The housing gap

The growing human cost of not building enough homes

July 2013

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Contents

Series introduction

This series of papers examine the current conditions within the UK housing sector and will demonstrate that improvements need to be made to encourage further house building.

In the 1950s the UK built an average of 354,584 homes per year, but between 2000-2009 the annual average stood at 191,325 and has declined further due to continued challenging economic conditions.

This occurs at a time when the ONS is projecting the formation of approximately 260,000 extra UK households - person(s) who have an accommodation as their only/main residence - per year. UK house building in 2011 on the other hand has fallen to approximately 140,000 homes. The need for housing is therefore forecast to be considerably higher than current house building provision. Given the difficulty individuals are already having in purchasing properties, this housing gap will only worsen problems going forward.

Currently, there are already pressures on the UK housing stock with a significant number of households on waiting lists for social housing, in overcrowded living conditions or living in temporary accommodation. The housing gap will further exacerbate these existing issues.

Furthermore, analysis shows that there is forecast to be a growing disconnect between this decreasing supply of house building and demand. This will compound the already long standing problems of the housing market, such as house price inflation, raising further question marks over the ability of the housing market to function in the future.

This series will argue that radical reform of the housing market is needed to rectify these growing problems with a higher priority given to the issue of housing reform and house building by government and all political parties.

The solution this series will advocate takes a sophisticated approach to tackling the housing gap and aims to account for individual's preferences, local needs, financing, planning and the provision of infrastructure to developments.

This series of papers looks to analyse, debate and suggest how a possible future model for the development of housing in the UK could operate

Abstract

This paper is the first in ACE's housing paper series and explores in detail the conditions within the UK housing market.

It finds that there is a serious housing gap (where the number of households formed outstrips houses built) looming in the UK. The paper argues that unless the growing disconnect between supply and demand is tackled through major house building, the housing gap may prove potentially irrevocable. Such a failure to tackle this housing gap would have serious social and economic consequences for the UK.

The analysis in this report reveals that by 2021 the UK will have developed a housing gap of £185bn, the equivalent to 886,000 households, requiring housing to be built on the scale of a city twice the size of Birmingham. This additional gap on top of the already tight conditions in the housing market will if unchanged lead to a future where millions of people in the UK will be unable to afford to own a home.

This analysis highlights an urgent need for the housing gap to receive greater priority from government and all political parties, as well as the need for a new housing model to allow such increased house building to occur.

Executive summary

A potentially irrevocable housing gap (where the number of households outstrips houses built) is looming in the UK. Unless tackled this housing gap will see, at a conservative estimate, hundreds of thousands of extra people in the UK unable to own a home. The analysis in this report reveals that by 2021[1] the UK will have developed a housing gap of £185bn, the equivalent to 886,000 households. This growing housing gap, will add ever greater pressures to existing housing stock, as well as the ability of most to afford a deposit or access a mortgage. As such, the failure to tackle this housing gap through increased house building will not only remove the aspiration to own a house for most, but have massive widespread social and economic consequences for the UK's future. The urgent need for both a new model to allow the increased house building the UK needs and for housing to move up the government's priority list is greater than ever.

Projections[2] from 2011 onwards show that the number of households – person(s) who have an accommodation as their only/main residence- formed in the UK has outstripped the rate of current and historic house building. In 2011 this housing gap projection stands at the equivalent of 88,000 households moving to 886,000 households by 2021. To put this into context, this housing gap projection in 2011 is equivalent to the number of houses in Portsmouth, jumping to one the size of Kent by 2018, twice the size of Birmingham by 2021.

Given the definition of a household, it is also possible that the housing requirement to house all of these extra households is underestimated. This is because any persons sharing a living or sitting room, such as multiple occupancy houses, would be considered a single household, but in reality would want to buy several houses. This may mean that the numbers of houses needed to tackle the housing gap, as well as the individuals caught up in it, could easily cross into the millions by 2021.

The extra strain caused by the growing housing gap will exacerbate the problems the UK already faces on its current housing stock. As a paper by Shelter[3] highlights:

"There are a number of aspects that point towards a historic and continued housing shortage, with 1.7 million households waiting for social housing, approximately 650,000 households in England are considered overcrowded, and an further 49,000 households were living in temporary accommodation arranged by local authorities."

As a result, the extra burdens that the housing gap will add to a chronically pressed housing stock may lead to a choke point being reached. Government will be forced to take radical action on an already stretched welfare bill, e.g., as rent bills rocket and housing benefit continues to increase rapidly.

The pressures on the ability of those seeking to enter the housing market, in terms of ability to pay deposits and to access a mortgage, will also increase drastically in the future.

For example, this report takes median wages and house prices, and based on a simple rolling average calculates that if an individual saves 10% of their income (which is significantly above the current savings ratio of around 7%), and wishes to secure a mortgage with a 25% deposit (significantly below the 2010 level of 35%) they still would not have managed to save a sufficient deposit by 2050.

If the same assumptions are used for a couple, it is revealed that they would need to have been in a stable 22 year relationship, saving 10% of their combined disposable income every year to accrue a 25% deposit.

These conditions going forward will not only be limited to first time buyers, but a wide range of individuals. From young families to average earning households, measures such as turning to parents for help to get on the property ladder or upsize an existing property[4] are increasingly common and necessary.

And as supply is constrained further by the pending housing gap, the pressures on these demand side problems of being able to provide affordable deposits or accessing a mortgage will only increase.

Such worrying implications for those with aspirations of home ownership are being caused by the growing disconnect between demand and supply that occurs in the current housing market. This disconnect has led to significant house price inflation over the past 35 years[5]. House price inflation during this period has seen prices rise by 2035%. To put this rise into context, wages over this period increased by 936%[6]. Even if housing is looked at as an investment (as it is by many today), the FTSE 100 over the period 1985 to 2010[7] increase by 318%, but house prices increased by 709%.

The potential negative repercussions of this house price increase goes far beyond an individual's aspiration to own a home. The wider consequences for not only personal wealth but the cost of government pensions and welfare bills will be significant, if the increase is not tackled.

For example, as house prices increase a shift away from home ownership to renting will follow, with the ONS 2011 Census stating that the last decade has seen the first rise in the percentage of households renting, since 1918[8]. If this shift away from home ownership continues, government will not only need to reassess its housing benefit model, it will also need to reassess how it targets services such as health care and education to families and individuals as the frequency of house moves increase.

Whilst recent data has pointed to improving conditions within the housing sector, as will be demonstrated in this paper, it builds on a dangerous longer term trend of significant price increases and under provision of housing. Without serious action, there is a significant chance that a future housing bubble will be created, potentially leading to another more serious subsequent borrowing crisis.

Surely if housing were any other commodity, government would have taken action, to address the seriousness of the supply shortage? Yet successive governments have missed or failed to deliver on housing targets. For example, the Telegraph reported in 2010 that House building target were missed in every region in the country over the previous eight years[9].

Now, however, with missed housing targets turning into a real housing gap where hundreds of thousands more in the UK will not be able to buy a home, the human cost of not reforming the housing market and increasing house building has grown massively.

A good comparison to raise here is the seriousness that government has given to tackling the energy gap. The energy gap (the gap between energy generation and energy demand) was estimated by Ofgem to require a £200bn energy infrastructure investment by 2020 only one year shorter than the aforementioned housing gap. The energy gap has now been deemed to have reached a point where serious policy action is needed. As the Prime Minister outlined in April 2012:

- "In Britain today we face not only a looming energy gap, but a reality gap - between Government rhetoric and actual reality. We can't close one gap without closing the other first[10]"

Even though the housing gap will reach a similarly daunting £185bn, however, there are no signs from government of an increased focus, or a sophisticated or innovative response that seeks to increase the UK's house building to tackle the gap.

This primacy of supply over demand side problems in creating this housing gap, i.e., lack of house building being the main problem, is the critical point that this paper will argue.

As this report will discuss, whilst demand conditions may have tightened, and measures such as the Help to Buy[11] scheme have launched, the fundamental under provision of the supply of housing is the primary factor behind the UK's housing sectors growing structural problems.

The government in June 2013 recognised the scale of the supply issues in the housing sector announcing that it would provide significant support for the housing market. This consisted of a total of over £5.1 billion of investment to support housing in England between 2015-16 and 2017-18. Including £3.3 billion of new funding for affordable housing between 2015-16 and 2017-18 and certainty on social rents up to 2025-26. This is anticipated to provide over 200,000 new affordable homes by 2018-19. However whilst this announcement is for England alone, it still falls significantly short of the 886,000 homes required in the UK by 2021 just to house forming households. In addition this does not help to ease current constraints in the supply of housing.

This is not to dismiss the importance of demand side problems on housing, e.g., the ability to get a mortgage or put down a deposit; nor to ignore their interdependent relationship with supply side issues. The key to solving the housing gap, however, will be primarily through building more homes.

This paper will also note that the failure of supply to react to such an increase in value shows that the housing market is not connecting supply and demand as a well functioning housing market should.

This disconnect between supply and demand has been further stretched by the financial crisis, which has subsequently changed the market dynamics of the housing sector for a number of reasons. These include amongst other things, the availability, access, cost and willingness of consumers and companies to take on credit. For this reason, the likelihood of heading towards future crises seems ever more likely, with the housing market not able to correct itself by properly aligning supply to demand.

Radical reform is therefore needed and, given the scale of the challenge, needs to be bold in its approach. Innovative thinking and policies are needed within the housing sector to address the ever-shrinking number of homes being built and the rift that has become apparent between supply and demand.

This situation, however, is made more challenging by the increasing disparity between the older and wealthier generations, which are asset rich and the younger generations and those on average earnings, which are asset poor. As this paper will argue it makes policy formation more complex as any shift in the price of housing has to occur at a rate that does not have a negative effect on the confidence of the market.

Within this, policy must consider local needs, infrastructure requirements and how to encourage the use of brownfield sites and not just promote greenfield development.

The extent of house building needs to increase, but also has to take place in a manner that is forward thinking, responsible and sustainable. Any policy that encourages the mass construction of poorly developed housing will not only repeat the mistakes of the past, but also increase the cost to future generations as demolition and replacement will be required.

Given all of the challenges, it is time for central and local government, public bodies, and the private sector to innovate, discuss and develop a new way. One that will provide confidence, certainty, availability, affordability and importantly also attempt to, over time, slowly shift the market to a sustainable rate of house price growth. This will therefore prevent the housing market precipitating the UK's next wider economic crisis. This paper sets out the background behind the problems to show the issues that any new housing model must resolve to best inform a solution to tackle the housing gap.

The UK is failing to meet its housing needs

Introduction

The UK is facing a number of potential economic challenges. One of which is the real prospect of a housing gap. Using projections for the number of households and a 10 year rolling average for house building it is revealed that England is facing a housing gap above and beyond the UK's current rate of house building that equates to approximately 886,000 homes being needed by 2021 that are not being built. Using the mix adjusted price from DCLG for 2010, this places the market value on this gap of £185bn. To put this in comparison policy has shifted significantly to meet the estimated energy gap of approximately £200bn.

HOUSING GAP £185BN OR 886,000 HOMES

The analysis occurs over the period 2011 to 2021 to ensure the accuracy of the forward projection, and could be considered cautious in terms of its approach as house building over the entire period is estimated to average approximately 180,0000 homes per year, well above the current annual rate of house building which stands at approximately 140,000 homes.

Given the definition of a household12, it is possible that the housing requirement is underestimated. This is because any persons sharing a living or sitting room such as multiple occupancy houses would be considered a single household, but in reality would want to buy individual houses.

Such a gap would have a significant effect on social conditions, with the human cost of the under supply of housing resulting in families living in cramped or inappropriate conditions, and with younger and medium income families stuck in the rental market.

