarantees arrangements [could] address these constraints.'*
> HBF 2015

In short, large phased building projects need access to funding to get off the ground, and in order to finance initial construction work, developers tend to rely on a relatively small cadre of cash-rich buyers who can afford to buy a property 'off-plan' several years before it is completed. This limits the pool of funding available to large developers, because domestic buyers are unlikely to be given a mortgage for a home that will not be built for several years.

However, while homebuyers are one important source of investment, investment in building homes for renters is a growing segment of the investment market in London, because this is where a significant and growing proportion of domestic demand is located (Savills 2016d). Molior estimates that there are currently around 19,000 rented homes in the planning system or under construction across the capital (Molior 2015), while Savills suggests that investment in new-build properties for private renting is worth £2.65 billion nationwide, some 60 per cent of which lies in the capital (Savills 2016d). The opportunity that 'institutional' investment in the rented market provides is that these developments are largely not competing for the same pot of investment funding as homes for sale, due to the length of time over which the investor expects to be repaid.

Therefore, where viable, new blocks of homes for rent can effectively open up different pools of funding, rather than lenders of capital looking for a quicker return. However, the sector also needs a level of stability in order to unlock the levels of investment that are needed, and so the government will need to take care that its reforms to the wider private rented sector do not adversely affect the supply of new 'built to rent' homes.[14]

Smaller developers are still struggling to access finance

Beyond the demand constraints affecting larger developments, it is also argued that smaller builders face particular difficulties in accessing finance. Holman et al (2015) found that the reluctance of lenders to offer development finance to small and medium-sized enterprises (SMEs) was a fundamental challenge to housing supply in the capital.

This issue was also highlighted by the Federation of Master Builders (FMB) in its submission to the commission, which argues that the current ratio of loan value to project value is set too low, limiting smaller developers' access to London's expensive land. Based on a survey of its members, the FMB estimates that SME output could be doubled:

> *'If the loan-to-project value ratios on offer were improved to 80 per cent from a standard 60 per cent, based on recent housing statistics, this could equate to almost 20,000 new homes being built, making a significant impact on the supply-side gap in the UK housing market.'*
>
> FMB 2015

While the private sector is delivering at near-peak levels in London – approaching the 17,000 homes a year it achieved in the mid-2000s – the challenge will be not only to sustain that level of investment and output but also to unlock the resources for the extra 8,000 market homes needed to reach the 24,000-a-year target identified in the mayor's housing need assessment. Increasing the availability of land to provide

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14 There are a number of other obstacles that stand in the way of achieving greater investment in the rental market, which are explored in more detail in chapter 5.

more development opportunities will be essential to achieving this, as will be supporting the delivery of different products, such as homes for private renting – which, as estimates from Savills show, is the fastest growing area of private housing demand (Savills 2016d).

Direct public investment in housebuilding is essential, but has fallen sharply

While funding conditions for private developers of sufficient size appear to be improving, the investment constraints on social housing providers are getting tighter. Over the last four decades there has been a significant shift away from direct investment in affordable housing by the government, especially through local authority development.

Social housing developers finance their construction from a range of sources, including grants, rents, cross-subsidy from other activities and borrowing against their assets. Direct investment from public funds is critical to the delivery of affordable housing, and also to the ability of their assets to unlock additional private investment.

For instance, the recent national Affording Housing Programme funding model was set out as follows:

> *'Housing providers [will invest] some £12 billion on new homes, funded by a combination of government grant (£1.8 billion), borrowing by providers supported by rents on the new properties (we estimate around £6 billion), and funding from other sources (about £4 billion).'*
> NAO 2012

In simple terms, the last programme managed to lever in around £5 for every £1 of government grant. The programme was mostly delivered by housing associations, who were able to borrow against the value of and cross-subsidise through wider development of homes for sale and for market rent.

The London funding programme was not dissimilar to that of the rest of England. Since 2011, the GLA has acquired operational responsibility for distributing its share of national capital funding, to be dispersed into a number of separate bidding programmes to provide both affordable homeownership (40 per cent) and affordable rent homes (60 per cent).

The value of the current GLA grants programme is £1.6 billion for 2015–2018, or around £550 million per year. The intention of the programme is to support the delivery of 45,000 new affordable homes – or 15,000 homes per year over that period. However, while the ambition is significant, the level of funding on a per-home basis has been sharply reduced. Under the mayor's programme it is estimated to be around £35,000 (GLA 2015e), roughly 60 per cent less than under the previous Affordable Homes Programme (IPPR estimates based on NAO 2012). In exchange for this reduction, housing associations and boroughs have been allowed to set higher rents, and are expected to draw in further resources from elsewhere.

The case for fiscal devolution to London

The critical point is that while this £550 million per annum is a vital resource for building affordable homes, a much higher level of investment is essential in order to deliver the extra 10,000 affordable and intermediate homes each year that London needs. Still, public funding does not have to pay for the whole home: grant funding unlocks additional funding from private sources. The challenge, then, is that while London has taken control over its element of Homes and Communities Agency funding through the GLA and mayor's covenant, its resources are still determined by national funding allocations, and not by housing need or GLA revenues.

In order for London to be able to provide additional resources and unlock additional borrowing, public investment in housing needs to be more closely aligned with property tax yields in the capital. In the broader context of a deal with government committing to specific development targets, responsibility for property taxes should be gradually devolved, in line with the approach to business rates taken in other city deals.

> London should be able to retain all or a substantial proportion of its stamp duty income with an equivalent adjustment to other grant-funding sources.

> In consultation with key members of the business sector (such as the London Chamber and London First), London should have the ability to adjust stamp duty taxes.

> Over time the government should review the case for greater devolution of property taxes.

Rent finance

Rents in both local authority housing and housing association homes are set largely through 'target rents' set by government. On the one hand, this ensures that neither tenants nor the government (through increases in housing benefit) are forced to pay the cost of development. On the other, it means that housing authorities' development programmes are subject to shifts in government policy: currently, a 1 per cent annual cut is being made to social rents, which could reduce housing supply nationally by some 14,000 units (OBR 2015). Over four years, London Councils estimates that the cut could reduce housing authorities' income by some £800 million (London Councils 2015), money that could otherwise be invested in building new homes.

> The government should conduct an independent evaluation of the impact of rent reductions on both household incomes and housing supply, and move towards greater flexibility on rent-setting when the four-year rent cut period concludes.

> If the government will not offer more flexibility in rent-setting, it should commit to a long-term rent settlement of at least 10 years, to provide some stability.

GLA loan and debt finance

Other sources of funding exist that might be used to plug the investment gap but which are also constrained by various controls on public policy. Generally, the mayor's powers to raise debt to finance housing are limited. The financial structures of the GLA group are complex, and have different debt limits that are determined by the authorised debt-limits set by the government and their own revenue streams (GLA 2015f). The GLA itself currently has a debt limit of £4.6 billion (GLA 2015f), while TfL has a higher limit, of around £10.6 billion in total debt allocation, partly on account of Crossrail financing (ibid). However, the GLA uses a significant amount of its own money to finance TfL projects rather than housing, and in any case, is approaching the limit for current borrowing set by the Treasury.

Communities and local government secretary Greg Clarke, in comments to the Travers Commission on London Finance, admitted that:

> *'Most of London's financing power is at TfL and this probably means that London's investment progress recently has been skewed more towards transport than in other areas such as housing, energy, waste and water.'*
> Cited in Travers 2013

Indeed, the London Finance Commission concluded that there needs to be a significant shift in both the borrowing and revenue powers of the GLA, stating that:

> *'Relaxing restrictions on borrowing for capital investment while retaining prudential rules and simultaneously devolving the full suite of property tax revenue streams would afford London government greater autonomy to invest in the capital.'*
> Travers 2013

> The GLA's powers to borrow for the delivery of new homes on public land should be increased. The additional debt should repaid by additional property tax revenues and receipts from developments.

Borough loan and debt finance

Similarly, the capacity of local authorities to use debt finance is also subject to a series of constraints, in particular the setting of borrowing limits on borough housing revenue accounts (HRAs), the vehicles through which local authorities manage their housing assets and core social housing finances. In 2013 it was estimated that the borrowing headroom for all of the London boroughs was collectively £1.4 billion (GLA 2013c), sufficient to build 4,500 new homes at the average market rate, or many more if the local authority could provide the land free of charge. Given the historic position of boroughs as major housing developers, and their overall ownership of 400,000 homes worth around £25 billion (NHF 2015), this comparatively low limit on borrowing capacity is an unhelpful impediment to building more homes.

> Boroughs' housing borrowing limits should be lifted.

These limits are only one constraint on local authorities' ability to finance new housebuilding, however. As a review for the mayor's office stated:

> *'Existing [local authority new-build] programmes are funded through a variety of development models and utilising finance from a wide range of sources, including GLA grant, New Homes Bonus, receipts from Right to Buy sales and disposals, commuted s106 sums, private sector investment, as well as HRA borrowing headroom and surpluses. However, there are borough-specific constraints on investment that probably need to be addressed [including] operational capacity and the availability of land.'*
> GLA 2013c

While there is considerable support across the housing sector for raising local authority borrowing limits, the government is resistant to any such measures that increase the burden of housing debt on public finances. As such, local authorities have explored a series of measures to circumvent the current HRA system, for example by creating subsidiary organisations and joint ventures, or seeking out different forms of investment finance, such as the £178 billion local government pension schemes (Elphicke and House 2015). The chancellor has also committed to consolidating public-sector pension funds into a limited number of 'public sector wealth funds' to invest in housing and infrastructure. This potential additional source of investment, from institutions such as the London Collective Investment Vehicle, should be welcomed.

> To unlock further potential investment, the mayor and boroughs should work with the new pooled public-sector pension funds to identify investment opportunities in London housing.

