Chapter 1
Housing supply

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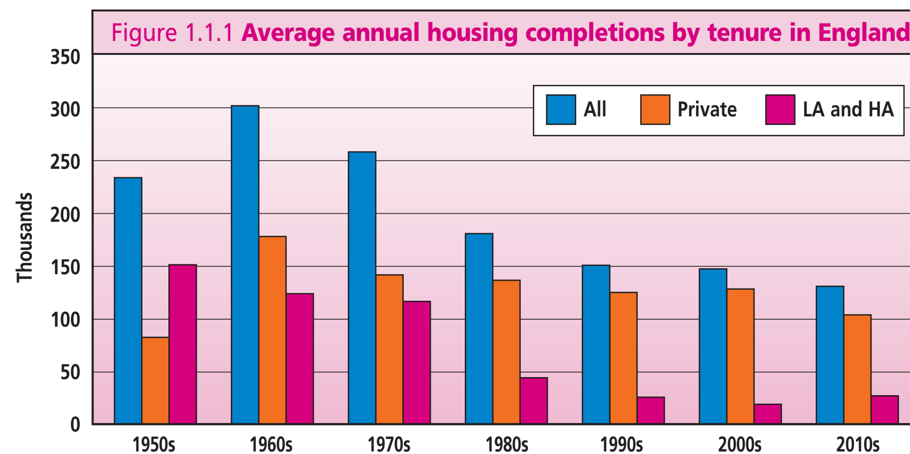
Housing supply remains at the centre of housing policy concerns. Research for Crisis and NHF, reported in the *UK Housing Review's* Autumn Briefing Paper 2018, identified a backlog for households in housing need of four million in England and of 4.7 million across Great Britain (GB). Over a 15-year period this implies a required housebuilding rate of 340,000 units per year in England and 380,000 across GB. These projections include allowances for suppressed household formation by younger households resulting from previous inadequate supply, as well as needs arising from demolitions. The required level of social rent housebuilding was estimated at 90,000 for England (100,000 for GB) with additional amounts for shared ownership and intermediate rent.

However, as Figure 1.1.1 demonstrates, annual average completions in England reached 300,000 only in one of the past six decades – in the 1960s – since when the yearly average has fallen in every subsequent decade since, down to 150,000 in the 1990s and to 130,500 in the post-Global Financial Crisis (GFC) decade of the 2010s. The largest component in the decline is the social rented sector – primarily local authorities which were the dominant providers of new social housing until the 1990s. Output in the social sector peaked in the 1950s (150,000 units per year), but fell to under 45,000 in the 1980s, and even the slight recovery in the 2010s (27,000) is a feeble echo of the past.

Figure 1.1.1 **Average annual housing completions by tenure in England**



Source: MHCLG Live Table 244.

Note: 2010s = 2010-2018. In the current decade the statistics understate LA and HA output – see later in the text.

This has left the private sector as the main provider. Yet the private sector never reached the peak levels of output in the 1930s when 'annual private housing completions as high as 250,000 were constantly achieved.'[1] Rather than fill the gap left as local authorities largely withdrew from housebuilding their output also fell back – falling from an average of 177,500 units annually in the 1960s to 128,000 in the 2000s (a marginal improvement on the 1990s in a decade which ended with the GFC). The post-GFC recovery has seen annual output rise to just over 100,000 in the first nine years of the 2010s.

Private housebuilding

The industry in Great Britain emerged in its modern form during the housebuilding boom of the 1930s when housebuilders first sought to raise capital from the stock market. The business model that became established is commonly known as 'speculative' which means that land is purchased by the housebuilder, which will then usually seek purchasers only when properties have been built. The builder therefore oversees the entire process from land acquisition to final sale. It means that risk is inherent to the model since the housebuilder cannot be sure of the price that the houses will sell for when it purchases the land. Further, in order to secure supply into the future, housebuilders must acquire and hold land (or options in land).