Economic events from the past five years have demonstrated how markets can and do fail. Within this the role of government in ensuring the integrity and stability of markets has also been something which has been questioned further.

This gap, alongside the significant increases in house prices over the past 35 years in the UK shows how serious an issue the housing market is becoming for those who wish to purchase a property. With, young families, first time buyers and those on average or below incomes becoming more and more restricted in terms of accessing the housing market.

However, the housing sector has always been a difficult market for policy makers to influence. The combination of financial commitments for the individual, planning regulations, financing of the development, legal systems and balancing social needs and demands against sustainable long term policy objects makes changes difficult to implement.

For example, it is interesting to note that private sector house building has remained broadly consistent since 1960 providing approximately 167,000 houses per year. Despite all the policy changes that have taken place over this period.

If an average is taken of each decade since 1950 it is found that house building fell to an all-

22 YEARS TO SAVE A DEPOSIT

time low during the 2000-2009 periods with the average being 163,260 homes less per year than the period 1960-69.

This lower provision of housing alongside a potential future housing gap, will result in no other outcome than further inflation of house prices. As this report will show, using simple assumptions even a couple who both earn the UK median wage will need to save 10% of their combined disposable income for 22 years to be able to save a 25% deposit. This shows how house price inflation is no longer just locking poorer families out of the market, but also single first time buyers, young professionals, and both couples in their 20's and 30's. If allowed to continue the UK will have to accept that this issue is going to begin to affect a much larger proportion of the market in general.

Some data such as affordable housing provision, whilst initially providing some positive signs such as provision continuing to increase each year following the financial crisis and recession, in reality is not as positive as it may seem. This is because this trend is only likely to have occurred because of the nature through which social and affordable housing is provided, with developers continuing to provide affordable housing as part of commitments made prior to the financial crisis and recession on projects that were unable to be halted. In addition, the scale of the provision of affordable housing is currently not on a scale anywhere near sufficient enough to provide the number of homes that would be required to significantly improve affordability within the housing market.

The housing sector and housing policy needs reform to better link price levels to the supply of housing, accounting for local factors and encouraging a responsive market. Failure to undertake such reforms, is likely to result in the majority of individuals born after 1990 not being able to afford to purchase a home until at least 2030, if at all.

A recent report by Shelter[13] shows the severity of the current situation regarding house price increases. By applying the rate of house price growth to a number of food products since 1971 they calculated that items such as a chicken would cost £51.18, compared to the a price of approximately £4.00[14]. Whilst there are some differences in the way in which commodities and assets are treated by individuals, this increase helps to demonstrates the true extent of the disconnect that has occurred between supply and demand within the housing sector.

It is important to remember that the issues surrounding price increases and constrained supply are not new ones. This is demonstrated by the 2004 Review of Housing Supply[15] which found that if Government wished to achieve lower real house price trends it would have to build between 70,000 and 120,000 additional private houses every year. Yet house building in 2011 was 30% lower than in 2004, not higher. Whilst, this is not completely unexpected that house building would be lower during a recession, even accounting for the boom period in building the UK is not providing enough housing to meet the Barker reviews base line scenario.

Just under ten years on from the Barker review, housing supply remains an issue and demand conditions have deteriorated. As such, the potential for serious societal consequences of a lack of housing given changes demographics and population growth continues to build further tension within the housing market.

Some will point to a shift towards a rental based market. However, as property prices increase and reduce the prospects of buying, they also increase rental demand. This is because those priced out of buying a home, are the majority of the time likely to rent as the alternative.

As such, rental prices rise and the market favours short term contracts where prices can change more often. Given this, why would the current rental market shift towards a model of long term contracts that were good for long term certainty? The simple answer is it won't.

In addition, over the longer term, even a rental market can't operate without adequate supply. A continued housing gap such as that discussed in this paper, will not only erode the stock available to sell but the stock available to rent. Therefore eventually constraining even the rental market, encouraging further price inflation.

The question that has to be asked is that if constrained enough, for a long enough period would the housing market create a position where the majority of individuals are not only unable to buy a property, but also cannot afford to rent?

This suggests the solution is going to come from ensuring that land is made available for development, that developers enough housing to meet supply, and that councils can provide the relevant infrastructure and local services with a reasonable level of local consultation.

The next section of this paper will explore in more detail some of the figures behind the issues highlighted above.

Analysis of factors influencing poor supply in the housing sector

Data on house building reveals that from the period 1990 to 2003, the supply and provision of house building in the UK remained consistent each year, with an increase in provision during the 2004-2008 period before the financial crisis and recession. Following this both, private and housing association[16] provision fell significantly.

The housing gap

The DCLG and ONS also produce a series which projects the number of households[17] in the UK. By 2021 the number of households in the UK are projected to grow to 29.2 million, with the number of households due to rise by 2.6 million or 260,000 per year[18]. This rise will therefore create additional demand for housing.

Using historical house building it is possible to create a simple forward forecast based on a ten year rolling average and compare this to the household projections mentioned previously.

The results show significant cause for concern with a clear and sustained housing gap going forward as house building does not keep up with demand.

260,000 NEW HOUSEHOLDS FORMED PER YEAR UNTIL 2021

The housing gap

Source: ONS, DCLG

This gap equates to approximately 886,000 homes being needed by 2021 that are not being built. Using the mix adjusted price from DCLG for 2010, this places the market value on this gap of £185bn.

To put this into context, this housing gap projection in 2011 is equivalent to the number of houses in Portsmouth, jumping to one the size of Kent by 2018, twice the size of Birmingham by 2021.[19]

To put this in comparison of other areas where investment is required, DECC estimate that Electricity Market Reform policies should help to address and deliver £200bn of investment by 2020, thereby starting to address the energy gap. However, whilst the energy sector has been seen as a priority for policy makers, and government given the cost and societal implications of the market failing, the housing sector has not.

2021, HOUSING GAP WILL BE TWICE THE SIZE OF BIRMINGHAM

Whilst the UK can import energy supplies, and even resort to using less efficient and cost effective older generating capacity it cannot import housing. This therefore makes the lag between policies being formed and implementation and investment occurring even longer in the housing sector.

It is also important to recognise that this gap has only been calculated up until 2021. Given the time it takes to reform, implement, plan, develop and sell housing though it is likely that this gap will continue to contribute to a continually growing problem with the supply of housing.

Another way to explore the extent of the supply side issue is to calculate what other sectors would look like if the performance of their supply matched the profile of the housing sector.

For example, in the already mentioned energy sector, this would mean that between 1951 and 2010 we would have only built 39% of the UK current power station capacity[20]. This demonstrates the extent to which supply has been constrained within the housing sector.

Another example that could be explored is that of the car industry. This for most households along with the purchase of a house will constitutes one of their largest capital purchases. Again if you take the number of houses in 1951 and apply the housing sector's growth rate between 1951 and 2010 to the private car market over this period, it is revealed that by 2010 there would only have been approximately 8 million cars registered. This is significantly below the actual figure for 2010 of over 27 million, and even allowing for households to own two cars, supply would still have been 10 million lower. Such constrained supply in this market would have had a significant downward effect on growth, and would have been unlikely to be tolerated by government given its current focus on improving economic growth.

These comparisons demonstrate the importance of reacting to issues when they are identified yet housing is a policy area which is currently lacking innovation. For example, policies developed over the past 50 years generally have focused on supply or demand with little relationship between the two. Further to this the UK has never clearly set out where local authority and central government's role lies in the delivery of housing policy. The system has the signs of heading to a breaking point, where there will be significant social consequences, and so action is needed.

It is also important to recognise that issues within the housing sector do not effect society or regions equally, hitting first time buyers, young families and those on average or below incomes harder. Therefore policies need to be able to tailor themselves to local market conditions, average wages, land and property prices etc.

Issues with house building and developable land are not new problems

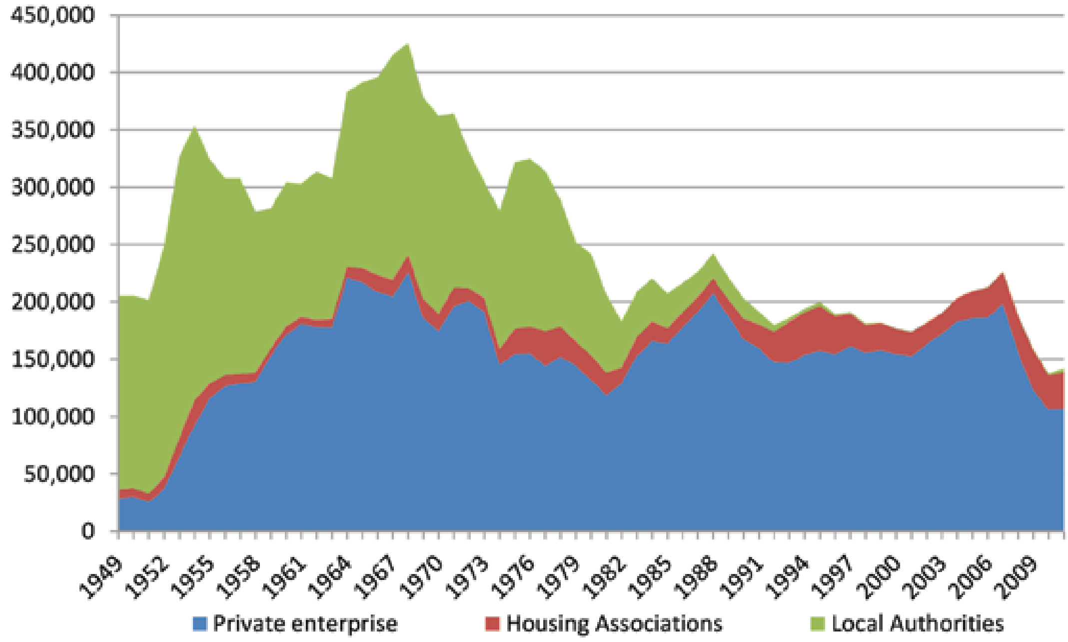
This fall in house building not only reflects the tighter demand conditions as a result of the financial crisis but also the actions of house builders to re-evaluate the value of their assets and pay off debt where necessary. Developers therefore will have a number of sites that were purchased prior to the recession which will require future increases in house prices to make them profitable for development.

LAND BANKS EQUAL 281,993 HOMES

This is because companies will currently be sitting on a number of sites that were purchased at higher prices prior to the recession which are now unprofitable given declines in house prices. Estimates in 2011 put the size of developers' land banks (sites suitable for house building) at the equivalent to 281,993[21] homes. Based on the number of houses completed in 2011 this would be the equivalent to two full years of house building activity.

If the housing market were operating more efficiently, with lower house price inflation and long term policies providing certainty, this would minimise the likelihood of significant boom and bust cycles and reduce the incentive for developers to hold such land banks.

House building



Source: DCLG

However, more interestingly if we look at data from the period prior to 1990 it is revealed that house building has fallen significantly. Local authority provision prior to 1990 contributed significantly to the provision of the housing stock.

An example of how policy has shifted was explored in a recent report by the IPPR[22], which shows that there has been a significant shift in policy with local authorities shifting from supporting affordable housing by using supply side grants. This resulted in policies shifting from one of increased building to one of subsidising rent (shifting from supply to demand).

The result of this change is that in the latest spending round approximately £4.5 billion will be spent on grants to support the building of new affordable homes, which compares to £94 billion spent on policies such as subsidised rents.

If an average is taken of each decade since 1950 it is found that house building fell to an all-time low during the 2000-2009 periods with the average being 163,260 homes less per year than the period 1960-69.

This suggests that the trend in the market is one of the supply of housing becoming more inelastic, and provision decreasing, with it, therefore encouraging significant price increases. This effect on prices will be discussed later in this paper, with evidence from price increases supporting the view that supply is becoming increasingly restrictive and disconnected from demand.