Summary: investment

The factors that shackle greater investment in London housing are both private and public. On the private side, larger builders appear to be faring best – they are able to access funding and leverage their balance sheets to support schemes of significant scale – and investment in homes for private renting make up a growing share of the investment market. However, smaller developers appear to be struggling still, facing resistance from banks and other lenders which is unlikely to be removed without a change in lenders' own practices.

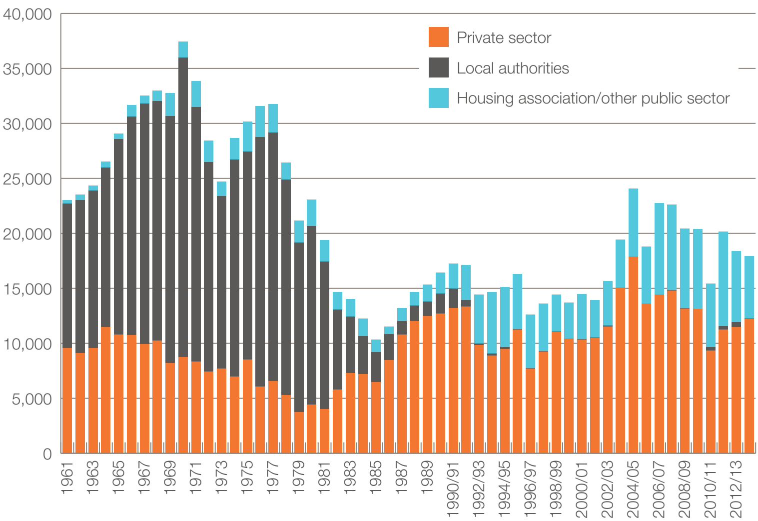
On the other side, both public spending and borrowing by London's public bodies remain constrained, and capital grants to boroughs and housing associations have been cut, along with rents, which is limiting their ability to build more affordable homes.

Housebuilders: capacity, social providers and the skills challenge

London needs developers – firms and people – to build new homes. This highlights two particular constraints on London's housebuilding capacity: the loss of major sources of housing supply over recent decades, and the combination of falling labour availability and increasing material costs.

As figure 3.6 shows, the make-up of London's developers has changed over the past 40 years.

Figure 3.6
Over the past 40 years, increasingly fewer London houses have been built by local authorities and more by private developers
Housing delivery by tenure type, 1960–2014



Source: Shelter 2015

The capacity of the private sector

New home numbers in London was at their highest in the late 1960s and early 1970s, when the private and public sectors were together building more than 30,000 homes a year. However, since then the scale and make-up of housing development has changed: the public sector has largely stopped directly building homes, and the two biggest builders today are the private sector and housing associations.

The private sector has evolved over recent decades, as illustrated by evidence from the Lyons review on national trends:

> *'In 1993 the 42 largest firms built 51 per cent of new homes; in 2013 the 41 largest firms were responsible for 73 per cent of new housing supply. During the 1980s there were on average 10,000 SME builders, and they delivered about 57 per cent of all output from the sector. In 2013, this figure had shrunk by almost three-quarters to just 2,800 active SME builders producing 27 per cent of new homes.'*
> Lyons 2014

Regional data on the shape of the industry in London is limited. However, research by Molior suggests that:

> *'The number of firms that build significant quantities of homes in London is limited. During the 12 months to June 2012, just over 11,000 homes consented for private sale commenced construction in London (in schemes containing 20+ private sale homes). 70 per cent of these units – roughly 8,300 homes – were commenced by just 23 firms.'*
> Molior 2012

London needs its major developers to deliver housebuilding at the requisite scale, especially in light of the constraints on building that the public sector is facing.

Private development is limited to the number of new-build properties that can be sold

The capacity of the private sector is constrained by demand. Because developers will only build as many homes as they think they can sell, and given the cost of homeownership in the capital, there is a ceiling to demand that is defined by what people are prepared to pay and what lenders are willing to lend. This in part helps to explain the government's emphasis on the Help to Buy programme as a way of increasing the demand for homes for sale. New-build properties in the capital are not cheap: the average selling price in London for a newly built home is £392,000 (Nationwide 2016).

The number of houses that the private sector will build for sale may also be constrained by other factors, not least of which is the level of investment in land and work in progress that they are prepared to carry. For instance, Holman et al (2015) argue that on large sites, phased development happens for a number of reasons, namely: 'it helps manage cash flow; it facilitates sequencing of complex construction tasks; and it ensures that build and sales rates are broadly kept in line'.

By facilitating developments that include a wider set of tenures – in addition to homes for private sale – some of these challenges can be partly overcome. Homes for rent, both social and private, are often presold and prefinanced, and so they do not carry the same level of risk that comes with homes built for sale.

Unfortunately the return on investment for rental properties tends to be materially lower for the developer and the landowner than is the case with homes for sale, so while the growth of build-to-rent is picking up (Molior 2016), it is difficult to see how volumes in this market can compete against the sharply rising prices seen in the build-to-buy market without receiving additional support and incentives.

Smaller builders are continuing to struggle

The long-running attrition among SME developers, highlighted in the quote above from the Lyons review, creates a further constraint on building. Given that 25 per cent of potential capacity in the mayor's land assessment lies in small sites, which are generally unattractive to major developers, the struggle for SME developers to compete in the market may act as another brake on delivering the homes that London needs.

The specific barriers that SMEs face include reduced access to competitive capital appropriately geared (FMB 2015); limited access to shovel-ready sites (Holman et al 2015), in part because housing and planning targets incentivise the release of and focus on larger sites; and the costs and risks associated with planning for small developments (ibid, Pocket Homes 2015).

London Housing Bank funds should be available as loans to local authorities to provide infrastructure and land remediation to create shovel-ready small sites for SME developers.[15]

In addition, a proportion of small public-sector sites should be offered to SME developers for first refusal at no initial charge, with landowners taking an equity stake in the sale or rental value of the developed homes.

The capacity of housing associations

Housing associations are essential to sustaining the capital's affordable housing supply. Collectively, housing associations deliver around a third of homes in London, at an average rate of around 6,500 homes per year (DCLG 2015d) – at their peak they delivered roughly 8,500 homes in 2011/12, at the tail end of the Affordable Homes Programme.

In response to a changing policy environment, not least around funding, the sector is diversifying. A report for the London Assembly found that:

> *'Housing associations are expanding their roles by offering different housing products. The G15 aims to deliver 13,000 affordable homes between 2011 and 2015. However, they have recently announced that in addition they will provide 4,000 properties for rent at market prices and at least 1,100 homes for sale at regular London prices.'*
>
> London Assembly 2013

The biggest housing associations in London, the G15, have since committed to expanding housing supply even further: the combined building plans of their members would deliver around 93,000 new homes by 2020 (G15 2015) which, depending on the proportion delivered in London,

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15 The London Housing Bank offers loans to developers in exchange for providing discount rent products and longer tenancies; properties are covenanted as rental properties until the loan is repaid.

could amount to an increase of around 40 per cent on what housing associations are current delivering. Much of this increase will be in homes for market sale and market rent, in order to compensate for falling levels of capital subsidy. Bringing forward more land will be essential to provide the opportunities for housing associations to increase there supply, and therefore:

> The mayor and boroughs should do a deal with housing associations to double their housebuilding in exchange for access to a pipeline of new sites.

Many associations said that they could expand, given the right policy conditions, but that current policy uncertainty was holding back any expansion plans. One association commented:

> *'While we are still unsure about the detailed implications [of government policy], the accumulation of these changes will reduce the capacity of housing associations to develop new homes and puts an obligation on us to be more creative and work closely with councils. … Housing associations must respond to the current and proposed changes by developing a range of housing products that address the broader range of the population, rather than cater for their traditional customer base.'*
> Submission to the London Housing Commission

While grants are falling and rents are being cut, housing associations could expand their building through the extension of Right to Buy to housing association tenants, which in theory will provide the housing associations with full compensation for the sale of the house (unlike local authority Right to Buy purchases) and thus provide the cash to invest further in replacing the homes lost into the private sector from the scheme. In practice, however, the programme is likely to be limited due to the high values of the homes in London, and the evidence concerning previous Right to Buy programmes is that replacement levels have been very low (Emmett 2015).

The extension of Right to Buy to housing association properties should be fully funded through general government revenue in order to allow for the full replacement of social rented homes. It should not be funded through the sale of high-value local authority homes.

The receipts from high-value local authority home sales should be retained by local authorities to replace homes sold on a like-for-like basis, with any surplus used to fund a second home.

The sale of housing association homes, to be funded by selling high-value council homes, is in the short-term likely to lead to a fall in the number of much-needed social homes in the capital, and replacements may inevitably take many years to be built, even if the funding for those replacements is provided in full.

Given that the high-value homes needed to pay for housing association Right to Buy sales are concentrated heavily in London, and particularly in inner London, the policy may well have the effect of changing the tenure profile and mix of households in inner London for the worse – that is, with fewer social rented properties available to the growing number of households that need low-cost housing options. The other specific challenge facing housing associations in trying to use Right to Buy income to increase supply in London is the availability of land on which to build replacement homes, which, as outlined earlier, is limited.

Even with the potential for extra capital from Right to Buy sales, the National Housing Federation has highlighted other brakes on the expansion plans of London housing associations (NHF 2015):

- cuts to social rent which nationally will reduce housing association incomes by some £3.9 billion over four years
- valuation of housing association affordable housing stock at below market values which reduces their borrowing capacity.

Neither of these can be resolved without major changes to government policy around rent-setting and affordable housing.

> As recommended above, the government should commit either to flexibility in rent-setting or to a longer-term rent settlement.

Local authorities were once major developers, but no longer build homes

While improvements to capital funding conditions and rent-settling policies could allow housing associations to expand further, on their own they have not been able to compensate for the decline of housing delivery by local authorities themselves, in part because, traditionally, much of their funding for building new homes has come from the same diminishing pot of public capital investment.

