Reimagine Places: Home ownership

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Let's reimagine...

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This paper is one of a series of thought experiments in which we imagine new ways for local and sub-regional bodies to deliver public policy goals and boost local economic growth.

Many of these ideas will explore the growing opportunities for productive collaboration between public and private bodies in places as decision-making powers gravitate towards the city-regional level. Many will draw on the huge potential of data and digital technologies, 'big data' and analytics techniques. Others will involve tapping into the power of markets, new incentives, transparency or the wisdom of crowds. In every case, it involves fresh ideas. To channel our thinking, we imposed three rules.

01 Ideas must be designed to produce better public outcomes without increasing the burden on the taxpayer.

02 They must align with the government's philosophy and headline policies.

03 They must be realistic and deliverable.

But within these rules we want to step outside conventional thinking, and test out new ideas. We want to stretch ourselves, applying new technologies and techniques to solve complex problems. We are not calling for a specific future – but we are reimagining it.

What do you think?

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Reimagine housing

Our housing market is broken – and the consequences range from rising inequality to depressed UK productivity. Mark Essex argues that we need a new approach: a mix of financial products and rental reforms could alter people's behaviour and foster a more balanced economy.

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Home ownership is like a meal deal: to get some of the benefits you have to buy other parts of the package which you don't need. Can we unbundle this so that people can get a home they can call their own without it consuming all of their disposable income to this pursuit? Mark Essex looks afresh at Britain's housing market and how it must change.

For many years, governments have worked to give people access to affordable housing – but that goal has slipped ever further out of reach.

In the 1970s, the average home cost the equivalent of less than three years' work at the average salary; by 2012, it was over seven years[1]. Fast rising prices have squeezed an ever growing slice of the population out of the housing market: between 2003 and 2014 the proportion of home-owning households fell from 71% to 64%[2]; amongst those aged 25-34, it tumbled from 59% to 37%[3] .

Meanwhile, rising house prices create social costs – many of which end up at the government's door. Between 1979 and 2013, for example, housing benefit spending rose eightfold to £25bn[4]: that's more than Whitehall gives our 400+ local authorities[5]. And economically, the spiralling value of property pulls in vast capital investment – starving more productive sectors such as scientific research, services and manufacturing.

Until 2008, the Labour government tried to tackle the problem by encouraging housebuilding and extracting affordable homes from developers; but between 1996 and 2012, the number of UK households grew faster than the number of homes in almost every year. Completions currently stand at 140,000/annum[6] whilst households are growing at 200,000, leaving a gap that adds every year to pent-up demand.

Since 2010, the Coalition and Conservative governments have concentrated on the demand side – offering financial support to help people buy. But with house prices rising at more than 5% annually since 2013[7], such initiatives are massively outgunned; and the additional cash brings yet more demand into the market, pushing prices still further out of reach.

Why we invest in property, not productivity

So where's all this demand coming from? Why are people so focused on taking a major financial risk, and accepting a 25-year debt and unpredictable maintenance costs, in order to purchase an asset that cannot produce a return unless they move out or sell up? After all, a property can be a gold-plated millstone: the time, effort, taxes and fees involved in selling and buying a home create huge barriers to relocation, making it difficult to pursue a new job or meet changing family needs.

The answer lies in the value of housing as an investment, likely to rise in value more quickly and reliably than most alternatives. This, of course, is only true because people believe it to be so, and thus keep on investing – creating a self-fulfilling prophecy. Yet for individual investors and families, the power of collective belief creates some very hard realities. As long as property values are rising faster than earnings – and wage growth has sat around 2% since 2009[8] – then house prices will never be more affordable than they are today. No wonder people prioritise purchasing a home.

The property market's dependence on people's expectations around future prices makes it highly vulnerable to economic shocks, as we saw – outside London, at least – following the credit crunch. But it also provides a way forward. If policies were introduced to create a structural fall in demand, we'd see inflation drop. Then the fears of non-homeowners and the hopes of investors would also be calmed, taking some of the bulls out of the market and returning price rises to more sustainable levels.

To create this decline in demand, policymakers would have to find other ways of providing the advantages that people see in home ownership. People view their home as a legacy – something to pass onto the kids. Once the mortgage is paid, pensioners can enjoy a rent-free retirement. And in the UK, a person's home is their castle; unlike renters, homeowners are not at risk of eviction, abusive landlords or unfairly withheld deposits.

Unbundling home ownership

These are substantive benefits. But home ownership also has its down sides; and if people had other ways to achieve their goals, we could pull a significant chunk of demand out of the market – reducing home inflation to the steady, slow uptick that best serves economic growth and social goals.

The issues of housing as an investment, a legacy and a rent-free retirement are relatively easy to address using financial products – at least once the shine has come off property inflation. Intelligent, long-term investments in businesses or shares should be able to produce a 5% return. Life insurance can provide a legacy – and it comes without the risk that social care costs will eat up a home's value before the offspring get their share.

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And a decent pension can pay pensioners' rents particularly if some of the money twenty-somethings have in deposit-savings were invested in a pension, with fifty years' of compound growth. It's hard to compete, though, with the returns produced by current levels of house price inflation. So to make financial products an attractive alternative to property investment, kick-starting this new model, we first need to reduce house price growth.