Period	Annual average
1950-59	276,518
1960-69	354,584
1970-79	320,160
1980-89	220,618
1990-99	192,654
2000-09	191,325

It is also interesting to note that private sector house building has remained broadly consistent since 1960 providing approximately 167,000 houses per year. However, this does call into question how effective policies are to boost private house building given they have had no significant impact over the period. Also, whilst traditionally private housing was mostly owned by the person occupying the building, this is now not as prevalent with the UK having a much larger number of private landlords and rented properties.

This is an area where housing policy continues to fail as it has not recognised the significance of the private buy to let investment market. The majority of homeowners will purchase a property, move infrequently, and only extract any capital gains as they downsize for retirement. Investors, however, are driven by capital and rental returns. As such higher levels of price inflation and shorter contracts are favoured as this can maximise the returns. Whilst having such investors is not necessarily a problem, if house building is constrained these investors over time account for a larger degree of the market and so aspects such as property prices will become increasingly disconnected from local conditions, and more reflective of local and international investors.

2011 THE UK BUILT APPROXIMATELY 140,000 HOMES

For example, recent house price growth in London has been driven by significant interest from international investors with sites such as the new Battersea power station, attracting significant interest abroad. Whilst this has brought significant investment into the area this has meant that a significant amount of housing is not available to purchase for individuals that live in London. Such international demand given the UK's current low level of house building will only further exacerbate the disconnect between supply and demand, and reduce the ability for individuals to purchase a property.

The role of affordable housing

Looking more closely at the provision of affordable housing since 1990 when local authority house building had declined, it is revealed that between 1997 and 2005 the provision of affordable housing was relatively low with an average of approximately 38,000 additional homes provided per year. Of these most were delivered within the social rent area[23].

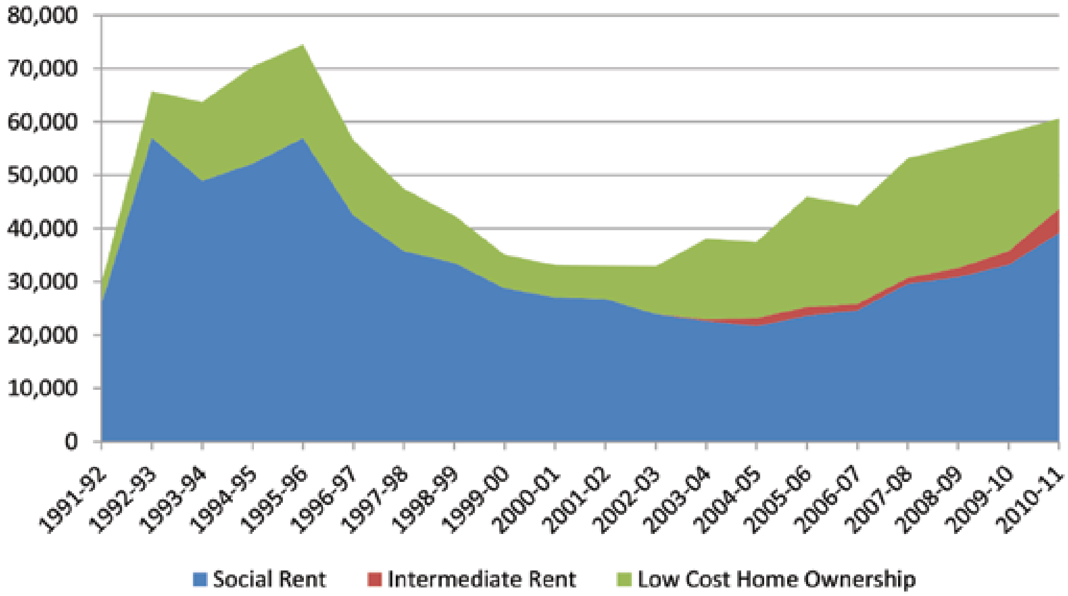
Between 2006 and 2011 affordable housing provision increased each year despite the financial crisis and recession. This means that on average over the period, 54,000 additional affordable homes were being provided annually, with the 2010-11 period hitting 60,626. The highest level of provision since 1995-1996. To put this in context, between 2011 and 2015 the Mayor of London has set a target to build 50,000 affordable homes.

This trend is likely to have occurred because of the nature through which social and affordable housing is provided. For example, local authorities in the period 2002 to 2007 became increasingly proficient at negotiating social housing provision under Section 106 agreements. This alongside, continued increases in house prices made negotiating with developers an easier task. Given the lag between development plans, negotiating Section 106 agreements and developments being constructed it is likely that the continued increase in affordable housing in 2009-10 is due to commitments made prior to the financial crisis and recession on projects that were unable to be halted.

However, there were also a number of projects where the reduction in price in the housing sector alongside the negotiated affordable and social housing provision under Section 106 has in current market conditions made sites unprofitable and so development has ceased.

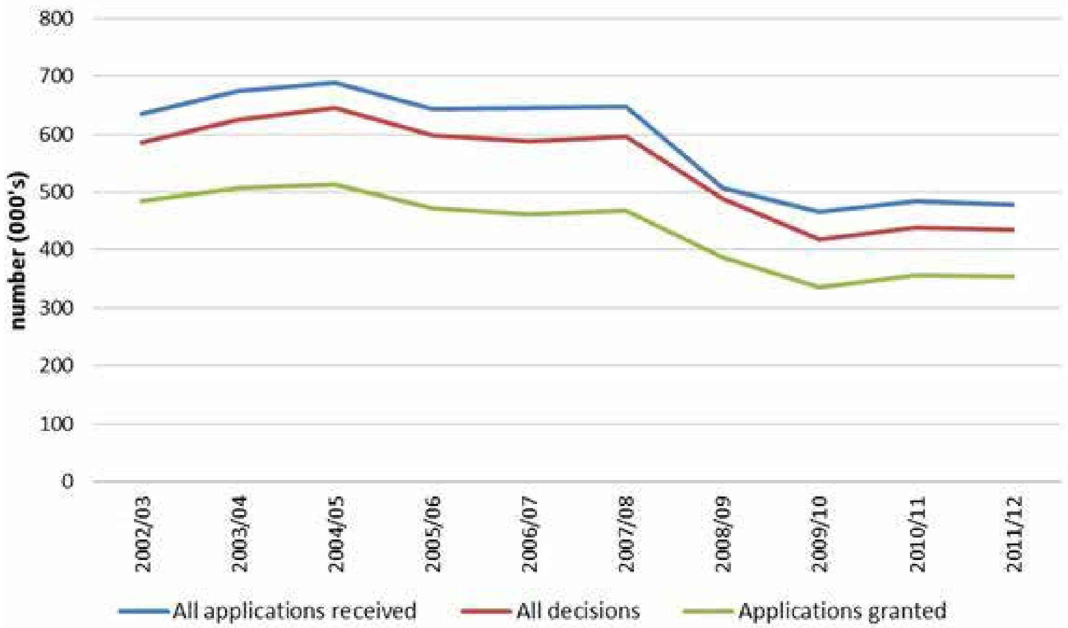
As such, one would expect this upward trend in affordable housing provision to reverse unless there is significant intervention from Government going forward. Government has recognised that there are issues in this area which is why they launched a consultation on the ability of developers to renegotiate a number of section 106 agreements to improve the prospect of restarting development.

Additional affordable homes



Source: DCLG

Are land and planning regulations restricting the market?



Source: DCLG

As can be seen from the table below between January and March 2012 the percentage of applications granted varies from 81% in London to 93% in the North East. The overall average for the UK across all the regions is 88%.

Planning decisions by region, type of authority and speed of decision

Authority/region	Applications granted	Major decisions within 13 weeks (%)	Minor decisions within 8 weeks (%)	Other decisions within 8 weeks (%)
North East	93	65	73	83
North West	90	52	68	80
Yorkshire and the Humber	87	60	71	84
East Midlands	89	47	72	83
West Midlands	89	63	71	80
East of England	85	57	72	85
London	81	31	60	74
South East	86	60	70	84
South West	90	56	66	79
Government Office Regions	87	53	68	81
National Parks	89	55	69	81
England	87	53	68	81
Non-Metropolitan districts	88	57	69	82
Metropolitan districts	84	48	66	78
Unitary Authorities	88	54	69	81
Urban Development Corporations	93	19	-	50

Importantly there are also measures for the percentage of major, minor and other projects where decisions are made within either 13 or 8 weeks. Across the UK it reveals that 52% of major projects are approved within 13 weeks, and both 69% of minor projects and 79% of other projects are approved within 8 weeks.

This would appear to suggest that the decision process within the planning system is not the main source of delays. Instead it is more likely to be aspects such as making amendments to plans, consultation with local residents, resubmitting applications and putting together proposals for development.

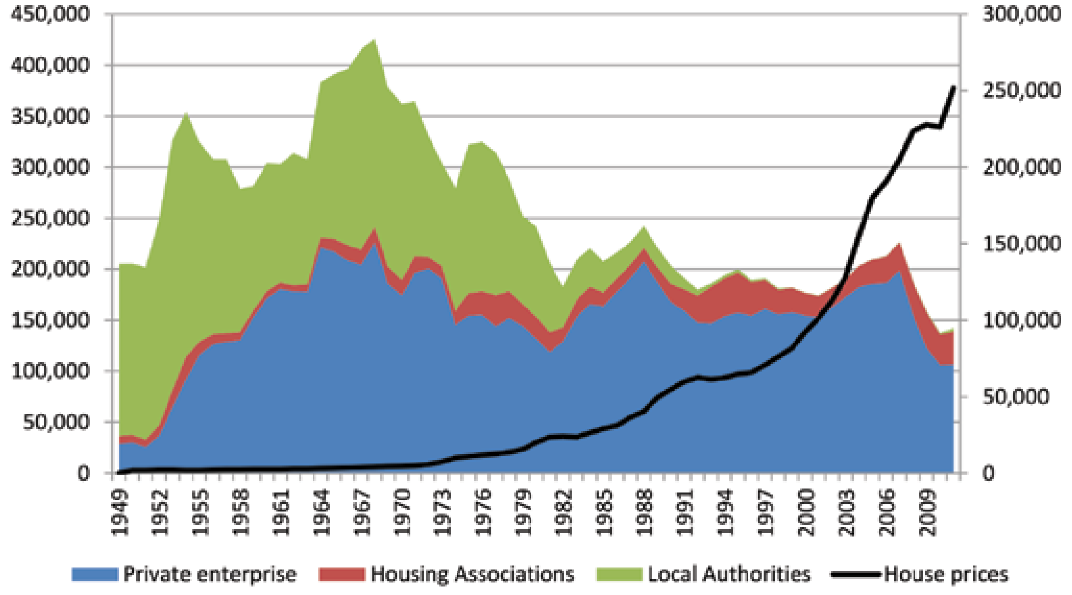
Addressing issues that slow down the system will help to enable the supply within the market to respond slightly quicker but ultimately the development of new properties will depend on the commercial viability of a site (acquiring the land, planning and process costs, build costs, number of units, sale price, social housing requirement, environmental considerations etc).

Forget affordable housing, is any housing affordable?

Of critical importance within the housing sector is the need to link housing price to the level of supply and determine how connected and responsive the market is to price variations in terms of the provision of housing.

If the DCLG simple annual house price series is added to the previously discussed chart for historic house building it can be seen that house prices started to undergo significant increases as the average annual provision of housing (both private and public) fell below 250,000 properties a year.