As major landowners, landlords and planners, local authorities are well placed to deliver significant numbers of new homes, working with private developers and housing associations through contracting arrangements or joint ventures. However, over a long period of time, the scale of development undertaken by London boroughs (and local authorities nationally) has been significantly scaled back (see figure 2.5). This is the result of a wide range of policy decisions that have affected the funding available to local authorities to build new homes and the incentives to transfer their stock to housing associations.

In particular, local authorities have been subject to significant reductions in funding since the 1970s. As IPPR has characterised it previously, the capacity of the public sector has diminished with the switch in spending from 'bricks to benefits' (Cooke and Davies 2014). This shift has had a dramatic impact on output: while London boroughs built an average of around 20,000 homes a year throughout the 1960s and 1970s, borough housing completions in 2014/15 numbered just 280 (DCLG 2015d).

However, while they have relatively little borrowing capacity or capital funding to invest directly, London boroughs continue to hold significant land assets. Used effectively, these assets could provide valuable support for the building of new affordable homes, and a long-term income to the local authority.

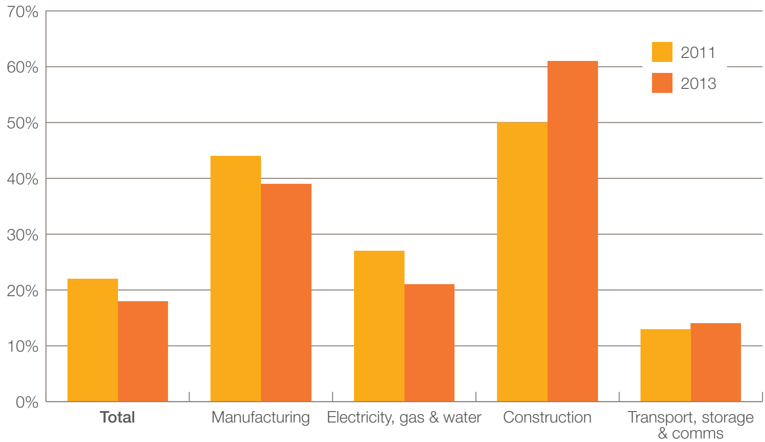
Borough-owned land should be brought forward through joint-venture partnerships with housing associations or private developers in order to develop affordable and market housing. The public landowner should retain a long-term equity stake in any such development.

Finding skilled labour is becoming more difficult

A building programme capable of delivering the 50,000 homes needed every year demands a commensurate supply of building materials and labour. While there remains a question as to how severe these constraints are, particularly concerning labour supply, there is a growing challenge facing the construction industry that could serve to both drive up costs and reduce supply.

The LGA has recently undertaken an analysis of labour availability, and it appears that filling posts in the construction industry is becoming more difficult.

Figure 3.7
Filling skilled trade vacancies in construction has become more difficult in recent years, unlike in other related sectors
Percentage of vacancies in selected skilled-trade occupations that are 'hard to fill', 2011 vs 2013



Source: LGA 2015

London is expected to see the greatest growth in employment in the construction sector, at 2.4 per cent growth between now and 2019, against an anticipated UK growth of 1.9 per cent. However, despite this, the Construction Industry Trade Board predicts a net additional recruitment need of around 2,500 new skilled tradespeople each year for the next five years in order to keep pace with current building trends (CITB 2015).

In its submission to the commission, the London Chamber of Commerce and Industry highlighted that (LCCI 2015):

- 20 per cent more workers will be required, on average, to meet the demand in 2014–17 than were needed in the years 2010–13
- 29,000 workers in training are needed to deliver the current pipeline of demand for construction workers
- however there are currently only 14,500 in training, or around half as many as are required.

While the sector does appear to making do at present, there is clearly a need to escalate training provision now in order to support any increase in the pipeline of new homes. Equally, there is a need to train now to replace the 400,000 construction workers who are set to retire within the next five to 10 years (ibid). The simple point is that unless there are the workers to build 50,000 homes a year, the homes will not get built.

> As and when adult skills funding is devolved to London, the mayor should use these new powers to ensure that a central component of the adult skills programme will be devoted to increasing the number of skilled workers for the construction sector.

Material costs are rising

In addition to growing labour shortages is the issue of material costs, which have increased by around 20 per cent in five years (BIS 2015), feeding into the costs of development and ultimately into the viability of housebuilding projects.

The problem is such that, according to a report by Turner and Townsend (2015), London is one of the most expensive places in the world to build a dwelling, second only to New York. They suggest that while the labour costs in London are 70 per cent cheaper than in New York, overall building costs are only 4 per cent less – they speculate that this is driven by a range of factors, including logistics, the design and contracting process, the rising cost of getting materials onto building sites, and various rules around the protection of nearby heritage buildings (ibid). While a submission from Mace suggests that a shift to offsite manufacturing could reduce building costs by around 30 per cent compared to traditional methods (Mace 2015) – which is in line with estimates made by McKinsey (Woetzel et al 2014) – these gains are potentially being overplayed: much of the major housing development that occurs in inner London does not employ traditional methods anyway, but is based on assembling steel, concrete and glass.

Conclusions

Ultimately, there is not one constraint on housing supply in the capital but many. Confronting these constraints, however, must begin with the question of land, because without land to build homes on none of the other elements – planning, investment or developer capacity – will matter. The mayor and the boroughs can do much to identify land within the GLA boundaries, but changes to public policy will help to unlock further land opportunities and to moderate land prices.

On planning and investment, government policy is the more severe constraint. The government will need to work with the mayor and boroughs both to increase the resourcing of planning departments, and to identify and unlock more resources for investment. This investment could and arguably should be used to bring more developers and developers of different tenures into the market, whether that is through more activity by boroughs themselves, housing associations, new private entrants, or even the GLA and TfL directly.

4.
WHAT IS PUSHING UP THE COST OF HOUSING IN THE CAPITAL?

London is a desirable place to live. It attracts people from all income groups from around the world, as well as from other parts of the UK itself. But there is more to housing demand than simple population growth: the availability of credit, property's role as an asset class and public policy can all impact on overall demand for housing in the capital.

In this chapter we consider the various drivers of demand for homes in London, and the extent to which they drive up the cost of housing.

Market forces

London's strong population growth is a key driver of demand

London's population is growing rapidly. The population growth expected over the next 15 years – from 8.5 million today to 10 million by 2030 (GLA 2014e) – implies that London will have to find additional living space for the equivalent of the combined populations of Birmingham and Manchester.

The flows in and out of London are considerable. To 2030, around 3.3 million people are expected to come to London from other parts of the UK, and around 4.3 million are expected to leave. International migration to London is expected to be lower, at around 3 million individuals, with only around 1.8 million expected to leave over the same period – thus contributing significantly to London's growth. London's population growth is also driven by internal factors, such as a higher birth rate than other parts of the UK (ibid).

As we set out in the previous chapter, this suggests London needs to house an additional 50,000 households per year over the coming decades (DCLG 2015g), but actual delivery of new homes comes nowhere close to this figure.

This new housing demand is not spread evenly across income groups. The mayor's draft housing strategy in 2014 recorded that:

> *'Research indicates that the greatest shortfalls in supply relative to demand are in the low to mid-priced segments of the market. These trends suggest that there is a need to expand both the range of products delivered and the number of places where they are built.'*
> GLA 2014d

The Strategic Housing Market Assessment, which estimates the demand for new homes, suggests that of the 50,000 new homes needed annually in the capital, only around 48 per cent need to be 'market homes' – homes sold or rented on the open market without any form of subsidy. The remainder will need to be offered at below-market rates: 32 per cent should be social housing, and 20 per cent intermediate (intermediate rent or shared ownership) housing (GLA 2013a).[16]

Put simply, slightly more than half of the new homes required will have to be subsidised, whether by the developer or through public funding. However, research by Savills shows that it is precisely these subsidised homes that London is failing to deliver. Within the mainstream market – that is, excluding homes for the very wealthy – we are building less than one-third of the amount of lowest-cost housing needed for those on the lowest incomes, but around four-fifths of the homes needed for those who can afford to pay the most (Savills 2015b). This indicates that London's housebuilding, which is already below-target, is particularly bad at meeting the needs of those on lower incomes.

Credit conditions can either boost or subdue demand

Another key part of demand is the cost and availability of mortgage credit. Credit conditions play a significant role in determining how many potential buyers are able to make a

16 See note 12.

purchase, and what they are able to pay. For instance, the IMF has found that house price growth is 'positively and strongly associated' with growth in housing finance, with a 10 per cent increase in housing credit leading to an increase of six percentage points in nominal house prices (IMF 2011). This relationship remains statistically strong even when other relevant factors are taken into account, such as real GDP growth, inflation, the rate of population growth, interest rates and unemployment (Dolphin and Griffith 2011).

This suggests that credit conditions can act as both a pump and a brake on demand, depending on whether credit is more or less easy to access – whether that is determined by regulation or by lenders' own behaviour. The commission heard from a number of mortgage lenders that lending conditions in the capital have 'largely normalised', notwithstanding record low interest rates.

Much of the control over lending conditions rests with the Bank of England, which has oversight across a range of areas, including macroprudential regulation – in this case, regulating access to mortgages and setting specific conditions concerning the level of risk that lenders can offer to mortgagors. For instance, the Financial Policy Committee (FPC) has the power to curb mortgage lending at debt-to-income or loan-to-value ratios that it considers to be excessively high, while the Prudential Regulation Authority (PRA) has recently begun a review of buy-to-let credit conditions, given recent rapid lending growth.