Why does this model persistently fail to produce enough housing? The government's Calcutt Review which reported before the GFC argued that 'the industry is answerable only to its investors and shareholders and not to the public interest.'[2] Consequently, it placed responsibility on government to devise 'incentives and opportunities' for the industry to act in the public interest. More than ten years on, this attitude seems complacent, although it is obvious that the context in which the industry operates will affect how it performs.

Planning

The planning system has long been held by many commentators to be the culprit for the failure of housebuilding to keep up with needs. Policy Exchange published a recent example of this approach, in which the authors claim that the 'state has substituted itself for the price mechanism in landmarkets' leading to needs assessments that lag behind reality and the 'strong tendency... to excessively ration

the supply of developable land.'[3] The consequent inflation of land values causes developers to skimp on design standards and quality, and results in land-use patterns that are inefficient and often form unattractive neighbourhoods. The authors make a number of interesting proposals including a call for the current system to be replaced by a simplified binary zonal approach in which land is either zoned for development or non-development, with each designation carrying a corresponding presumption for or against development. Thereafter the market should determine land use in place of what the authors see as excessive micro-management within the context of a rules-based development system. Rules would set out what *should not* be allowed in a development zone and what *should* be allowed in a development zone.

However, experienced administrators, such as Lord Kerslake (former permanent secretary at DCLG), take a more measured view. He argued that, 'however slick, efficient and effective you make the planning system you will not double supply through that route. That is for the birds....'[4] A National Audit Office report on the English planning system pointed to the majority of local authorities not having up-to-date local plans and to possible deficiencies in the methods used to calculate housing need at a local level, but observed that ultimately councils cannot control the numbers of houses built once land has been identified and permission granted.[5] The report raises issues of infrastructure provision, noting the complexities of developer contributions through section 106 agreements and the Community Infrastructure Levy, and the reduced spending and staffing in planning departments in recent years.[6]

However, the report does note that more than 80 per cent of major residential planning applications were approved in 2017/18. Indeed the simple view that the planning system excessively restricts supply sits uneasily beside statistics on the numbers of units of housing receiving planning permission. These consistently exceed the numbers of houses completed by private and social providers combined across England, Wales and Scotland. Notwithstanding that the approvals statistics include conversions as well as new builds, the gap is striking. Completions in England were fewer than half the number of permissions granted over the 2011-2018 period – a difference of 1.1 million units.[7] The differences were proportionately smaller in Scotland (75 per cent) and Wales (69 per cent).

This might be taken as evidence of landbanking – the practice whereby a developer holds on to land in the hope that its value will rise, rather than building it out. The industry has always rejected that it indulges in such practices, arguing that landbanks are required to allow a pipeline of development, taking into account the time it takes to gain planning permission as well as market conditions. Further, they argue that it would be pointless to hoard land with planning permission because it will lapse. Most reports tend to confirm that 'these firms do not, in general, speculate in land that has received planning permission.'[8] Following an investigation that took place before the GFC, the Office of Fair Trading (OFT) concluded that:[9]

> *Having a stock of land helps a homebuilder cope with fluctuations in the housing market and also helps to reduce its exposure to risk resulting from the planning system. We have not found any evidence that homebuilders have the ability to anti-competitively hoard land or own a large amount of land with planning permission on which they have not started to build.*

But what happens once building begins? Slow build-out rates may go some way to explaining why there is a gap between permissions and completions. The Calcutt Review rejected any action to encourage faster build-out rates, arguing that it would put production at risk. However, the Letwin Review[10] was established to 'explain the significant gap between housing completions and the amount of land allocated or permissioned in areas of high housing demand.' Letwin also concluded that there was little evidence of landbanking per se, but instead attributed slow build-out rates to the 'absorption rate' – suggesting that there is a limit to the speed at which a large site can be built out without lowering prices and hence profits.