House building and house prices

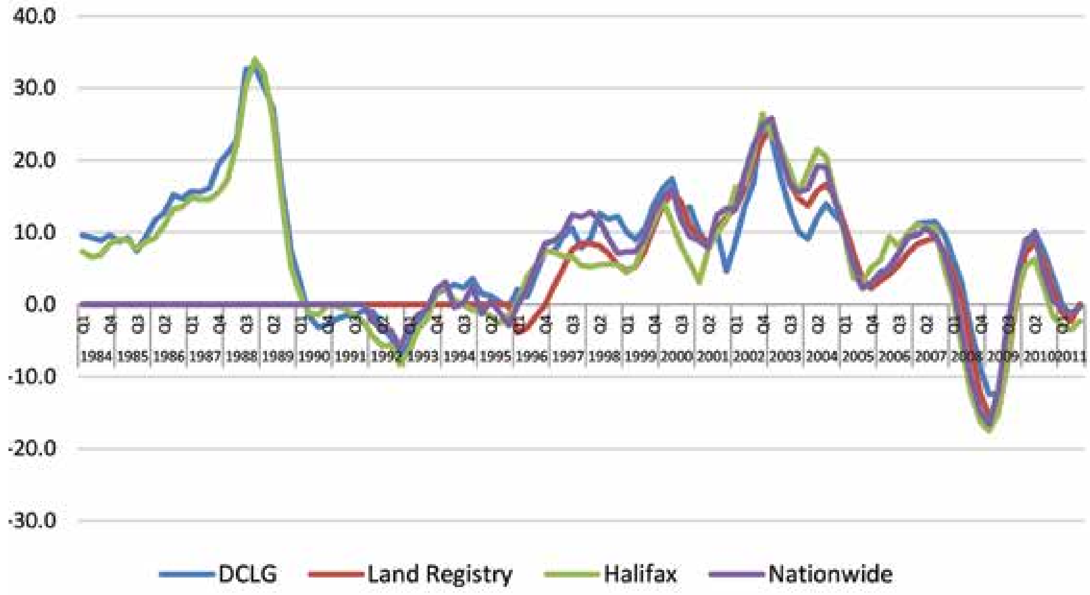


Source: DCLG

At the lower average rate of a provision of 190,000 since 1990, it can be seen that house prices have continued to rise. This therefore suggests that there is a strong link between the annual provision of housing, and price. Given this, if prices are increasing significantly the conclusion has to be drawn that the provision of housing is significantly below what is needed to satisfy demand.

This increase in prices does not appear to be an anomaly. A sustained increase, is also shown in series from Halifax, Nationwide and Land Registry showing similar trends and growth rates since 1990.

Annual house price growth



Source: DCLG, Nationwide, Land Registry, Halifax

This raises the question as to what rate of house price growth is acceptable and sustainable given individuals' ability to save and enter the market for a given level of housing supply.

A recent report by Shelter[24] shows the severity of the current situation regarding house price increases. By applying the rate of house price growth to a number of food products since

1971 they calculated what their current price. It was revealed that:

- A 4-pint carton of milk would cost £10.45 (currently £1.29[25])
- A chicken would cost £51.18 (currently £4.00[26])
- A box of 6 eggs would cost £5.01 (currently £1.40[27])

This meant that the average weekly expenditure on food for a family of four would be £453.23. Such levels of inflation would not be tolerated by government in other industries, so why is it in the housing sector. For example:

- Energy prices are consistently reported as being too high and government has implemented policies to encourage competition and investment to lower long term costs.

- Regulators such as Ofwat actually have consumer affordability and price at the heart of their regulatory remit to ensure that water remains affordable, whilst allowing sufficient investment.

- Government can alter tax policies to help counter price effects. Recently the government has cancelled and delayed fuel duty increases given the cost of fuel would be deemed as damaging to the economy at a time when household budgets are constrained.

This question is not a new one. This is demonstrated by the 2004 Review of Housing Supply[28] which found that if Government wished to achieve a real house price trend of 2.4%[29] it would need to build an additional 20,000 private sector homes per annum on top of their baseline scenario of 140,000 private housing starts and 125,000 completions in England.

If Government wanted to achieve a lower rate of 1.8%, an additional 70,000 private homes and 17,000 social homes, together with 1.1% real growth per annum an additional 120,000 private homes and 21,000 social homes would need to be built.

These supply scenarios are significantly above the average since 2004-5, for private enterprise starts in England which currently stands at 114,950, and below the base rate assumed in the 2004 Barker review.

But conditions have changed significantly since the Barker review.

The supply of housing in England has fallen from 146,000 dwellings started in 2007-8 to 84,000 in 2011-12. Alongside this, demand conditions have also changed. Fewer individuals are confident enough given the possible risk of unemployment to enter the housing market, and fewer individuals are also able to borrow given tighter lending criteria. This therefore reduces transactions in the market.

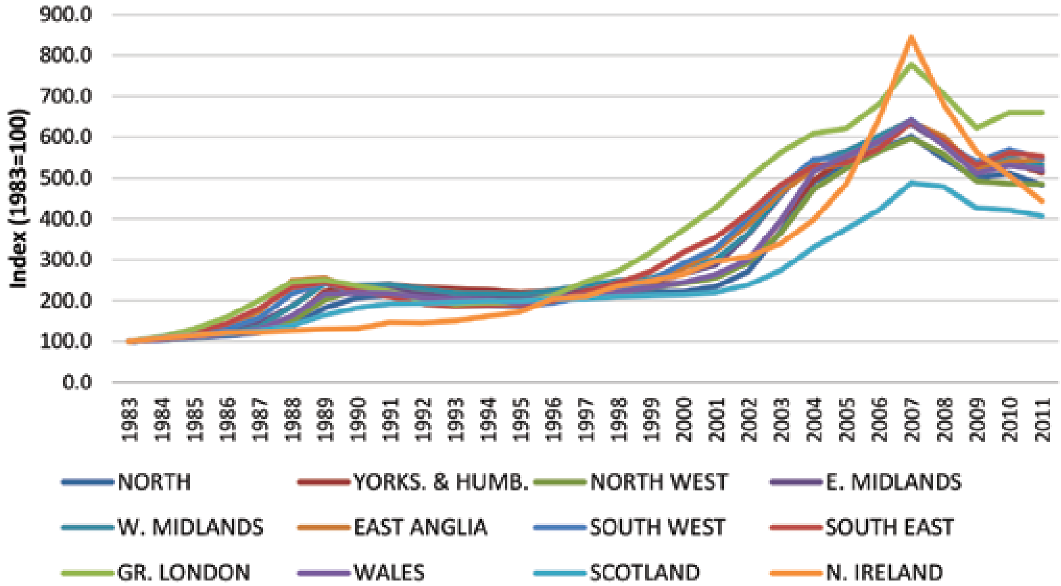
So whilst house prices have fallen and interest rates remain at historic lows helping affordability, there are still significant supply shortages if the government wishes to even meet the original Barker reviews baseline scenario.

So just under ten years on from the Barker review, housing supply remains an issue, having deteriorated to the point that there is the potential for serious societal consequences. Further changes to demographics and population growth will continue to add pressure to the housing market as supply cannot keep pace with demand. Given the experience of the financial crisis, and calls for preventative measures the housing sector should be an obvious target for government to remedy a potential storm of society pressures.

However, it is also important to note that house price increases are not uniform across the

UK. The latest data from Halifax reveals that Greater London is generally above trend and Scotland has been below trend since 2001. Northern Ireland also differs in performance to other regions in the UK with its peak in 2007 likely to be tied to the significant level of foreign direct investment that occurred across the economy.

House price index by region



Source: Halifax

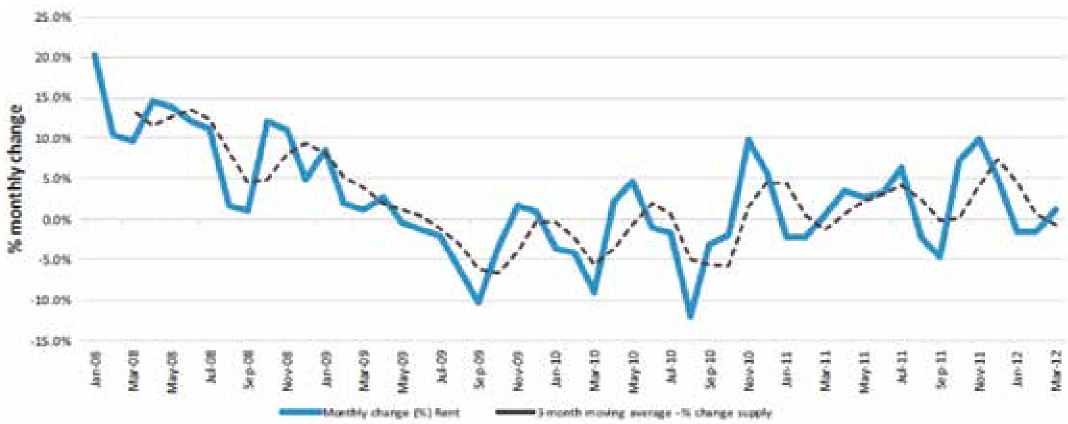
The variation in local and regional prices demonstrates the need to have policies in place that align house building with local conditions. For example, private sector developers will want to build in the areas with the highest prices and greatest return, but these are also likely to be the areas with the lowest land availability and strongest opposition. Policies therefore need to try and account for local prices and provide communities with adequate compensation to drive house building forward.

Don’t forget the rental market

Another dynamic to consider is that of the rental market vs the cost of ownership.

Recent data from Findaproperty.com suggests that whilst the growth in rental rates did cool in summer 2009 and 2010, they are once again starting to rise.

Rent changes



Source: FindaProperty.com

This can have several effects on the property sector:

- It can prevent current individuals that rent from saving a sufficient deposit for the purchase of a property (which will have been exacerbated by tighter lending conditions).

- It encourages investors who are seeking to make profit in the sector as yields increase, but as such, also raises the price of properties for homebuyers such as first time buyers that are trying to enter the market.

- Raising rental prices make the opportunity cost of rental greater as mortgage costs and the investment in property becomes more attractive.

The three factors above alongside earlier discussed aspects such as future price rises above wage increases and credit conditions remaining tighter, further increase the likelihood of rental increases.

Further to this, recent data from the Council of Mortgage Lenders suggests that lending within the buy to let market is improving with gross mortgage lending of £4.2 billion, (33,500) taking place in the first quarter of 2013. By the end of March buy to let lending accounted for 13.4% of total outstanding mortgage lending in the UK.

This is further evidence that despite the recession reducing costs, the base rate being at historic lows and government initiatives such as the Help to Buy scheme the rental market is still seen as a profitable investment. With the low rate of house building, this will continue to inflate prices and make the prospect of home ownership no longer a reality for many.

Whilst the rental market itself is not responsible for the UK housing shortage, and does provide short term flexibility for individuals, it also has currently not provided the type of long term stable contracts that families would require to provide social stability given the difficulty they face in entering the housing market. The short term nature of the UK's market and the uncertainty it can provide for both parties has been highlighted in reports previously, with suggestions that rental contracts could be extended to as long as five years[30].

The recession did provide a period of cooling prices but the UK now looks to be firmly back on trajectory for continued rising rental prices.

Why would the rental market therefore supply long term contracts that were good for stability? The simple answer is it won't. With a significant housing gap developing, rental prices will continue to increase. For investors to make the most of rising prices they will continue to minimise the term of the contract to allow for prices to be reviewed.

However, whilst government could regulate, provide social or subsidised rents this does not solve the actual issue that the housing market is not providing enough supply to meet long term requirements, and is targeting investors rather than traditional homebuyers.

Demand is disconnected from supply, damaging housing prospects

Introduction

Demand conditions within the housing sector have traditionally been considered to be less of a problem than that of supply constraints. However, the financial crisis has highlighted just how quickly demand can be constrained when banks reel in the availability of credit, and increase the conditions required to access finance.