So far the FPC has only applied limited restrictions on lending: rather than applying a hard cap on the debt-to-income ratio for an individual mortgage, it has applied a limit on how much 'risky lending' a lender can hold. Specifically, large mortgage lenders can lend up to 15 per cent of new residential mortgages at loan-to-income ratios at or greater than 4.5 (BoE 2014). However, the governor of the Bank of England has also recently voiced concerns about the growing volume of buy-to-let lending in particular (BBC 2015), which – as we cover in the next section – is especially important to London's housing demand.

Investors make up a significant proportion of overall demand

Housing demand is not just driven by people looking for homes to live in but also by people looking for homes to invest in. That housing might be treated as an investment is nothing new, but two particular types of investment activity have attracted considerable attention in recent years, particularly in the capital: buy-to-let landlords and foreign investors.

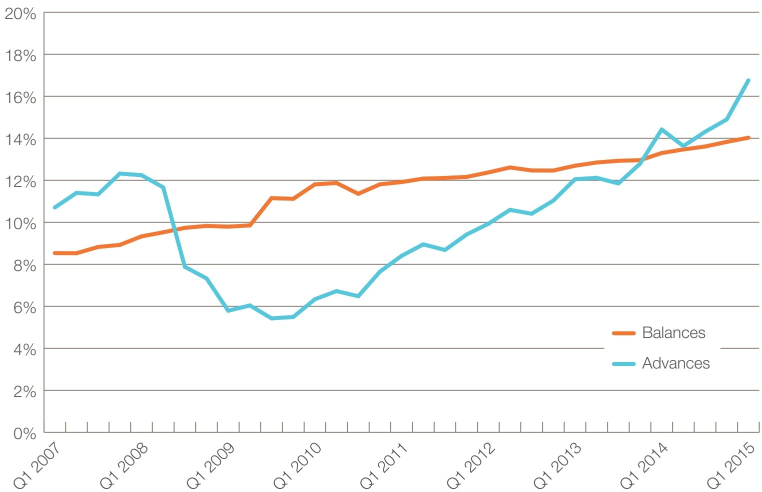
Buy-to-let investors

Buy-to-let property investment is now a major source of housing demand in the UK, and in particular in London. The Council for Mortgage Lenders (CML) estimates that over the last five years, buy-to-let has accounted for more than 60 per cent of the overall growth in mortgage balances outstanding (at £44 billion out of a total of £71 billion growth in outstanding balances) (Clarke 2015). Around 17 per cent of new lending is to private landlords, and nearly 14 per cent of mortgaged debt is held against buy-to-let property, up from 8.5 per cent in 2007 (Bank of England 2015). Figure 4.1 shows how buy-to-let lending has taken off since 2009.

Figure 4.1

Buy-to-let has made up an increasing proportion of all new mortgage loans over the past 10 years

Buy-to-let mortgage lending as a percentage of total gross lending, UK, 2007–2015



Source: Bank of England 2015

The CML attributes the growth of buy-to-let to a range of factors, based on growing demand both for rented housing from the wider population, and for rented property as an investment opportunity. These factors include (Clarke 2015):

- more young people in higher education
- high levels of migration
- reduced availability of social housing
- reduced job security
- affordability pressures on would-be owner-occupiers
- poor returns on pensions and investments, which has led investors to seek out other options.

Increased credit availability and increased competition between lending firms is also thought to have played a role.

And nowhere in the UK is buy-to-let more popular than in London. The CML estimates that a quarter of all UK buy-to-let mortgages are taken out on properties in London, compared to 13 per cent of UK residential mortgages (Clarke 2015). Within the new-build market, the ratio is even higher: Molior (2013) estimates that buy-to-let investors bought almost half (48 per cent) of new-build purchases in the capital in 2013. This is in spite of the fact the returns on investments from rents in London are weak relative to other parts of England (see chapter 5), which suggests that it is the expected capital gain that drives buy-to-let investor demand. Table 4.1 presents a breakdown of buy-to-let purchases, by the category of buyer.

Table 4.1
Buy-to-let purchases of new dwellings, London, 2013

	New buy-to-let homes sold	BTL sales as % of total London housing sales
Private individuals (1 or 2 homes)	6,250	29%
Private individuals (larger portfolios)	3,150	15%
Private block purchasers	750	4%
Total	**10,150**	**48%**

Source: Molier 2013

Buy-to-let investment is therefore a significant source of demand for new homes in the capital – and where this investment is directed at new-build private rented homes, can be a strong positive force for increasing investment and housing supply in the capital.

Foreign investors

The hypothesis that foreign investors are driving up prices in the capital has received significant attention in public debate, but unfortunately there is limited research in this area. A study by Knight Frank of prime property (worth £1 million or more) looked at the prevalence of two kinds of buyer in a sample of 3,500 sales: foreign-born buyers and foreign non-resident buyers. Across the sample, which included purchases of both new-build homes and second-hand properties, 51 per cent of properties were bought by UK nationals, 49 per cent by foreign buyers. Across all sales, 28 per cent of purchases were made by non-resident buyers (Knight Frank 2013); however, non-residents (who may nonetheless be UK nationals) were over-represented in the new-build homes market, buying around half of those included in the sample (ibid).

While this seems to paint a picture of significant investment activity by foreign buyers, in the context of the wider housing market they are unlikely to be providing a significant additional boost to overall demand. As the GLA points out:

> *'Overseas-based investors purchase in the region of 10 to 15 per cent of new-build homes in London as a whole, but this activity is highly concentrated in 'prime' central London areas with UK residents buying over 90 per cent of new build homes in outer London.'*
>
> GLA 2014d

In any case, the new-build market makes up only a small fraction of total housing transactions in any given year, and thus domestic demand, whether from first-time buyers, home-movers or buy-to-let landlords, is much more important for 'mainstream' markets.

Public policy

Policies designed to support homeownership and stimulate demand

Demand for housing in the capital is also underpinned by government policy, with the objective of helping both first-time buyers and home-movers to access the credit they need to purchase a home. London is a particular concern for government, given that levels of mortgaged homeownership have fallen by 12 percentage points in a decade (DCLG 2015a).

This is reflected in the falling number of sales in London: while prices have risen above their pre-crisis levels, the number of property transactions has not yet recovered. Sales remain some 20 per cent lower than their long-run average (Land Registry 2015), which is thought to be related to ever-larger deposit requirements reducing demand among first-time buyers. As we noted in chapter 2, the average deposit required for a first-time purchase in London is estimated at £74,000 (Hudson 2015a).

The government's response to falling transaction rates and declining levels of homeownership has been to try to stimulate demand through a number of programmes, including Help to Buy and Starter Homes.

Help to Buy

The government's Help to Buy scheme aims to do two things: reduce barriers to market entry for first-time buyers, and improve the affordability of new-build homes for both first-time buyers and home-movers. The scheme incorporates several products: Help to Buy ISAs offer a 25 per cent government top-up of savings towards a deposit; Help to Buy equity loans are government loans of up to 20 per cent (40 per cent in London) of the cost of a home, provided interest-free for five years; and the Mortgage Guarantee Scheme provides a government guarantee to lenders, effectively transferring a part of the mortgage risk from bank balance sheets to government balance sheets, and allowing borrowers to borrow at higher loan-to-value ratios (to some extent contradicting the controls the Bank of England is looking to impose on riskier borrowing). Certain elements of the scheme are focused exclusively on new-build homes, which the government hopes will boost housebuilding as well as demand.

Some elements of the Help to Buy policy were strongly supported by various submissions to the commission's call for evidence (see for example CML 2015), especially equity loans on new builds, which in theory should create additional demand for newly built homes for sale in the capital. However, while there has been strong take-up of this support in other regions of England, particularly the North West, the impact on demand in the capital has been fairly limited. Between the policy's introduction in 2013 and 2015, only 3,150 equity loans were taken out by first-time buyers across the capital, or only 6 per cent of total take-up across England (HMT 2015a).

Figures for the Mortgage Guarantee scheme are more opaque, but again its impact on demand for homes appears fairly limited, accounting for just 3,200 transactions between 2013 and 2015, or around 5 per cent of take up in England, and around £323 million of equity in the capital (HMT 2015b). Of the 197,000 housing transactions that took place across England over the last two years, these equity loans and guarantees made up only 3 per cent of all house sales.

On account of both the cost of housing in the capital and the sharp decline in the numbers of first-time buyers, the government from February 2016 increased the upper limit on the support available through Help to Buy equity loan scheme in London, from 20 per cent of the value of the home to 40 per cent. Savills estimates that this will help to significantly stimulate demand: with the new 40 per cent loan, a household with an annual income of £50,000 would be able to afford a lower-quartile new home in 20 of the 33 boroughs, where previously the same household would only have been able to afford to buy in eight boroughs (Savills 2016c).

The Help to Buy ISA is another, similar form of support to address housing affordability: the government offers a maximum of £3,000 to buyers who manage to save £12,000. However, in London, this may have a limited impact in terms of supporting additional demand: the rate of house price growth in the capital implies that by the time an ISA holder has saved enough to earn the £3,000 bonus (given that an individual is allowed to save only £200 a month), the price of the house they want to buy is likely to have risen by some £44,000, and the deposit by £8,400 (IPPR analysis based on Nationwide 2016 and PwC 2015).

Starter Homes
Another government initiative which may work to increase demand for housing is the Starter Homes programme. The policy effectively fixes the price of a new-build home built specifically as part of this programme to the market level, and then applies a discount of 20 per cent (which expires after five years of ownership) – in principal this should stimulate additional demand among consumers looking to buy new homes. The details of the policy are currently being debated as part of the government's Housing and Planning Bill, but the government has put aside significant sums to deliver Starter Homes – around £2.3 billion to support the first tranche of 60,000 houses across England – and is also intending to directly commission them on the Old Oak Common site in north-west London, which, given the significant delays that have occurred already in turning the Old Oak site into homes, will directly contribute to new supply.

