BRITAIN’S HOUSING CRISIS – AND THE FAKE SOLUTIONS ON OFFER:
New #ElectionEconomics policy briefing from the Centre for Economic Performance

Housing affordability is a key concern of an ever-larger fraction of UK voters who are crammed into artificially limited space. At the same time, a lot of wealth lies in housing assets and there are many vested interests in keeping things this way, such as current homeowners and private landlords.

Substantive reforms could solve the housing crisis, but politicians of all stripes back away from such reforms out of fear of being demonised by the vested interests. Instead, proposed policies tend to tackle the symptoms – rather than the causes – of the UK’s housing affordability crisis.

These are among the conclusions of a new report from the Centre for Economic Performance (CEP) – the latest in a series of background briefings on key policy issues in the May 2015 UK general election. Among the findings:

- In 2014, UK house prices per square metre were the second highest in the world (topped only by Monaco), with especially high valuations in London and the South East. New houses are about 40% smaller than in similarly densely populated European countries.

- Over the last 40 years, house price growth in the UK has been faster than in any other OECD country and has far outstripped earnings growth. Consequently, a ‘housing affordability crisis’ has developed. The homeownership rate has been in decline since the turn of the millennium, falling from 69.6% in 2002 to 63.6% in 2013. Extending Right-to-Buy might halt this decline, but it would be likely to worsen the affordability crisis.

- The ratio of London house prices to average UK house prices has increased substantially since the 1970s. The price-to-income multiple in the Greater London area in 2014 was 8.5; for the UK as a whole, it was 5.0.

- The UK’s planning system is the main cause of the affordability crisis, especially in London and the South East. Despite population growth and rising real incomes, construction of new housing has been decreasing steadily since the 1970s, leading to a substantial housing shortfall.

- Where supply is constrained, the main effect of policies that stimulate housing demand – such as Help-to-Buy – is to increase house prices rather than supply. These policies may thus be an ineffective waste of taxpayer money at best and counterproductive at worst.

- A similar argument applies to property-related tax reforms. In supply-constrained areas, higher taxes are capitalised into lower property prices.

- The failure to revalue the council tax since 1992 and introduce effective property taxes has made the idea of a ‘mansion tax’ popular. Such a tax would be likely to
reduce the prices of expensive houses making them more affordable for wealthy would-be buyers and imposing a one-time negative wealth effect on current owners. It may have the effect of encouraging owners to subdivide their properties in an attempt to circumvent the tax.

- The evidence firmly suggests that the stamp duty land tax – which taxes property transactions – reduces household mobility. The resulting mismatch in the housing market exacerbates the affordability crisis.

- The ‘bedroom tax’ is most likely to affect landlords, who reduce rents to keep their tenants. This limits the potential to free up used space. To the extent that landlords do not fully take the hit, it has the potential to trigger displacement as shortages of smaller properties in some areas imply that tenants have to move away.

- A local annual property tax with automatic annual revaluation could provide incentives for residential development by generating local tax revenue that is tied to local development. This could help to reduce the chronic housing shortfall.

Dr Christian Hilber, author of the report, concludes:

‘Research points clearly to the UK’s rigid planning system as the main cause of the housing affordability crisis. Demand-side policies such as Help-to-Buy don’t work in this setting because they merely increase house prices.’

‘The current property-related taxes are inefficient, especially the council tax and the stamp duty land tax. While the former is regressive and does not provide sufficient incentives to permit development at the local level, the latter hampers household mobility and generates distortions in the housing markets. Importantly, it discourages downsizing of the elderly and upsizing of expanding young families.’

‘Solutions to the housing affordability crisis lie in a set of more supply-side friendly policies. But the obstacles to moving to such policies are vast since these policies antagonise vested interests, which appear to have been created in perpetuity.’

‘Yet the long-run consequences of political inaction – and the continuation of excessively low rates of new building – could prove socially explosive and economically traumatic.’

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Notes for editors:

‘UK Housing and Planning Policies: The evidence from economic research’ by Christian Hilber is the latest in CEP’s #ElectionEconomics series.

Objective, brief and non-technical, CEP Election Analysis is a series of background briefings on the policy issues in the May 2015 UK General Election.
This series discusses the research evidence on some of the UK’s key policy battlegrounds, including immigration, austerity, real wages and living standards, productivity and business, Europe, the NHS, schools, tuition fees, gender gaps, urban and regional policy, top tax rates, inequality, housing and planning, crime, climate change and energy.

These analyses are provided by some of our expert researchers and draw on some of our past and current research.

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