Within a perfectly functioning market you would expect supply to react to such an increase in value, but this has not occurred. This not only suggests that there is a potentially serious disconnect between supply and demand in the UK but also that even allowing for inflation and the recession, that the disconnect between supply and demand is continuing to deteriorate.

As this paper will discuss in this section whilst demand for housing and credit conditions may have been more preferential in the past, the market could hardly be considered as functioning well.

1975-2010 HOUSE PRICES UP 2035%, WAGES 936%

This is shown by the continued and almost exponential increase in house prices over the last 30 years. Within a perfectly functioning market you would expect supply to react to such an increase in value, but this has not occurred.

Individuals are working off price assumptions that are nothing short of dangerous for the economy, as they plan for future house price increases to improve their wealth and fund their pensions. These expectations are based on house price inflation during the past 35 year[31] period which has seen prices rise by 2035%. To put this rise into context, wages over this period increased by 936%[32].

Even if you look at housing as an investment, the FTSE 100 over the period 1985 to 2010[33] increased by 318%, but house prices increased by 709%. If this were any other commodity government would have taken action, to address the seriousness of the supply shortage.

Such increases can only go on so long and with many individuals not planning for any other alternative. If the UK passes this tipping point the consequences for not only personal wealth but the cost of government pensions and welfare bills would be significant.

This shows that there is either a potentially serious disconnect between supply and demand in the UK, or that the market equilibrium is approaching the point where it could be deemed to be socially unacceptable, and even damaging to the future of the UK economy. Either way the system is broken, and should not be allowed to continue along its current path.

Even though there was some cooling of prices through the recession, the UK has a serious issue with the overall affordability of housing.

Given the scale of the disconnect within the housing market, some recent signs that suggest demand is starting to revive could potentially be a more worrying prospect than a continuation of lower demand conditions. This is because higher demand conditions will feed through escalating prices, and as explained in the previous section the housing market so far has been unable to respond on the supply side.

Does the UK want to allow itself to build its next wave of house price increases on the very tenuous ground of ever increasing house price rises?

Throughout the recession without the action of the Bank of England to maintain the base rate at historic lows, and so keeping mortgage rates affordable, a significant number of individuals would have fallen foul of this systemic failure, losing their family home. However, it is also generally overlooked that the action taken to keep mortgage affordable is also the same policy that limits an individual's availability to save for their deposit. This is because interest rates on savings accounts have not only been poor but below the general rate of inflation. As such saving is actually losing an individual's real wealth not building it.

There is also the issue as to how these individuals will react if interest rates have to rise in the future. For those that have benefitted from low interest rates, many may not have factored in how significantly the costs associated with their home ownership could rise.

Again, this going forward poses a risk if individual's income and wages cannot cover the increased cost of mortgage payments.

Demand in the UK housing sector is unlikely to fall, population increases and the prospect of owning property continue to be big influencers in individuals' decisions. However, it is clear is that the UK has got to start addressing how rising demand does not align with the supply of housing as discussed previously.

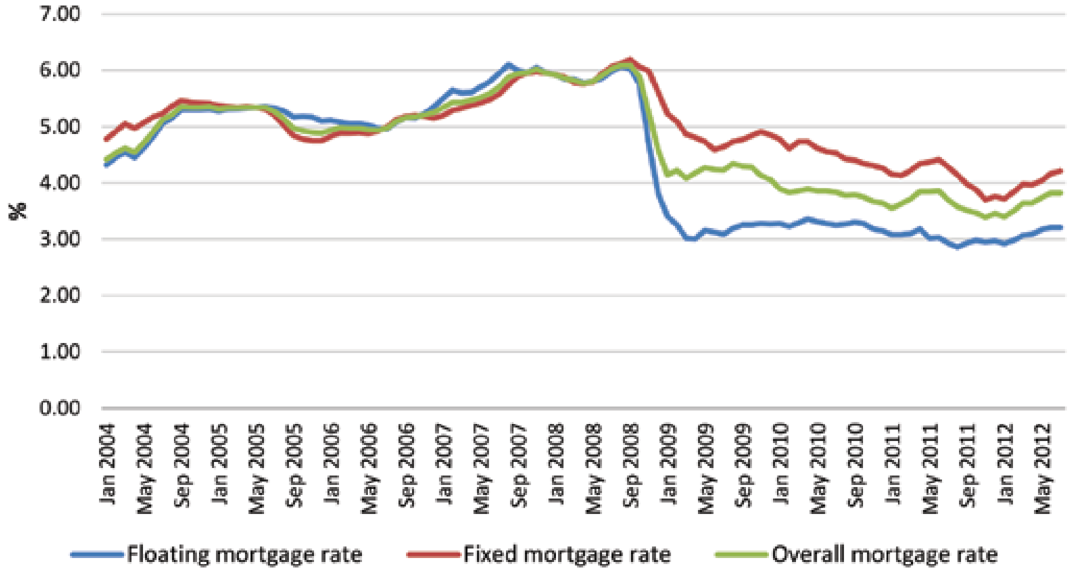
Analysis of factors influencing housing demand in the housing sector

The financial crisis has had a profound effect on the housing sector with the dynamic between consumer and banks shifting considerably. One of the main factors influencing an individual's decisions in purchasing a property is the rate of interest they will pay on a mortgage.

Interest rates

Data from the Bank of England shows that whilst the base rate was reduced from 5% at the start of October 2008 to its historic lows of 0.5% on 5 March 2009 that the effect on the effective costs of mortgage rates was less pronounced. Rates on mortgages fell from approximately 6% (1% above the base rate) to an overall rate of 3.82% in July 2012 (3.32% above the base rate).

Effective interest rates



Source: BOE

This shows that the margin between the base rate and the rate charged to consumers has widened. This widening has occurred as the financial crisis took hold and the confidence and lending between banks fell significantly. This subsequently led to an increase in their cost of raising finance which is then reflected in the margin required above and beyond the base rate. This effect was exacerbated by the need of banks to raise capital to secure their financial positions, as a requirement from Basel post the financial crisis and recession.

These new Basel III rules are designed to ensure that banks hold a greater degree of safe assets and capital against their investments. Whilst the proposals are likely to increase the long term cost of raising finance, they are being put in place to help to ensure the loss of confidence in the sector does not occur again.

Such policies have implications for the long term costs of mortgage lending. This is because banks will have further incentives to reduce the risk of products, thereby restricting supply compared to the pre-financial crisis position. In addition, to which, the cost of holding less risky assets also infers returns are likely to be smaller and so costs of products will have to increase to maintain profitability. This is because banks use products that are higher risk but provide higher return to effectively subsidise the rates they charge on products such as mortgages.

Attitudes to risk that operate in this way are not a new phenomenon. During recessionary periods banks and investors shift their funds towards gold and government bonds as these are considered safer assets. These safe assets types can therefore pay lower returns, as demand for them increases substantially. For example, given the instability in the Euro area and the willingness of investors to find safe havens, Germany was able to sell € 3.9 billion of six-month bonds with an average yield that was negative (-0.0122%[34]). Therefore it was actually costing banks money to hold their investments in these products, and so profitability was reduced.

This is part of the rationale behind schemes such as the UK Governments Funding for Lending scheme[35]. This scheme aims to provide banks with access to cheaper capital in return for them passing the benefit of this reduced costs onto consumers.

Whilst this scheme has had some success in lowering costs, such as the interest rate paid on mortgage products, other areas of the market continue to restrict access. For example, mortgage products following the recession generally require higher set up fees, and requiring larger deposits to secure the best market rates.

These restrictions will be part of the rationale behind the Government Help to Buy scheme which attempts to support buyers with deposit requirements. However, such policies drive demand, and as has been discussed in the paper previously the balance between the supply and demand side of the housing market is already distorted to the extent it has created significant and unsustainable price increases.

Going beyond the immediate period, once the base rate starts to rise, and conditions move away from those instigated as part of the recession and financial crisis, it is unlikely that the UK will not see mortgages return to their level of affordability of the pre-recession levels if the proposed changes to the financial system take place.

Whilst current conditions are important it is also essential that policymakers consider future market conditions. Individuals and affordability are being supported by the current low interest rates but this won't be the case forever. Eventually interest rates will rise, and this is likely to result in significant affordability pressures to those owning a property if real wages are not increasing and able to absorb this change. This may lead to repositions and arrears actually increasing following the recessionary period. As will be explored in the next section of this report, repossessions and arrears have been unusually low in the current recession as historically an increase would have already taken place.

In addition, raising interest rates will also affect those wishing to purchase a property as the cost of doing so increases, constraining affordability further. To avoid this either lending criteria such as deposit rates would need to ease or wage increases would need to account for the increase in interest rates, and higher deposit rates.

Mortgage lending, arrears and possessions

Tighter lending criteria for mortgages, alongside the reduction in confidence of buyers given job uncertainty and inflationary pressures have made it less likely that consumers consider themselves able to afford a property. They are therefore less likely to enter the housing market. The combination of these effects are likely to be the primary reasons behind the fall in the Bank of England's mortgage lending data, with lending falling from above £32bn in January 2007 to £11.3bn in February 2013.

This lower level of demand from individuals due to changes in lending criteria is also important as housing developers will also determine their building rates on current levels of demand and likely short to medium term demand conditions. The longer these subdued levels of activity take place the more likely it is for developers to reduce their future development numbers. This reduction in supply will put further pressures on price rises.

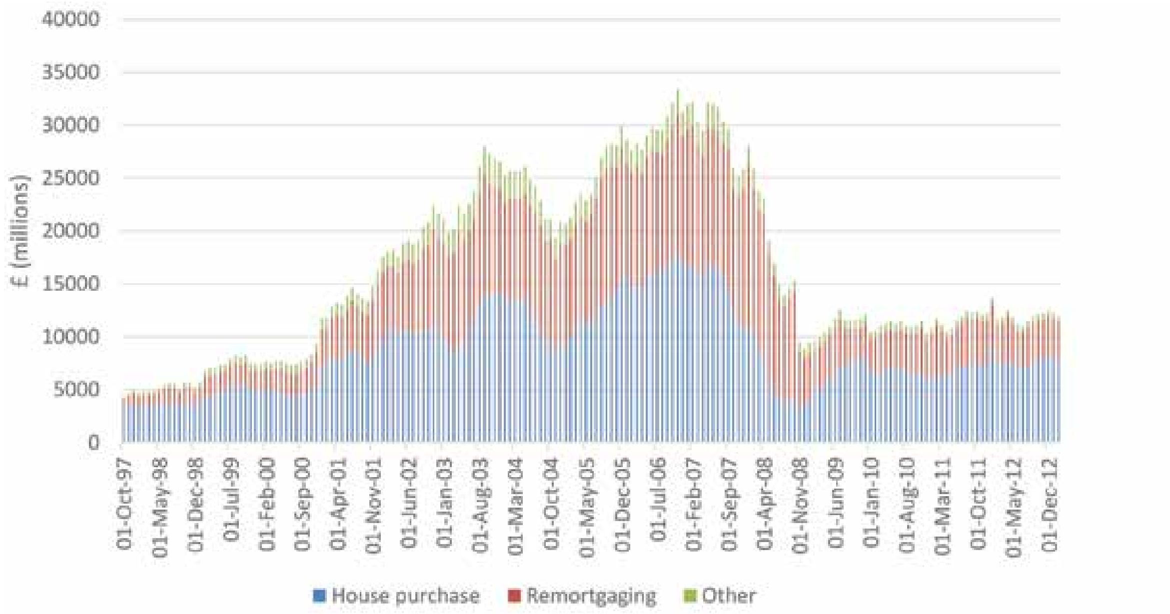
Within a perfectly functioning market you would expect supply to react to such an increase in value, but this has not occurred. This not only suggests that there is a potentially serious disconnect between supply and demand in the UK but also that even allowing for inflation and the recession that the disconnect is continuing to deteriorate.