However, there are specific concerns about Starter Homes in the London context. Because the cost of a Starter Home is pegged to market prices, the 20 per cent discount is unlikely to make these homes affordable in most boroughs for first-time buyers (Shelter 2015). Equally, the policy may actually slow development. Savills has suggested, for instance, that 'there is a risk that the Starter Homes policy could distort the new homes sales market, without significantly increasing the number of new homes delivered overall' (Savills 2016c).

In the national context, there is considerable concern that the 20 per cent discount transfers to the owner of the home after only five years, at which point the public subsidy is lost. This prospect distorts the market and leads buyers to overvalue the home. To reduce this incentive:

> The government should consider maintaining the Starter Homes 20 per cent market discount in perpetuity, or at a minimum extend the period for which the 20 per cent discount applies to at least 10 years.

A final concern centres on the fact that the government policy demands that Starter Homes are included as a part of the affordable housing provision negotiated between developers and local planning authorities. This is despite the discounted price of a Starter Home in London being capped at £450,000, which is significantly above what first-time buyers are paying for homes in the capital (see Nationwide 2016), and the fact that, unlike other affordable housing products, the discount transfers to the owner after five years, returning their home to full market value.

The government's commitment to increasing the number of homes is welcome. However, the commission believes that Starter Homes should be delivered in addition to existing affordable housing requirements, not as a replacement for social rented homes.

> The government should not impose a Starter Homes quota as part of local authority affordable housing negotiations, but instead leave it to local discretion.

Policies designed to dampen investment activity

On the evidence above, the government has clearly sought to stimulate housing demand across the UK. However, it appears increasingly interested in *shaping* demand too, in particular by tilting the balance of policy towards first-time buyers and away from people buying homes as investments.

For instance, recent changes to policy have led to increased taxes on owners of multiple properties, via increases to stamp duty on buy-to-let and second-home purchases, which from April 2016 will see buyers paying an additional 3 per cent. At the average London property value of £500,000, the stamp duty bill for a buy-to-let property (or second home) will rise from £15,000 to £30,000.

Knight Frank suggests that this change is already having a dampening effect, with foreign buyers increasingly looking at alternative locations, such as Edinburgh (Sullivan 2015). Impact assessments of the policy suggest it will bring in a further £825 million by 2020 (HMT 2015c), and the biggest share of this is likely to come from London. However, there is no evidence that this additional cash from raising taxes on property will be channelled towards investment in building more homes.

More widely, the property tax regime needs certainty in order to encourage institutional investment in new housing projects. Therefore, if the government wishes to continue to attract institutional investment into build-to-rent, in order to deliver the 10,000–15,000 homes that London needs, then it should continue to exempt bulk purchases of 15 new homes or more.

As recommended above, control of stamp duty should form part of a major package of devolution to the mayor and boroughs.

Rental demand

In London, the demand for rental properties has skyrocketed as people have increasingly found themselves priced out of homeownership: both the total number of tenants and the percentage of London residents who rent have doubled within a decade (DCLG 2015a).

With this growth in the number of renters, rents have risen significantly: the average monthly rent in London is now around £1,400, compared to the average in England of £600 (VOA 2015), and Savills predicts above-inflation rises in London rents for the next five years (Savills 2016d).

As with house prices, the gulf between the cost of renting in London and elsewhere in England is getting wider (ONS 2015b). And wages in London are not keeping pace with these rising housing costs: as figure 4.2 shows, average rents are now more than 115 per cent of the average weekly earnings in the capital.

Research by the Resolution Foundation estimates that a quarter of households renting in London are paying more than 50 per cent of their income to their landlord (Resolution Foundation 2016). Affordability varies significantly by borough, but data from the Valuation Office shows that median rents now exceed 50 per cent of median household income in eight of the 33 London boroughs (VOA 2015, GLA 2015b).

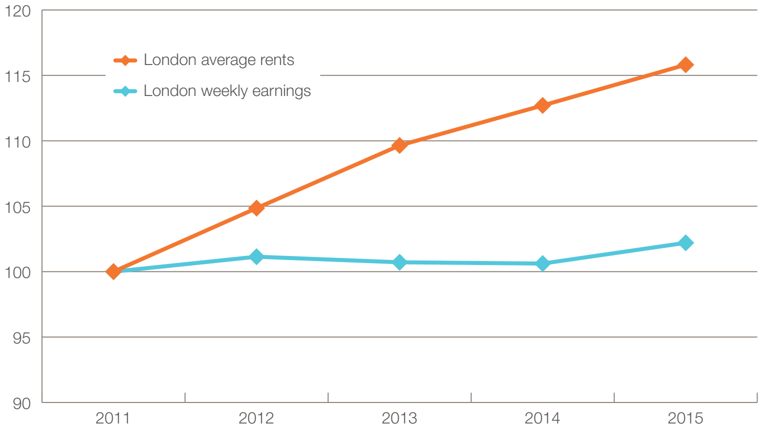
Insecurity of tenure and its impact on rent costs

The average length of a tenancy in the rented sector is much shorter (at 3.5 years) than it is for social renters (11 years) or owner occupiers (17 years), according to the English Housing Survey (DCLG 2015h). Shorter rental contracts also allow for more frequent rent increases, and so may play a role in rent inflation.

Figure 4.2

Rent costs have risen much faster than average earnings in London

Average weekly rents versus average weekly earnings, London, January 2011 – January 2015 (index 100 = January 2011)



Source: ONS 2015b

The same survey found that private rents were, on average, significantly lower the longer a tenant had been in their current home: those in their current home for less than a year were paying £198 a week on average, compared with £158 for residents of 5–9 years (DCLG 2015a).

There are several possible explanations for the prevalence of short-term tenancies. It could be that they are simply favoured by landlords, since they provide the option to increase rents or dispose of assets at regular intervals.

It could also be that letting agents are pushing shorter-term contracts. A review by the London Assembly stressed this possibility:

> *'There is growing evidence that letting agents are encouraging landlords to raise rents and to offer short tenancies. Shorter tenancies offer the prospect of more frequent upward rent reviews, encourage 'churn' of tenancies and allow charges*

for registration, credit checks, renewal fees that all increase the already high cost of the sector.'
London Assembly 2013b

The Residential Landlords Association argued in its submission that mortgage lenders were partly responsible for limiting their members' ability to set longer tenancies (RLA 2015). The CML took a different view, stating:

'We have been working with mortgage lenders to remove barriers to access for tenants by helping to reduce onerous mortgage terms, particularly those which limit the length of a tenancy … However tenants, often led by lettings agents, incorrectly assume that they are only entitled to a six or 12 month agreement. Mortgage lenders who have relaxed their criteria report that uptake of longer term tenancy agreements is limited. This could of course be for a number of reasons but crucially mortgage lenders should not be viewed as a barrier to longer tenancies.'
CML 2015

Presently, the mayor and boroughs have limited powers to demand changes to the market-standard assured shorthold tenancy. They can use planning decisions and financial investments (such as the London Housing Bank) to require that properties offer longer tenancies – and they have shown their willingness to do so. Such moves are welcome.

To support longer tenancies in the rental market, the mayor should establish a London lettings hub, which should offer discounted fees to landlords offering longer tenancies, and enable tenants to search for properties by tenancy length through its online platform.[17]

Boroughs should have the power to use licensing fee discounts and, where appropriate, licensing conditions to drive longer tenancies in their areas.

The impact of public policy on rental demand

Other than rent controls, which a great deal of international evidence suggests would harm investment and lead to lower-

17 See chapter 5 for more details.

quality properties (for example, see Clarke et al 2015), there are relatively few tools at governments' disposal to counter rent inflation.

Policymakers have instead focused on helping those on low incomes to meet their housing costs directly, through housing benefit. However a series of recent decisions, such as the introduction of a housing benefit cap, appear to illustrate a growing reluctance on the part of government to compensate for ever-increasing private rents.

While social rents are usually met in full by housing benefit, the same is not true for tenants who rent privately – the equivalent benefit that they are able to access is the local housing allowance (LHA), which provides rent subsidies for low-income private renters.

In an attempt to curtail the cost of housing benefit, the 2010–2015 Coalition government sought to reduce the level of payments by linking LHA to market rents at the 30th percentile, rather than the 50th. At the same time, these allowances were frozen at 2011 rates, and thus have not kept pace with the increase in rents of roughly 16 per cent across the capital in the period since (ONS 2015b). For example, Crisis found that:

> *'In London almost six in 10 LHA rates (57 per cent) are at least 5 per cent lower than the estimated 30th percentile of local rents. This is considerably higher than the national average of one in 10 LHA rates falling at least 5 per cent lower than the 30th percentile.'*
> Crisis 2015

On the one hand, rent subsidies may underpin rising demand and rent-cost inflation; however, on the other, it is clear that they are now falling significantly short of local London rents, which leaves many households facing a financial crunch.

While the government has attempted to compensate for this problem by providing additional money to help in high-pressure housing markets through the Targeted Affordability Fund [TAF], qualitative research for the DWP has found that market rents tend to surpass LHA rates even with discretionary support available (DWP 2015b).[18]

> The government should relink local housing allowance to local rent levels to ensure that low-income households can continue to rent in the capital.

A crucial response: building more homes and more affordable homes

While London has fairly limited powers to control the scale of demand for housing in London, what it can and must do is respond to that growing demand by building more houses.

Building new homes is essential to meet growing demand for properties, and tackle the scarcity that underpins cost increases in the homeownership and rental markets. Government research has calculated that for each shortfall of 100,000 homes per year in housebuilding nationwide, prices will increase by a magnitude of 12–14 per cent each decade above baseline trends (ODPM 2005).