Like Calcutt, Letwin did not favour measures to force speedier build-out rates as these would cause financial problems for housebuilders. Instead, he sought to identify ways in which absorption rates could be increased on large sites. He attributed low absorption rates to the homogeneity of houses on individual sites, and proposed ways in which diversity, of both housing type and tenure, could be increased. Central to this is the idea of adopting planning rules that require diversity. He also suggested that local authorities should be empowered to use

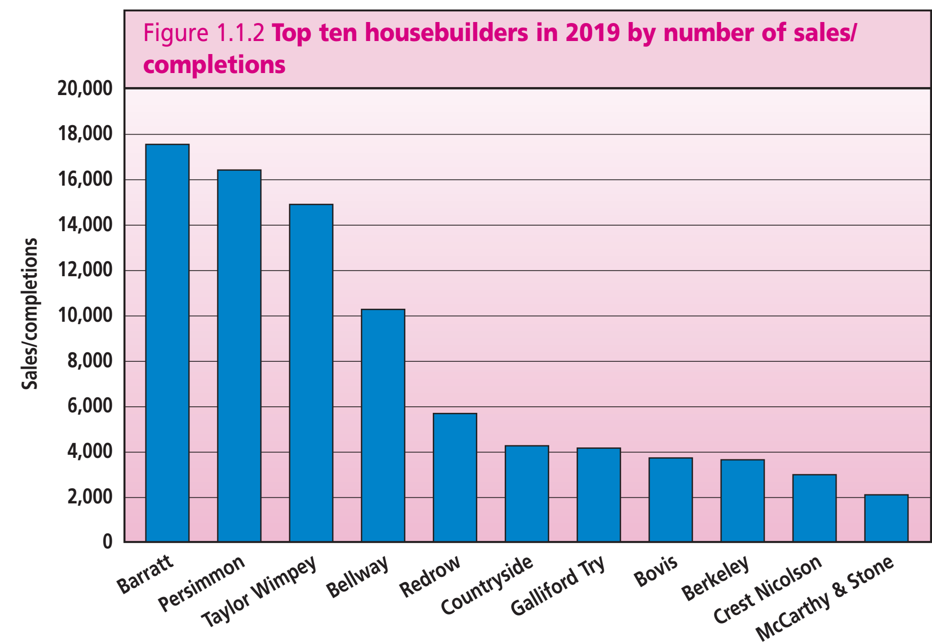
compulsory purchase powers and to cap the value of permitted land at ten times agricultural use value on large sites. In other words, he proposed that a form of land-value capture be employed in order to finance diversity. The government's formal response effectively rejected these proposals, relying instead on planning guidance 'to further encourage large sites to support a diverse range of housing needs, and help them build out more quickly.' It is also committed to 'evolving the existing system of developer contributions' rather than replacing them. However, the government did suggest that Homes England might have a role in identifying sites and to 'support local authorities to further diversify their large sites.'

Competition

One of the established trends in the private housebuilding sector is its growing concentration over time. This was charted by Fred Wellings for the Calcutt Review.[11] He noted that in the 1930s the ten largest builders had a market share of about 6-7 per cent; at the beginning of the 1970s this was 8-9 per cent; and by the early 1980s the market share of the top ten had risen to 17-18 per cent. Over this period the annual output of the top ten doubled from about 16-18,000 units each to 32-33,000. Volatility in the market led to some fluctuations in the share of the top ten, but by the early 2000s their share had risen to more than 40 per cent. A more recent analysis published by the Social Market Foundation found that the biggest four housebuilders currently enjoy a market share (the CR4 ratio) of one-third, a couple of percentage points lower than in 2014, but still higher than the pre-recession level of 30 per cent (in 2006), which itself had risen from 25 per cent in the early 2000s.[12] Our provisional calculations for 2019 (see Figure 1.1.2) suggest that the share of starts accounted for by the largest housebuilder is 10.1 per cent, with the top four accounting for more than one-third of starts (CR4 = 34.1 per cent) and the top ten almost a half (CR10 = 49.6 per cent).

These statistics relating to concentration are driven by the growth in scale of the largest companies. Mirroring developments in the building society and housing association sectors, housebuilding began as a local activity, but some firms developed first into regional players, and later into national ones. Wellings identifies Wimpey as being the first 'national' housebuilder in the 1970s, followed by Barratt and Tarmac McLean.

Figure 1.1.2 **Top ten housebuilders in 2019 by number of sales/ completions**



Source: Stone Real Estate reported in *pbc today*, December 17, 2019.