Data also reveals that in 2008 there were £214bn in value of loans which were approved and house building stood at approximately 190,000. Whereas in 2010, £131bn of loans were approved, yet only approximately 137,000 houses were built.

Over a slightly longer period, the total value of mortgages, re-mortgaging and other loans increased by 639% between Oct 1997 and May 2007, the number of dwellings increased by only 8% and the rate of house building by only 15%.

This clearly shows that supply has not been reacting to demand, and that the disconnect between supply and demand is not a recent phenomenon.

Mortgage lending data



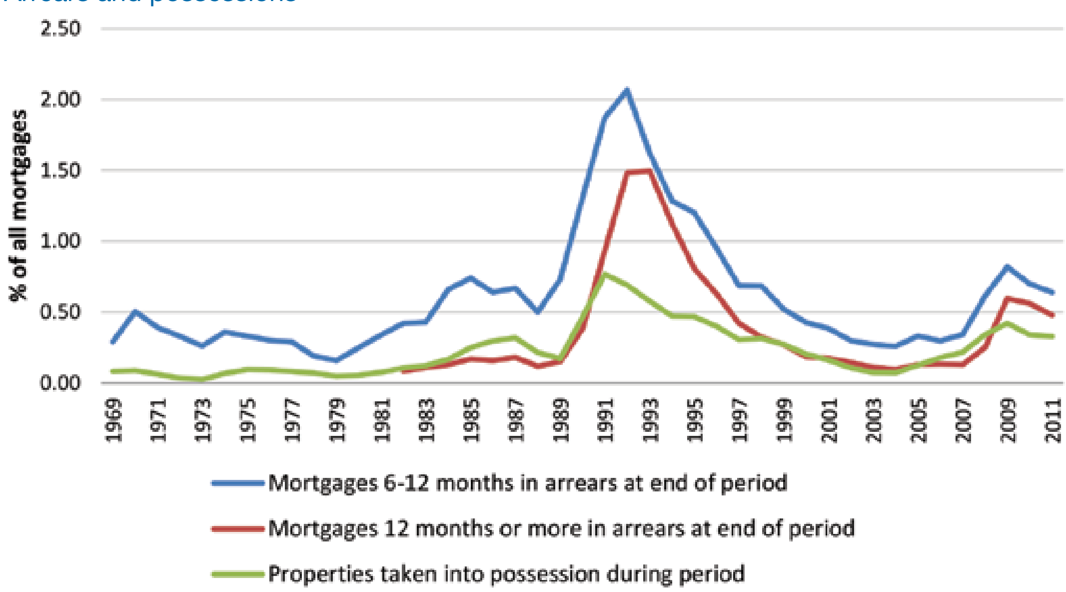
Source: BOE

Whilst there has been a contraction in lending, some individuals will have benefited. For example, those individuals with significant savings, parents that can assist them or high wages and can meet the lending criteria then they currently are able to attain a mortgage with a lower rate of interest than they could have prior to the financial crisis.

However, this leaves those that have to re-mortgage, and those on average or lower incomes that can no longer access the market, in tougher market conditions. These groups represent a sizable proportion of the housing market, and so conditions which affect their affordability of housing also need to be explored in greater detail.

If we look at those currently in the mortgage market a good indication of conditions is that of mortgage arrears and possessions. Data from the Department for Communities and Local Government (DCLG) reveals that whilst there has been an increase in both arrears and possessions in the current recession it remains significantly lower than that of the previous recession.

Arrears and possessions



Source: DCLG

This could be the case for several reasons including:

- Individuals taking action to reduce spending and boost savings as a result of the crisis and insulating against any employment changes. Thus shifting the distribution of their earnings to create a buffer, which coincides with a sharp increase in the savings ratio which is shown below. In addition, the Bank of England in its 2012 Q4 quarterly bulletin felt that "Households have chosen to save more since the crisis, and that has also weighed on spending[36]". Such trends are not only UK specific and a number of recent economic papers[37,38] have explored the extent and rationale behind this shift during the recent recession.

- Another possibility for the lower rate of repossessions and arrears is that this is the flexibility and support within the financial system, put in place by the base rate being held at historic lows. This has helped to prevent arrears and repossessions occurring. The importance of this flexibility should not be underestimated with the same Q4 bulletin from the Bank of England finding that 12% of all households were very concerned about their debt levels and over 30% being somewhat concerned. As such, even a small rise in the base rate, would result in higher repayments for millions of mortgage payers at a time where spending and incomes continue to be restrained, risking more repossessions.

12% HOUSEHOLDS VERY CONCERNED ABOUT DEBT LEVELS

- Also, the impact of the recent recession on employment was not as significant as during previous recessions. So whilst incomes have been squeezed, households have still been able to cover essentials such as mortgage payments helping to minimise the effect on arrears and repossessions.

However, whilst the financial market appears to have responded positively in terms of providing flexibility with regards to arrears and possessions, conditions for those trying to enter the market have become more challenging adding to the pressures already in place that are causing the serious supply and demand disconnect.

Saving a deposit is now a significant challenge

These difficulties within the housing market post-recession have not only been driven by continued weakness in the supply side of the market but also by new weakness in the demand side as individuals struggle to access finance. This is in contrast to the pre-recession period where most issues would have been considered to be on the supply side of the market.

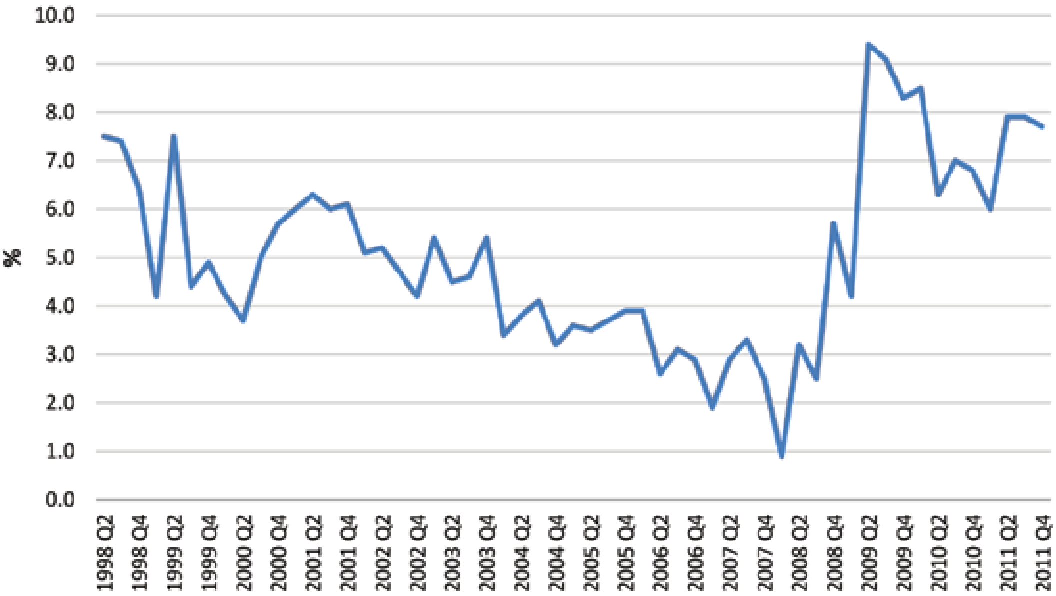
Whilst house prices did go through a period of contraction following the recession and financial crisis, prices for a period remained relatively stable, and recent data suggests are about to regain their pre-recession peak. This price change, alongside real term declines in incomes has therefore continued to impact on overall affordability.

Looking at demand weakness, there are two aspects which are creating this challenge. The first is the price of the property itself compared to earnings. As such, it is important to access and measure not only overall affordability, but also deposit and saving requirements to access a mortgage in the first instance.

Looking at the savings ratio[39] which shows the level of savings from households out of their disposable incomes, it is quite clear from the following chart that saving rates during the recession increased considerably. This was done by individuals to insulate themselves from any possible negative effects of the recession. It is also therefore possible that when growth returns individuals will have savings that could be put towards a house deposit.

Whilst savings increased though, the interest earned on those savings plummeted, meaning that there has been negligible benefit to saving. However, with the median wage in the UK at £26,244 and the savings ration since the start of 2008 averaging 6.3%, an individual would have only saved approximately £8250[40]. As will be shown in this section later, this is significantly below the average deposit requirement for a mortgage and would still require 20 years or more of saving.

Household saving ratio



Source: ONS

For example, the Institute of Economic Affairs[41] recently explored affordability using its Median Multiple ratio. This was created using median house prices and median annual gross income. This ratio therefore created a measure which it was felt represented affordability, and could be explored across each region of the UK. They found that whilst this ratio across the UK's regions varied, all regions were significantly above the average for English speaking countries worldwide. Whilst there will be significant differences between international comparisons, the data again shows that the UK does have a serious issue with the overall affordability of housing, highlighting the problems created by the imbalance between supply and demand.

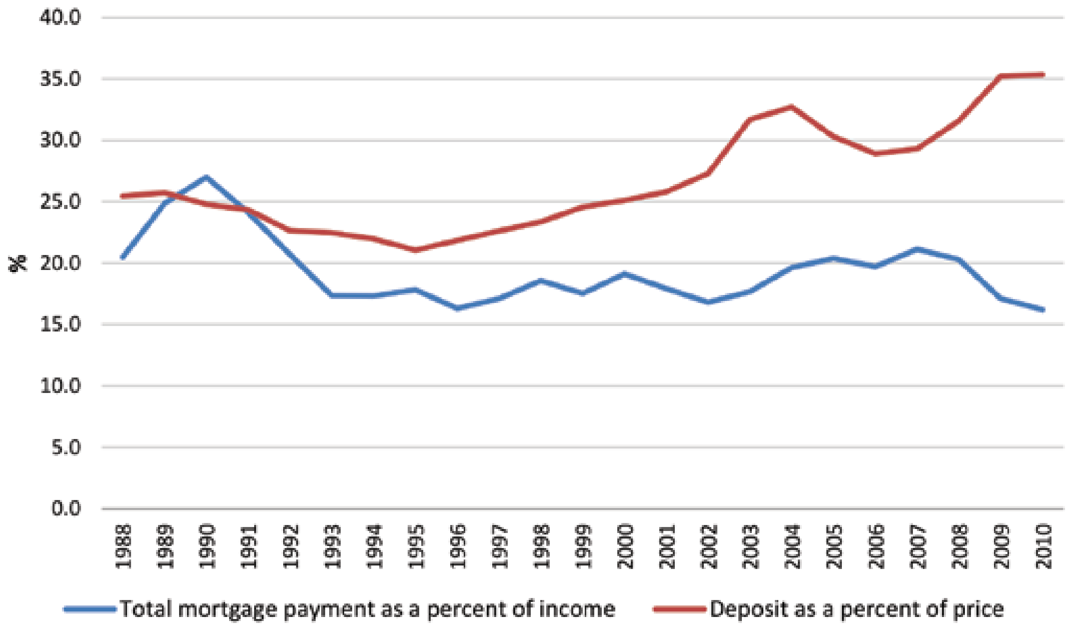
Earnings compared to prices and deposit requirements remain a challenge

Looking more closely at affordability in relation to deposit requirements data from DCLG, it is revealed that in the housing market, the deposit required as a percentage of the price has undergone a significant rise. This can be seen in the following diagram with the deposit requirement increasing from 21.1% in 1995 to its current level of 35%.