> *'Undersupply underpins scarcity and higher house prices. The perception of undersupply also encourages market expectations of higher prices, thus encouraging speculation and over-consumption of housing as a good. For long-term reasons of economic health and social equity, the UK needs more homes.'*
> Dolphin and Griffith 2011

The extent of demand for property in London means that it is going to take a lot of building just to contain prices, let alone see them fall. In its submission to the commission, members of the Highbury Group illustrated the challenge:

> *'If we delivered 35,000 more than in the past, for the next 10 years, then, using the econometric modelling of the Barker review, this 1 per cent extra stock per annum would reduce house prices by 1.3 per cent per annum. In other words, the inflated average*

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18 Furthermore, the DWP review highlighted a number of responses that showed that homelessness due to eviction for not keeping up rent payments is on the rise.

> *house price in 10 years' time would be £750,000 rather than £850,000, ie 15 per cent lower.'*
> Highbury Group 2015

However, it is also worth noting that building more homes would also increase demand for homes, precisely because it would become more affordable to live in the capital (Bramley 2016). Thus the first conclusion is that there is a need to build a lot of homes for a long time to contain rising house prices and match the scale of demand. The second conclusion is that volume alone is not enough: a range of subsidised homes as well as market homes will be required to ensure that key workers – such as nurses, police and care workers – and existing residents can continue to live in the capital.

London is not delivering enough affordable housing

The mayor can work to tackle the affordability crisis by delivering more affordable housing, that is, housing for people 'whose needs are not met by the market':

> *'Affordable housing is social rented, affordable rented and intermediate housing, provided to eligible households whose needs are not met by the market. Eligibility is determined with regard to local incomes and local house prices … Affordable housing should include provisions to remain at an affordable price for future eligible households or for the subsidy to be recycled for alternative affordable housing provision.'*
> DCLG 2016c

However, the definition of affordable housing is shifting. One implication of the Housing and Planning Bill currently going through parliament is that Starter Homes (priced at 20 per cent below the market, as described earlier in this chapter) will count as affordable housing, despite the fact that the price of the home will return to market value five years after purchase, and the subsidy provided by losses to other affordable housing products will not be recycled for future housing provision. With these changes, the definitions of what is affordable will be determined by the secretary of state.

While the government's commitment to increasing the number of submarket homes for sale is welcome, the types of affordable homes that are needed in London should be decided by the results of the housing needs assessment.

> The next mayor of London should commission a new housing need assessment for London, to identify a wider range of housing needs for different income groups. The mayor's housing investment programme, and the types of housing that this funds, should be designed to fund homes across this range of needs.

The pot to invest in building more affordable homes is too small

The mayor's office, London boroughs and housing associations build and acquire a large number of subsidised housing through the mayor's covenant programme. The capital funding, worth around £550 million per year, is intended to provide around 15,000 homes per year within the spending period – 60 per cent for shared ownership, and 40 per cent for affordable rent. The average grant rate is therefore around £35,000 per home (GLA 2015e).

London's biggest demand is from households on modest or low incomes. If the target for social and intermediate housing in the strategic housing market assessment is 25,000, then the mayor's programme is clearly not big enough to provide for this growing group of people – in fact it will be around 10,000 units short on its own terms. On the basis of the per-home grant set out above, this leaves the mayor's capital programme short by at least £350 million per annum.

The mayor's capital programme could go much further and build many more homes if housing associations and boroughs were prepared to take on more debt in exchange for lower levels of grant funding and the ability to set higher rents – effectively spreading the total subsidy further but more thinly. The problem with this approach – aiming for maximum supply on low subsidy – is that in order to cover the cost of the development, the tenant or purchaser would need to pay more in rent or mortgage payments, which may defeat the objective of providing homes that are genuinely affordable.

Table 4.2 illustrates a number of different 'affordable' housing options, the rent they could be expected to require, the extent to which these monthly costs are affordable (against median and bottom-quintile incomes) and the level of grant funding required per home.

Given that there is a range of income groups to be accommodated by the 25,000 new affordable homes needed each year, the general point is that the next mayor will have to provide a wide range of subsidised homes, and there is a tension between maximising the number of homes delivered and how affordable those homes are to live in.

The second point is that the amount of grant subsidy required to build the home is strongly determined by the amount of rent or mortgage a tenant would be expected to pay – as tenants pay more in rent or buy more equity, the level of grant needed to cover the cost of the home tends to be smaller.

Table 4.2
A summary of submarket housing options and their affordability

	Cost: monthly rent	Affordability: Housing costs as % of household earnings*		Funding: estimate of capital grant per home
		Median earnings	Bottom quintile earnings (estimated)	
Social rent	£467	14%	26%	£89,000
Affordable rent	£775	24%	42%	£35,000
Shared ownership (30% equity, 10% deposit, £360,000 purchase price)	£1,020	31%	56%	£21,000
London living rent, set at 33% of median income	£1,076	33%	59%	Unknown
Starter Home (80% borrowing, 3% APR, £360,000 purchase)	£1,366	42%	75%	Unknown

Source: IPPR analysis of NAO 2012, DCLG 2015i, GLA 2015a
*** As noted above, various poverty-based measures of affordability suggest a household should not be spending more than one-third of its income on housing costs.**

Third, rents set in line with local median incomes – such as ‘living rent’ (see Lupton and Collins 2015) – are more like an ‘intermediate’ rent than they are a social rent. Therefore, they must target a different group of people to those targeted by social rents and even affordable rents – that is to say, they will target roughly the same people as shared ownership homes.

The fourth point is that Starter Homes are the least affordable option for households on middle incomes across London, and in London at least these homes would clearly be targeted at the upper end of the income spectrum. In fact, the monthly mortgaged cost of a £360,000 Starter Home would be largely comparable to market rents (VOA 2015).

In summary, then, as the market rises further and further away from average incomes, the need for affordable housing is growing quickly. Given that households on middle incomes are being increasingly squeezed by rising accommodation costs, there is a need to provide a wider range of housing products to ensure that key workers can continue to work in the capital.

However, providing a wider range of affordable housing options should not come at the cost of delivering fewer social rented homes. Rather, to make sure that London is building enough of the right type of homes to reflect demand, the size of the programme would need to grow significantly in order to deliver more homes of all types.

> To help meet its own target of delivering 1 million homes by 2020, the government should increase the capital subsidy to the mayor's housing covenant by at least £350 million per annum.

> In the medium term, the additional financing for the mayor's capital programme should be tapered away in exchange for greater devolution of the powers to set and retain property taxes in the capital.

Conclusions

Affordability is at the heart of the capital's housing crisis. The demand for homes in the capital, and people's growing willingness to spend more and more on rents and deposits in order to live in the capital, is such that reducing accommodation costs in the current environment – both market and policy – is going to be extremely difficult.

Nevertheless, policymakers do have options if they are willing to commit resources to delivering affordable homes, whether these are homes for sale or homes for different forms of renting. In doing so, however, there is a tension between delivering the maximum number of subsidised homes and delivering a smaller number of more heavily subsidised properties that will support those on the lowest incomes.

Just as there are limits on how much policymakers can influence house prices, there are similar challenges in seeking to control the affordability of rents. Rents are driven by the demand for properties and by what landlords think they are able to charge, in the absence of any market intervention such as rent controls. Our call for evidence also highlighted concerns around market actors pushing up rents and shortening tenancies to maximise profits.

For London to continue to be affordable for those on low incomes, however, the constraints on affordability cannot be managed by the mayor and the boroughs alone. Housing benefit and the local housing allowance provide a vital safety net for the unemployed and low-paid, but benefit levels are abjectly failing to keep pace with rent rises. The government will need to work with the mayor and the boroughs to provide relief to those on low incomes or face the risk that, in the short to medium term, levels of poverty will rise sharply and more and more of the low-paying jobs that keep the capital functioning on a day-to-day basis will be left unfilled.

5.
WHAT'S STOPPING LONDON PROVIDING MORE GOOD-QUALITY RENTED HOUSING?

In addition to the general constraints on housing delivery in London that we covered in chapter 3, and the constraints on social rented housing covered in the previous chapter, there are specific challenges to providing new much-needed private rented homes that are worth exploring in more detail.

In short, to reflect housing demand in the capital, London needs more market rent homes, of good quality, and professionally managed for those who either do want or cannot afford to buy their own home. It needs more submarket homes for rent for those on modest to low incomes to ensure that low-paid and key workers can continue in the capital, and it needs fewer substandard rented homes to protect the low-paid and most vulnerable citizens from having to live in poor conditions.

The growth of the private rental market

Renting is becoming the new norm in London. As of 2014, 50 per cent of households in London rented their housing, either from private landlords, housing associations or local authorities (or local arm's length management organisations, ALMOs) (DCLG 2016e).

The private rented sector (PRS) is the fastest growing tenure type in London, having more than doubled in size in a decade from 400,000 households to now over 1 million (DCLG 2015a). And the demand for private rented homes is growing faster in London than elsewhere in England: the capital now has just over a fifth of all of England's renting households (DCLG 2016e).[19]

As the private rented sector grows, the demographics of the sector are changing. The traditional profile of renters suggests they are young, mobile, single and economically active individuals. Now, however, there are three broad submarkets of renters: young professionals, families with children, and low-income and vulnerable households. So not only is the whole sector expanding faster than any other in London, but the changing demographics of those living in the rental market present an increasingly diverse set of demands (Montague 2012).

The commission recognises that new homes of all tenures are needed to address the housing crisis: the government's focus on homeownership runs the risk of increasing the number of people who own a home but not, ultimately, the number of homes available.

Looking at the figures on who bought *new* homes in 2013 illustrates this problem: of the 16,800 market homes sold in London in 2013, only 6,800 were purchased by the owner-occupiers (Molior 2014). Even if London Help to Buy manages to significantly increase demand for new homes to buy – say, up to say 10,000 homes – the mayor's assessed need for 24,000 new market homes each year means that between 10,000–15,000 of these will need to be for market rent (whoever ends up actually buying them).