There are many ways to achieve this – and we will need a wide range of tools if we're to cool our overheated housing market to a sensible temperature.

Cooling housing demand

In a previous paper[9], we have suggested one approach to encouraging older people to move out of under-occupied homes, whilst providing them with better care in high-quality accommodation. This document also set out how we could make better use of our housing stock, whilst helping young professionals in the rental market and reducing loneliness amongst old people.

Meanwhile, though, in order to cool housing demand it will also be important to make renting a more attractive option. And that means addressing the insecurity of tenure which so bedevils the experience of renting a home.

The most straightforward way to do this would be to make indefinite tenure available as a rental option, giving people the right to stay in their homes as long as they wish. This wouldn't work for every landlord or property, of course, and would require some public sector intervention: planning authorities could attach provisions to permissions requiring a certain proportion of new properties to be let on indefinite contracts, via a covenant for example, and long-term investors could be encouraged into the market. But once the legal framework for indefinite rental contracts has been created, the policy incentives required would be no greater than those used in recent years to generate social housing or support private buyers.

Transforming the incentives

Taken in the round, this approach could provide people with a set of financial products offering investments, legacies and comfortable retirements, whilst combining the best aspects of both home ownership and renting: security of tenure, plus the freedom to move house rapidly and cheaply. Like some of the ideas in our previous paper, that flexibility could support more efficient use of our housing stock, whilst boosting labour mobility and thus supporting British businesses.

Above all, it could disentangle Britain's houses from our investments, making homes more affordable whilst redirecting capital into more productive activities. For decades, we've tried to keep up with demand in our housing markets – but as a player in the market, government is dwarfed by far bigger forces. So why not try instead to redefine the game, adjusting the market forces themselves?

For a country that leads the world in financial services, we have a rather damaging addiction to bricks and mortar. Let's play to our strengths instead – and reimagine the way we manage our housing market.

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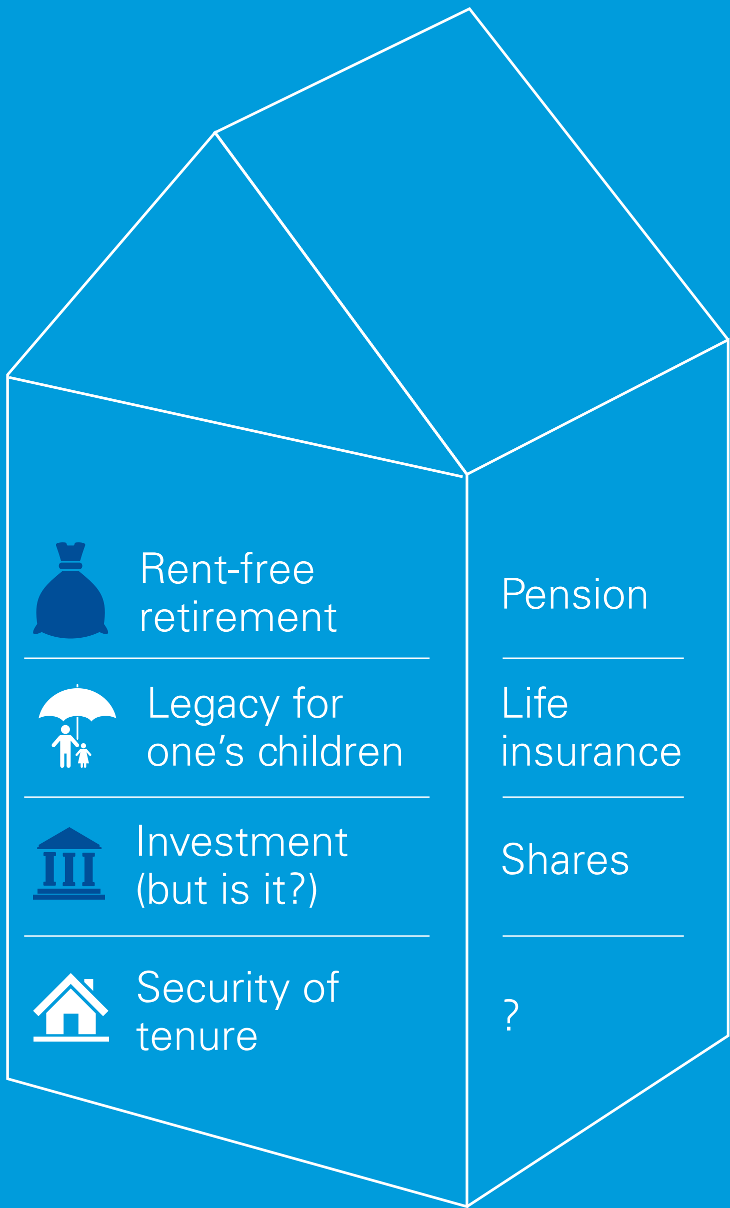
Home ownership provides a meal deal of benefits, most of which can be switched for a financial service.



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