2010 AVERAGE DEPOSIT 35%

Despite there being some relief in the period between 2004 and 2007 with loosening deposit requirements, there was a sharp rise in this requirement following the financial crisis and recession with the current deposit requirement at approximately 35% of the property value. This rise in deposit requirements will have meant that some individuals and households that could have purchased a house during the last few years have been unable to do so, with the market favouring investors. These investors however, are only likely to exacerbate problems driving property prices and rental prices higher whilst the relative stock available for medium and lower income families falls.

Deposits and repayments as a percentage of income



Source: DCLG

More positively, the data also reveals that mortgage payments as a percentage of income are below the long term[42] average of 19.3% to its current level of 16.2%. This means that those currently with mortgages have not only had housing costs fall relative to income, during a period of limited wage growth, but also that it would have been possible to pay a greater proportion of their mortgage off if they maintained the level of their previous mortgage payments in absolute terms.

MORTGAGE PAYMENTS AS A PERCENTAGE OF INCOME 16.2%

This in some ways is more damaging to the UK housing sector because there is increasing a disparity between the older/wealthier generations which will be asset rich and the younger and increasingly also the average earning generations which will be asset poor.

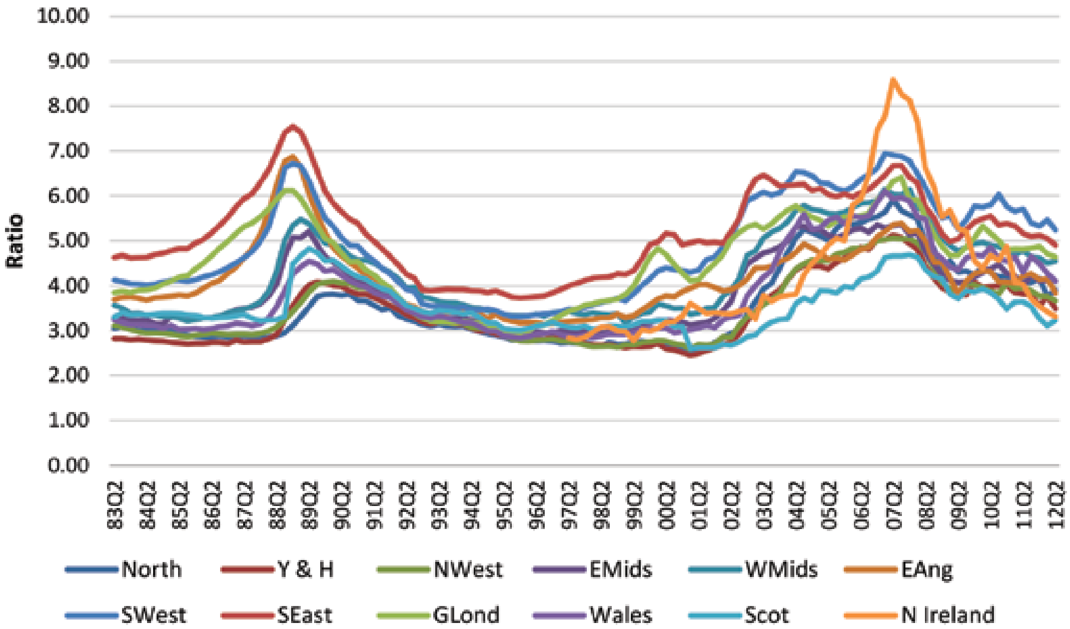
This disparity, given constrained supply will only result in higher prices, and younger generations having to make larger and longer commitments to enter the property sector. Thus it makes the aspiration of owning a property a more distant prospect than ever before. If this shift away from home ownership continues, government will also need to reassess how it targets services such as health care and education to families and individuals as the likelihood of more frequent movement increases.

Part of the rationale behind the Bank of England's decision to maintain the base rate at historic lows, will be that wage rate increases have been restrained (1.3% December 2012[43]) and running below the level of inflation (2.7% December 2012[44]). This therefore encourages banks to maintain lower interest rates on their products, thus helping affordability for those within mortgages and those seeking to enter the mortgage market.

However, as mentioned previously this support does not address the issues surrounding deposit requirements for those trying to enter the market, and even may act as a disincentive given that saving rates have also been reduced by banks to reflect the lower base rate. These reduced savings rates make it more difficult to save a sufficient deposit. This raises a wider question as to affordability of housing in comparison to income, and who in society will be able to afford a home.

Halifax produces a number of regional earnings ratio series. These series reveal that whilst there was a sustained increase in the ratio across regions between 1997 and 2007 that these fell as a result of the financial crisis and recession as housing prices fell. Currently these ratios vary between 3.4 (Yorkshire and Humberside) and 5.19 (South East).

House price earnings ratio by region



Source: Halifax

Any fall in this ratio[45] represents affordability increasing as earnings are able to cover a larger proportion of a houses overall price. For example, if an individual wanted to purchase a property at £250,000 and earned £50,000, their earnings to price ratio would be five. Following the financial crisis if this same house's price fell to £200,000 and wages remained unchanged, the ratio would have fallen to 4, showing that their wage is able to cover more of the house's cost. Therefore affordability has increased.

So recent falls would be welcomed by individuals trying to enter the housing market. However, this ratio does not account for the tighter lending conditions, through aspects such as higher deposit requirements. As such, whilst it may appear that affordability is improving this may not actually be the case.

For example in 2011 the median wage was £26,244[46]. If the average of the regional earnings to house price ratio in 2011 (4.4) is taken this suggests a house price of £115,473 and a deposit of £40,415[47]

If we compare this to 2007 the average median wage was £24,043 and the ratio average of 5.79. This when combined suggests a price of £139,208 and a deposit of £40,788[48].

A similar result can also be obtained if you use Halifax house price data rather than calculating an inferred price from the ONS median wage and Halifax's house price ratio.

In 2010, the average annual house price according to Halifax was £166,739 which calculating the deposit as above suggests a final amount of £57,299. In 2007 the average house price was £196,478 which results in a deposit of £57,586

As can be seen from the above again in absolute terms the deposit requirement appears to have changed little (down from £57,586 to £57,299), but as a percentage of the asking price the deposit requirement has increased by more than 5%.

Interestingly, if the same deposit requirements are calculated using DCLG mix adjusted house prices for 2010[49] (£208,755) and 2007 (£213,807), the deposits required are not similar at £62,645 in 2007 and £73,481 in 2010.

So depending on which house price measure is used, there can be variation in the scale of the absolute value of the deposit. However, whilst the actual amount in pounds that is required as a deposit may not have changed significantly, the deposit requirement as a percentage of the house price has. Thus, actual affordability is being effected. An individual needs to be able to save a similar amount in 2010 to 2007 to cover a house which has a lower value.

Unfortunately, looking into the future, whilst deposits as a percentage of house prices may indeed reduce back to a level of around 25%, this will come alongside significant house price increases due to a continued shortage of housing. As such, any benefit that may be gained as the percentage falls will be lost by the increase required due to the increase in house prices.

For example, a recent report by Oxford Economics[50] was reported[51] to forecast the average deposit requirement for a house purchase in London by 2020 to be in excess of £100,000. This is reported to be at a deposit requirement of 25%. This again demonstrates that credit conditions are expected to remain challenging going forward.

AVERAGE COST OF RUNNING A HOME £9,590

These examples demonstrate that UK housing policies are failing to address the disconnect between supply and demand, and are therefore allowing items such as deposit requirements, house prices and interest rates to vary at different points in the economic cycle with the result being a continued and sustained erosion of affordability within the housing sector.

Other data from Halifax also reveals how affordability is also being squeezed within the running and operation of a home once a house purchase has been made. The average cost of owning and running a home rose by £179 between 2012-13[52]. The average cost of running a house per year currently stands at £9,590, with £3,571 of this attributable to mortgage payments. However, it should be noted that the mortgage cost has reduced in recent years due to the measures taken by the Bank of England to keep the base rate at historic lows.

Again such considerations have to be taken into account by families, and younger generations looking to purchase a home. However, this assumes that they have reached a position to purchase a home, and consider such costs. Is being able to buy a home realistic by say the age of 30?

Owning a house before 30 is not a reality

Using the deposit requirements, wages and savings rates this report will calculate how long it could take for both an individual and a couple to save a deposit. The challenge remains a significant one.

For example, using data for median gross wage in the UK (£25,882) and house prices (£208,757) it is possible to forecast their increase going forward using a ten year rolling average based on previous growth rates. Using this method between 2010 – 2040, earnings growth on average is approximately 2.4% (above the long term target rate of inflation of 2%) and house price inflation averages 5% (which is below the ten year average of 8% and significantly below the long run average of 10.2% between 1970-2010).

If you then assume an individual saves 10% of their disposable[53] income (which is significantly above the current savings ratio of around 7%), and receives interest of 2.25% (The Building Societies Association figures for Branch notice accounts averages 2.25% since Jan 2002 – Jan 2010) and wishes to secure a mortgage with a 25% deposit (significantly below the 2010 level of 35%) they still would not have managed to save a sufficient deposit by 2050. In fact, interest rates on savings under this model need to reach 4.7% until an individual can afford a deposit by 2050.

INDIVIDUAL NEEDS 4.7% INTEREST RATE TO SAVE A DEPOSIT BY 2050

Worryingly even if you raise the saving rate to 15% of disposable income (assuming the historical average rate of interest of 2.25%) again the individual will not meet deposit requirements by 2050, However, more than one individual may purchase a property, such as those in a relationship as there is more than one income. Starting from 2010, assuming two people wish to save for a deposit who both earn the median wage, and save 10% of their combined disposable income it is possible to meet the required deposit of 25% of the value by 2032.

This therefore suggests that a couple would need to have been in a stable 22 year relationship to have saved the required amount for a deposit.

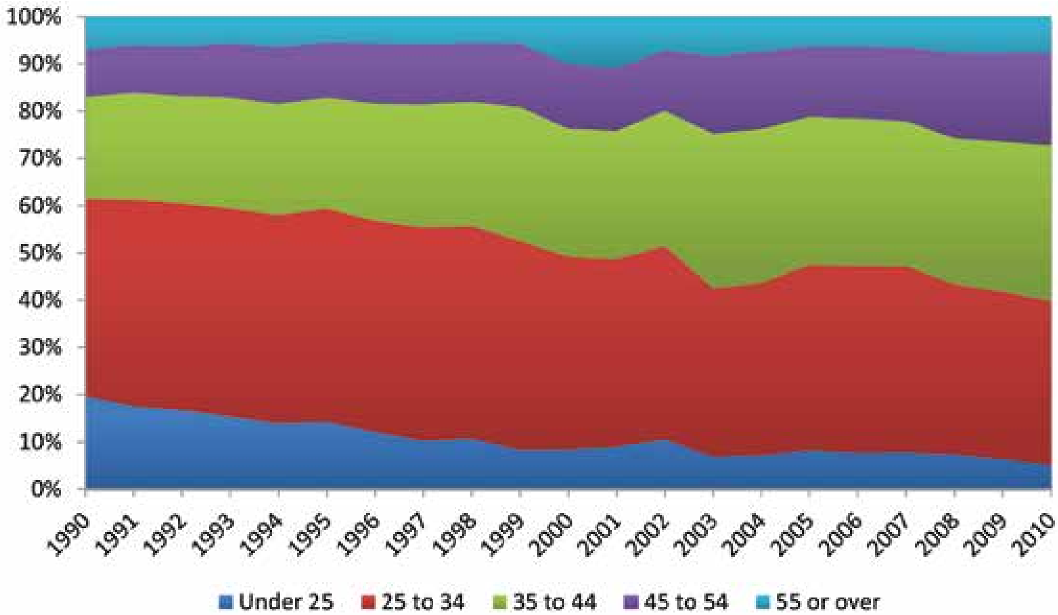
If you raise the saving rate for couples to 15% it improves their ability to save for a deposit with them reaching the 25% deposit requirement by 2022, and if interest rates over the period are increased from 2.25% to 3% this is possible by 2029, and at 4% by 2027.