The rest will need to be submarket homes – of which a great many will need to be for rent. On this score too, London is falling far short of what is needed. The mayor's assessment suggests that London needs at least 15,000 homes per year for social rent – yet on average over the last decade, London delivered around 8,000 of social rent homes per year (DCLG 2016f, 2016g).

Put together, London needs at least another 18,000–23,000 more rented homes to be built every year to make up the supply shortfall, and critically to ensure that London is building homes that people want and can afford to live in.

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19 Figures from the GLA show that the highest proportion of households renting privately are located in affluent inner-London areas. For example, over half of all households in eight wards in Westminster and Kensington and Chelsea are renting privately (GLA 2014d).

Constraints within the London rental market

The supply of build-to-rent houses

Homes for rent make up a small but growing proportion of the total stock of new delivery in London. Molior estimates that of London's third-quarter 2015 construction pipeline of around 240,000 homes, around 19,500 units were new block-built rented schemes (blocks of homes built only for rent); of these, around 8,000 had planning permission, 6,500 were under construction, and around 4,500 had been completed (Molior 2016). The same report also shows that the sector is growing quickly, with 7,010 private rented homes started in 2015, equivalent to more than half (54 per cent) of all private rented starts since 2009 (ibid).

Delivering more homes for rent is desirable as part of a wider strategy to increase housing supply across all tenures, and build-for-rent has the additional advantage of encouraging developers to deliver new homes quickly, because it is more difficult for them to build blocks for rent in stages, and they need the income from rents as soon as possible in order to finance the costs of the development. As the mayor's planning guidance notes:

> *'Such schemes are beneficial in a number of ways, they have the potential to accelerate delivery; can offer longer-term tenancies/more certainty over long-term availability; and can ensure high-quality management through single ownership.'*
>
> GLA 2015g

However, there are constraints on 'build-to-rent' development too. The Resolution Foundation has identified a number of specific barriers to institutional investment, some of which are more important in London than in other parts of the country:

> *'lower yields in the residential sector than the commercial sector; the lack of opportunities for investment at scale, concerns about possible risks to reputation; and the lack of efficient, high quality management … In general, investors are reluctant to invest in the development phase to get schemes up and running.'*
>
> Alakeson 2012

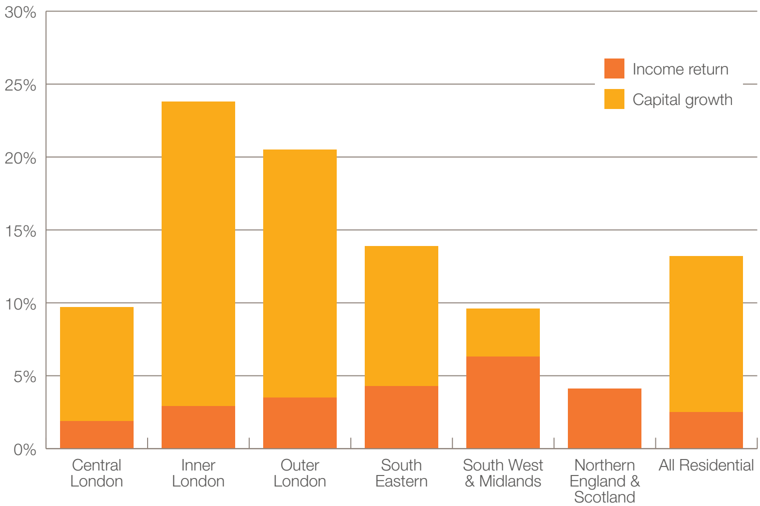
New rental blocks struggle to compete with homes for sale

Despite this high and rising demand – and despite an alleged 'wall of money' looking to enter the London property market – build-to-rent struggles to compete when compared with build-to-buy. Investment returns on residential lettings – relative to capital appreciation – have been limited, and there is an upper limit to how much rent landlords can charge, even as house purchase prices continue to outpace private rent inflation.

Figure 5.1

Return on build-to-rent investment in London is skewed towards capital appreciation rather than rental income, compared to other parts of the UK

Rental and capital yields in selected markets, 2014



Source: DTZ 2015

As figure 5.1 shows, income yields are far outstripped by capital yields in London. This illustrates the stark choice between patient or quick returns on residential investment – factors which inevitably drive what investors and developers are willing to pay for land. The evidence also highlights that, while rents are rising more sharply in London than in other parts of the country (LendInvest 2016), income returns from rents are much higher in areas where property prices are lower (DTZ 2015).

Thus, on top of the general constraints facing housing development in the capital – as we set out in chapter 3 – the specific challenge facing new rental supply is to ensure that new schemes are financially viable where property is to be built and retained as rented accommodation for a significant period of time. As the government's Montague review into rental development found:

> *'Developers wishing to build housing for rental will therefore compete for land with housebuilders that sell to the owner-occupied market. Because property can switch freely between the owner-occupied and private renting markets, the opportunity cost of an investment in housing is the price it could achieve on sale to an owner-occupier, not another investor.'*
> Montague 2012

As the main contribution to the cost of a building scheme is land, the main challenge is therefore land prices, and the inability of build-to-rent developers to outbid the build-to-buy sector and remain financially viable (Holman et al 2015).

In theory, lower land prices should bring higher yields, which itself would encourage more investment in build-to-rent. However, with the current set of policy tools, the state can do little to influence the price of land for build-to-rent developments through the planning system, as rental market property is usually within the same planning use class (class C) as build-to-buy homes.

The government also appears resistant to allow the application of a different use class to lower-value land, despite the recommendations of its own commissioned review (Montague 2012). Evidence heard by the London Housing Commission suggested that a use class specifically for rental developments would apply unnecessary rigidity to London's housing market.

At present at least, there is significant growth in the private rented sector – while not enough to match estimated demand. For instance, there are some 19,000 new-build homes to rent in the pipeline (Molior 2015) and the number of build-to-rent homes under construction at the end of 2015 was at least three times higher than in the previous year, with some 8,900 new rented homes under construction, and 5,300 completed (Molior 2016). Nevertheless, as noted in the introduction to this chapter, London does need many more of these schemes if it is going to deliver the 10,000–15,000 rented homes a year that are needed.

> The commission recognises that, on balance, there is not a sufficient case yet for a use class to support build-to-rent developments. If the conditions change to warrant the creation of such a planning tool, it should only be applied to new-build homes, with a strict time limit on how long the use class is applied.

However, there are other changes that could support the delivery of new build-to-rent blocks, including using public land to deliver rented homes for both market and affordable rents.

> A proportion of the non-operational public land identified by the London Land Commission should be earmarked for new rented homes (at both market and affordable prices), with the landowner taking a stake in the rental income from resulting developments.

> Where private developments need public money to unlock them, planning covenants can be applied by the mayor as a condition of that lending, to keep homes in the rental market for a period of time, as has been the case with London Housing Bank rules.[20]

Finally, the supply of certain types of build-to-rent homes may be facilitated by adjusting space standards. The space standards in London for a one-bed flat assume that two people live there. For some younger individuals, such as graduates, it may be appropriate to allow smaller space requirements in exchange for better communal facilities and reduced rents, as is provided, for instance, by The Collective. Flexibility on space standards could therefore could be offered to developers in exchange for certain rent limits, and these homes could therefore be held indefinitely as an entry-level housing option.

20 See note 15.

Most renters do not live in new blocks, and quality in older rented homes is variable

Building new rental homes will be crucial to providing an increased stock of professionally let, good-quality homes. But much of London's growing private rental stock comes from older homes transferred from other tenures (London Assembly 2011), and in these homes the standards of accommodation – in terms of both physical conditions and management quality – vary considerably.

A review by the GLA showed that 32 per cent of homes in London's rental market – or 280,000 homes – fail the 'Decent Homes' standard, higher than in other tenures.[21] Furthermore, approximately one in seven is unsafe, in terms of having a category 1 hazard under the HHSRS rating system – again, this is higher in rented homes than other tenures (London Assembly 2012).

There is evidence that poor-quality housing can have various negative social effects. For instance, Shelter found that living in poor-quality housing during childhood increased the likelihood of poor health in later life, an increased risk of mental health and lower levels of educational attainment (Harker 2006).

The reasons why a significant minority of the rental market is poor-quality are contested. For one, by comparison with the social rented sector, a disproportionate share of private rented housing is older stock: in London, nearly half was built before 1919 (London Assembly 2012), and so frequently fails to meet modern definitions of good quality in housing.

For another, a review by the GLA has suggested that many small landlords have limited financial resources with which to improve their properties, when compared with larger-scale providers such as registered social landlords (RSLs). This covers landlords who are unable to access finance to make substantial improvements, and those whose cash reserves or profit margins are too small to afford even minor repairs (London Assembly 2012).

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21 The Decent Homes standard is a measure of property conditions, based on whether meets the minimum statutory standards for a property, whether it is in a reasonable state of repair, whether it has modern facilities, and whether it has a reasonable degree of thermal comfort.

While it is true that private landlords have not been able to access the substantial capital funding available for the improvement of social homes, most recently through the Decent Homes programme, they have had the benefit of various tax allowances, including mortgage interest relief and 'allowable expenses' – that is, relief on the costs of operating as a landlord, including maintenance and repairs of the property (HM Government 2016).

Regulation and enforcement in the rental market is patchy

Furthermore, there may be financial disincentives to seek and maintain good quality rental homes. The English House Condition Survey reports that gross rental yields are higher on non-decent homes than on decent homes. Lower management costs and lower expectations from tenants may reduce the financial burden on landlords to improve the quality of their home (Rugg and Rhodes 2008). Another factor may be that regulation is unhelpfully fragmented across different types of property, and for different household circumstances (Rose and Davies 2014).