ONLY 39.8% OF BUYERS NOW UNDER 34 DOWN FROM OVER 60% IN 1990

This demonstrates that home ownership, is not just becoming, but has practically become impossible before the age of 30 without parental assistance, or extremely low deposit requirements. The disconnect between supply and demand could be considered therefore to be approaching breaking point for individuals of this age, with little prospect of home ownership.

Given the change in financial conditions and the unlikely prospect of returning to 5% or lower deposit rates there will be serious implications for the affordability of housing for first time buyers. As can be seen by the DCLG chart below, since 1990 the percentage of buyers under the age of 34 has fallen from over 61.5% of the market to 39.8%.

Distribution of borrowers by age



Source: DCLG

One of the reasons behind this decline could be that:

- Since 1990 a continued trend of higher deposit requirements as a result of price increases has made it more difficult for this age group to access the market.

For example, given the age of this group they are likely to be first time buyers, and data from DCLG shows that the average deposit requirement has increased from 12.4% in 1988 to 27.5% in 2010. This is a significant increase and so would significantly increase the age at which younger individuals were able to access the housing market.

With the financial crisis significantly restricting access to even 10% deposit mortgages, there is little evidence to suggest that this trend will do anything but continue to decline.

However, as with the other trends discussed in this report whilst the financial crisis played its role in further exacerbating the problem, the reality is that affordability issues were being built into the system long before the crisis occurred.

And whilst actions such as the government's Help to Buy scheme will aid individuals to get lower deposit requirements, it is currently limited to a three year period. Further to this institutions such as the Bank of England have warned that it will only inflate prices further.

Again policy only appears to be targeting one side of the supply and demand balance, further distorting the housing market rather than addressing fundamental structural supply problems.

Mortgage rates may currently be low, but paying for a house is taking longer than ever

In addition, to the age of buyers, it is important to look at the length of mortgage terms that the market is supplying and individuals are purchasing. This data also shows a few interesting trends.

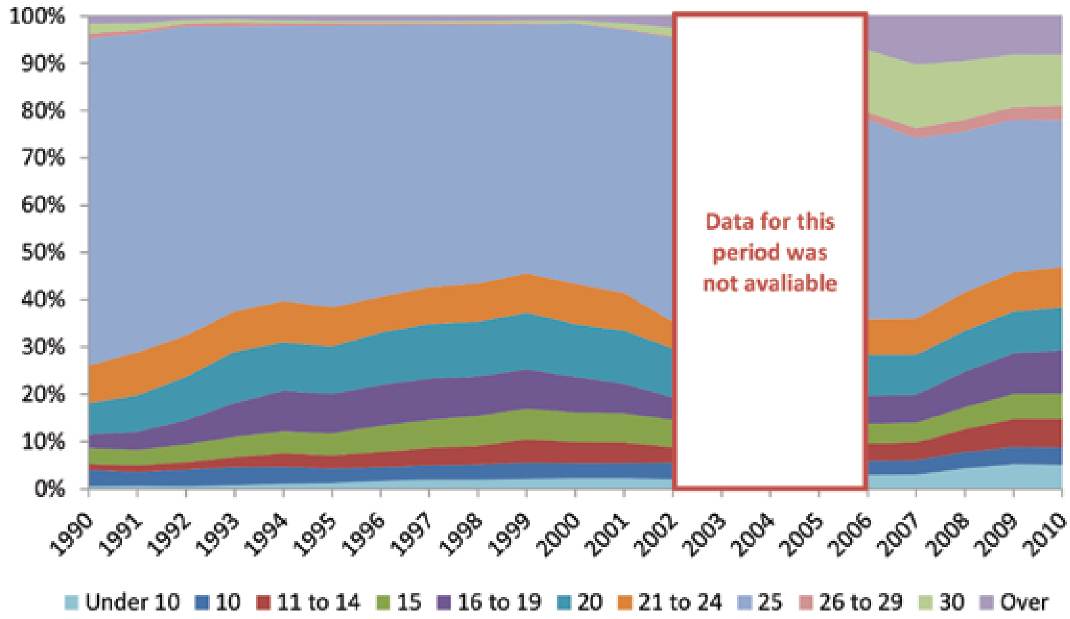
The first is that at the end of the market where you would expect to see first time buyers (longest term mortgages) the period of products has increased. Prior to 2000 the majority of long term mortgages had a 25 year term. However, post 2000 there is a significant expansion in the number of mortgages undertaken with a 25 year plus term. The rationale behind individuals taking a longer term would be either to reflect a higher purchase price, reduce monthly payments or a combination of the two. Squeezing buyers into longer term products not only demonstrates the building issues with regards to affordability within the market but also means that individuals are exposed to interest payments for longer periods thus also reducing their disposable income for a longer period.

The second trend is that since 2008 there has also been an increase in the number of shorter term products undertaken, with the middle of the market being squeezed. There are a few reasons why such a change would occur.

Whilst those entering the market are being required to take out longer products, existing individuals with mortgages will re-mortgage at points, with them being likely to reduce their mortgage term. This therefore squeezes the middle of the market and the distribution of mortgage periods will shift towards the extremities with an increase in both longer and shorter period products.

Another reason for this shift towards short term products is that as economic conditions have become more stable, banks and individuals favour shorter term products thus limiting their long term liabilities and exposure to debt.

Distribution of mortgage by term undertaken



Source: DCLG

This data therefore continues to bring into question wider issues surrounding the long term affordability of housing and the need for the mortgage market to effectively facilitate the process of house purchases.

Concluding remarks

The evidence explored in this paper, suggests that without action the housing market will head down its historic route of boom and bust, with the disconnect between supply and demand continuing to grow. However, with each bust the social consequences become greater and the UK nears a tipping point where the social consequences of inaction become more and more significant and potentially irrevocable.

This paper has identified a housing gap that equates to approximately 886,000 homes being needed by 2021 that are not being built, worth an estimated £185bn. This gap is in addition to the UK's lack of building over the past 35 years, which has seen house prices rise exponentially.

Demand and unrealistic expectations have also been discussed. There are a generation of individuals building significant house price increases into their retirement plans, such expectations and house price increases are not sustainable.

Alongside this, rising house prices, shortage in supply and deposit requirements are beginning to result in a generation that will not be unable to afford a home. This generation has been revealed not to just be those on some form of government support or minimal income, but also professional individuals earning even above average wages. As an individual, home ownership before the age of 30 has been revealed to be extremely difficult without parental support, and as a couple saving a significant amount of their combined disposable income will not be able to reach deposit requirements by the age of 30.

This suggests the solution is to address this disconnect between supply and demand. This disconnect it has been revealed is primarily due to failures in the provision and supply of housing. For this government will need to ensure that land is made available for development, developers are able to build, and councils can provide the relevant infrastructure and local services with a reasonable level of local consultation.

This paper has demonstrated that there is a dangerous longer term trend of significant price increases and under provision of housing. This alongside the potential £185bn housing gap shows that the problems within the housing sector are moving from one of just driving inflationary price increases to one of leaving individuals without homes. This will have tangible human, social and economic consequences. This demonstrates the urgency needed to find a solution.

However, the solution is not just a short burst of building on a mass scale, as this would damage the asset value of those relying on them for retirement. As such the solution needs to be planned over the short, medium and long term so that house price inflation is brought under control gradually, and reflects the area in which the house is built. London's growth and demand, for example, is not an accurate reflection of the entire UK housing market.

It is therefore time to open a new debate on the housing market, with the emphasis on developing a new way, a sustainable way, and a new model to solve these long established problems. A way that provides confidence, certainty, availability, affordability and importantly also attempts to over time slowly shift the market back towards to a reasonable rate of house price growth.

Endnotes

1 It is extremely likely that the housing gap will grow post 2021, causing further problems for greater numbers of households. However, to retain a credible level of accuracy (through a 10 year rolling average) the paper will stop its analysis at 2021.

2 Projections from the Office of National Statistics

3 Shelter, The housing Crisis, 2013 (click here)

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5 Data taken from 1975-2010

6 Data from DCLG and Measuringworth.com

7 The FTSE 100 index was formed in 1984, figures are calculated by using an annual average of 1985 and 2010 close data (click here for daily data on Yahoo Finance)

8 A Century of Home Ownership and Renting in England and Wales (full story); 2011 Census analysis (click here)

9 Telegraph, House building targets missed in every region, April 2010 (click here)

10 Telegraph, Green energy vital, says David Cameron, April 2012 (click here)

11 The Help to buy scheme operates in two ways, one providing an equity loan to help individuals meet deposit requirements, and the other as a guarantee for mortgages to reduce risk and reduce deposit requirements

12 The DCLG definition of a household is: One person or a group of people who have the accommodation as their only or main residence AND (for a group) either share at least one meal a day, or share the living accommodation, that is, a living room or sitting room. The occupant(s) of a bedsit who do not share a sitting or living room with anyone else comprise a single household. (click here)

13 T Carlyon, Shelter, Food for thought: applying house price inflation to grocery prices, February 2013 (click here)

14 Price from Tesco 24/05/2013 (click here)

15 Kate Barker, Review of Housing Supply, 2004 (click here)

16 Housing associations are private, non-profit organisations that provide affordable and social housing. These bodies can and do receive public funds, and recycle earnings to maintain their housing stock.

17 A household is defined by the ONS as one person living alone, or a group of people (not necessarily related) living at the same address with common housekeeping – that is, sharing a living room or sitting room or at least 1 meal a day

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19 DCLG, Live numbers on dwelling stock, accessed 2013 (click here)

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25 Current value from Tesco as of 24/05/2013)

26 Current value from Tesco as of 24/05/2013)

27 Current value from Tesco as of 24/05/2013)

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29 Real house price trends take into account inflation

30 Shelter, A better deal Towards more stable private renting, September 2012 (click here)

31 Data taken from 1975-2010

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33 The FTSE 100 index was formed in 1984, figures are calculated by using an annual average of 1985 and 2010 close data (click here for daily data on Yahoo Finance)

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38 L Pistaferri and I Eksten, Changes in the income distribution and aggregate consumption_ changes in the income distribution and aggregate consumption (click here)

39 The saving ratio is a key indicator of households' willingness and ability to purchase goods and services. In National Accounts terms, saving is defined as the part of households' available resources that is not spent on final consumption of goods and services. It does not therefore equate with the use of the term saving in common parlance. For instance, saving in the National Accounts sense will fall if households increase their spending through recourse to increased borrowing, even though they have not changed their saving in the conventional sense. Source ONS, Recent developments in the saving ratio (click here)

40 Calculated at £1650 a year with no allowance for interest being paid.

41 IEA, Abundance of land, shortage of housing, April 2012 (click here)

42 Average calculated on yearly data from 1988 to 2010

43 Month on year previous, ONS, average weekly earnings

44 CPI, measure of inflation December 2012, month on year previous

45 Calculated by dividing house prices by earnings

46 Median wages are used as official figures are openly available in this area. Also as the paper discusses first time buyers are increasingly those on median incomes.

47 2010 deposit as a percentage of income data (35.3%) used as it was the latest data available at time of calculation

48 2007 deposit as a percentage of income data (29.3%) used to calculate deposit from price

49 latest data available at time of calculation (2010 data used for both price and deposit as a percentage of house price)

50 Oxford economic, (click here)

51 Evening standard (click here) and Mortgage solutions (click here)

52 Halifax, Annual cost of owning and running a home rises by £179, Press release 03/04/2013 (click here)

53 Disposable income takes into account taxes, NI and personal allowance

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