Nevertheless, there is substantial regulation in place to govern rented housing. Local governments are responsible for ensuring local dwellings are up to legal minimum standards, outlined in various laws and regulations. Blanket coverage for all property is provided through the housing health and safety rating system (HHSRS), to ensure that housing across all sectors is not a risk for inhabitants, their neighbours or the wider community.

However, enforcement of existing regulation is patchy (RLA 2015, Battersby 2011). The charity Crisis, for instance, argues that environmental health teams are often too severely understaffed and under-resourced to make an impact on housing quality (Crisis 2014). A survey of local housing authorities by the Local Government Information Unit found that 'a lack of resources' was the biggest barrier authorities faced in trying to improve engagement with the private rented sector (Lucas et al 2013).

Prosecutions against landlords are very rare: Shelter claims that in 2012 only 487 prosecutions were made, in an estimated population of 1.2 million landlords (CLG Select Committee 2013), supporting their claim that 'the problem is not a lack of powers, but the willingness and ability of local authorities to enforce their existing powers'. Battersby's review of enforcement found that fewer than one in 10 homes with serious hazards are dealt with in any year (Battersby 2011).

Consumer power is weak

Another significant barrier to improving housing quality in the rented sector is the relative weakness of the consumers – or tenants – themselves. The Competition and Markets Authority (CMA) recently highlighted that, despite the private rented sector being described as 'offering choice', consumers' choices are in reality highly constrained in high-pressure housing markets, and tenants are often forced to 'take what they can get' (Strong 2015). In addition, the CMA highlighted a key concern that tenants were reluctant to raise issues with their landlords or letting agents due to fears of retaliatory action.

The London borough of Redbridge expanded on this concern in response to a review by the London Assembly:

> *'It would usually be expected that competition in this market would improve standards and keep rents at a reasonable rate. However, the demand for private rented properties is now so great that the opposite is taking place, with standards declining and rents increasing.'*
> London Assembly 2012

Furthermore, research by Shelter (2011) has shown that socioeconomic groups further down the income scale (C2, D and E) are less likely to have their problems or complaints solved by the landlord than tenants in higher socioeconomic groups (A, B and C1) – at 22 per cent and 37 per cent respectively. The former were also twice as likely to avoid taking action against landlords in the first place, as the CMA noted, for fear of reprisals.

> The mayor should launch a London lettings hub[22] to link up tenants directly with good-quality, accredited landlords. The hub should offer discounted fees to landlords offering longer tenancies, and tenants should be able to search for properties by tenancy length through the online platform.

22 Similar to the government's RentSquare service: see https://www.rentsquare.io/

> The hub should also allow tenants to leave feedback on the quality of properties and property management, and provide data collected by boroughs of enforcement and licensing activities in their areas.

Quality of property and management is also patchy

Despite the prices of property in the capital, London's private rental market is dominated by small-scale landlords – according to the GLA:

> *'89 per cent of landlords were private individual landlords, 5 per cent were company landlords, and 6 per cent were "other organisation" landlords. These were responsible for 71 per cent, 15 per cent and 14 per cent, respectively, of all dwellings in the sector.'*
> London Assembly 2012

Evidence suggests that, in most cases, it is not pernicious motivations that cause landlords to leave tenants' problems unresolved, but that rather many landlords remain ignorant of even the most basic legislation that governs their sector. According to Shelter (2011), many of the complaints made against landlords are the result of amateur landlords being unaware of their responsibilities rather than deliberately neglectful. At the same time, research by IPPR has found that private landlords can feel unsupported by the local authority, especially when it comes to dealing with 'problem tenants' (Viitanen 2012).

The landlord accreditation system is meant to support good landlords through training and recognition. However, the mix of statutory obligations and accreditation schemes appears to generate substantial confusion among both landlords and tenants about what they can expect or are required to do.

The London Rental Standard is an umbrella term for a selection of accreditation schemes designed to provide a pan-London hallmark of quality. It helps landlords to understand what is expected of them, and helps tenants to understand their rights. It provides a single set of minimum standards for landlords operating in the city, and in order to get accreditation, landlords must register for accreditation and attend a training course on property management. On the surface, the rental standard is straightforward, but in fact it amalgamates seven different existing accreditation schemes, each of which has slightly different expectations of its members (GLA 2016). Perhaps the wider issue is that the scheme is also voluntary, and consequently coverage is limited. Research suggests that just 0.2 per cent of properties advertised for rent state that the landlord is signed up to the rental standard scheme (Osborne 2015), although this is likely to under-represent the total number who are registered.

> Existing accreditation schemes should be consolidated under the London Rental Standard as a single industry-standard accreditation, and by 2025 accreditation should be a mandatory under a London-wide property licence.

The ability of the mayor and boroughs to improve standards is limited

The mayor and the boroughs, through existing legislation, can already take significant steps to improve poor-quality private rented homes, and their power to do so will be bolstered by the some of the reforms that are part of the Housing and Planning Bill. The bill contains a range of additional instruments to tackle poor conditions and management in the sector, including a series of civil penalties (like parking tickets) for landlords who fail to address identified problems; the extension of rent repayment orders, whereby the tenant or local authority receives back a proportion of rent paid as compensation for various offences; and a strengthening of the 'fit and proper' test for landlords responsible for licensable properties (DCLG 2016d).

The reforms offer the potential for both tenants and local authorities to have significantly greater powers to complain and resources to act. However, given the constraints facing local authorities' enforcement capabilities, the impact of such changes may be limited.

For all of the merit of the government's reforms, the mayor and boroughs are also limited in what they can achieve in terms of identifying landlords, let alone licensing them. There is no formal mechanism to ensure that all landlords are registered with the local authority, despite the fact that this would support them in their enforcement activites. The Residential Landlords Assocation (RLA) suggests, for instance, that a simple change to council tax forms to require not just tenants' names but also the name of the landlord would significantly support enforcement activity in local areas (RLA 2015).

A more holistic approach would be to implement area-wide licensing schemes, of the kind operating in Newham and Liverpool. However, these schemes require the approval of the secretary of state, and even areas that have managed to implement area-wide licensing are permitted to use license fees only to cover the cost of implementing the scheme itself, and not for enforcing breaches in management or property standards.

> In exchange for a commitment to eliminate the number of non-decent rented properties, the secretary of state should relax controls on enforcement by permitting boroughs to create area-wide landlord licensing schemes and to use the fees to fund enforcement activity. The ambition for this licensing regime should be to achieve London-wide coverage by 2025.

> It should be a condition of such licences that all homes must meet a defined standard of quality (the Decent Homes standard) by 2025.

> Boroughs should be allowed to use licensing fee discounts and, where appropriate, licensing conditions to drive longer tenancies in their areas.

Conclusions

The private rented sector in London is growing quickly, and will be a core part of London's housing offer now and for the foreseeable future. New supply offers the potential to provide high-quality, professionally managed new homes to middle income households across the capital, but this is ultimately constrained, primarily by the availability of land at a cost that makes build-to-rent developments viable.

At the same time, many private renters are not living in new blocks of rented homes, and a significant minority of these renters face significant problems in terms of the conditions and good management of their properties. While the policy framework has much potential, the mayor and boroughs are constrained by limited and dwindling resources, and by the current rules around licensing, which together prevent them from making a full and well-funded response to the worst-quality dwellings, management practices and lettings activities.

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APPENDIX: SUBMISSIONS TO THE LONDON HOUSING COMMISSION

The commissioners wish to thank the following people and organisations for their submissions:

- Affinity Sutton
- Association of Residential Letting Agents / National Association of Estate Agents
- Bristol Law School
- Dr Sue Brownill
- Catalyst
- CBI
- Centre for Urban Policy
- Chartered Institute of Housing
- Council of Mortgage Lenders
- Create Streets
- Crisis
- G15
- Generation Rent
- Highbury Group
- Home Builders Federation
- Home Group
- Homeless Link
- Housing Forum
- Deri Hughes
- Kensington and Chelsea Social Council
- L&Q
- Lendlease
- Labour Land Campaign

- Land Value Tax Campaign
- Local Space
- London Assembly
- London Borough of Barnet
- London Borough of Hackney
- London Borough of Islington
- London Borough of Lambeth
- London Borough of Waltham Forest
- London Councils
- London Labour Housing Group
- LSE London
- Gail Mayhew
- Chris Mckay
- Mears Group
- National Federation of ALMOs
- National Housing Federation
- Peabody
- Pocket Homes
- Policy Network
- Royal Institute of British Architects
- Residential Landlords Association
- Royal Town Planning Institute
- Daniel Scharf, Waitrose
- SHOUT
- Tibals
- Town and Country Planning Association
- URBED
- Professor Cecilia Wong
- Z2k

‘The London Housing Commission does not claim to have all of the answers, but it is clear that the status quo will not do. The housing crisis will not solve itself, and radical measures of the sort we outline in this report will go a long way to delivering the volume of quality, affordable homes that the capital desperately needs.’

Lord Bob Kerslake, chair

London faces unprecedented challenges in housing its citizens.

Providing enough secure, affordable and decent homes is one of the biggest challenges facing the capital – London needs at least 50,000 of them each year to keep pace with its growing population. Currently, it is falling far short: last year only 25,000 new homes were built.

London’s unprecedented housing crisis has serious consequences. Businesses struggle to recruit and retain staff. More and more people live in overcrowded social and rented homes. Housing-induced poverty remains stubbornly high. And the government is spending billions of pounds on housing benefit to keep a roof over renters’ heads and provide temporary accommodation for homeless families.

The next mayor of London and the 33 boroughs should join forces to strike a major devolution deal with central government. They should commit to increase supply to 50,000 homes a year by the end of the decade, to ensure that London has sufficient affordable housing for citizens of all income levels, and to eliminate poor conditions in the rented market. In return, the government should give London significant new freedoms to control its own planning, borrowing and taxes.

NEW IDEAS
for CHANGE