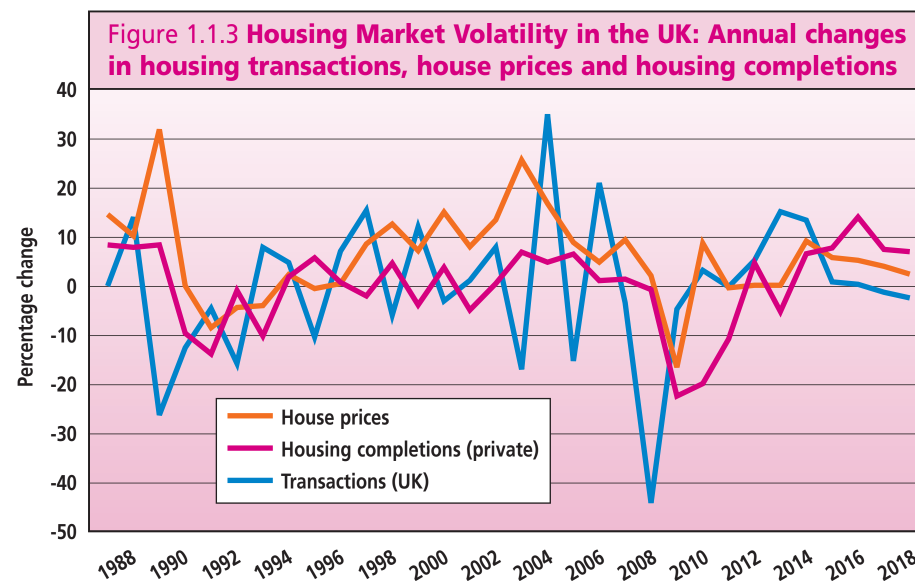
Whether the long-term trend towards greater concentration reflects economies of scale or scope is a moot point. Smaller builders complain of the costs associated with planning being disproportionate to small developments, but Wellings says there is 'no consistent evidence to support the proposition that large companies earn superior rewards to small companies.' Rather, once floated on the stock exchange, there is pressure for housebuilding firms to seek growth through gaining market share: 'they are not allowed to stop growing.' An OFT report argued that it is more profitable to sell a fixed number of properties from four sites than the same number from one because the impact on prices will be greater on a single site. Consequently, the imperative to acquire new sites 'drives many of the mergers and takeovers.'[13] Following this logic and its own examination of mergers, the Lyons review concluded that 'mergers have therefore had the effect of reducing the number of homes built post-merger.' The House of Lords Select Committee on Economic Affairs suggested that the sector 'has all the characteristics of an oligopoly' and this has intensified since the financial crisis.[14]

Smaller builders

Our analysis for 2019 suggests that housebuilders outside the top ten still account for half of housebuilding in the UK, and there is widespread agreement that smaller builders play a crucial role in housing supply, but their numbers have steadily diminished. The numbers of firms producing 100 or fewer units declined from more than 12,000 in 1988 to 2,400 in 2014 according to the House of Lords Select Committee. By 2017, the number had fallen to just 1,737. Nonetheless, Lyons described them as being 'a crucial part of the sector's capacity because they will develop small sites that larger firms will not.'

An NHBC survey of firms producing 50 or fewer units annually identified their most serious concerns as being the time it takes for planning applications to be processed, their costs and the uncertainty of outcome. Almost as important was the availability and cost of land, followed by the availability and cost of finance. In response to the last of these concerns, in 2019 the government launched a loan guarantee programme ('ENABLE Build') through the British Business Bank. However, since the programme is open only to established companies, it does not tackle the barriers to entry that inhibit new players.

Figure 1.1.3 **Housing Market Volatility in the UK: Annual changes in housing transactions, house prices and housing completions**



Sources: Transactions: Compendium Table 40; House prices: Nationwide; Completions: MHCLG Live Table 209.
Notes: Calendar years, except Housing completions = financial year ending; House prices = Q1 for each year.

Volatility

The broader economic context in which the housebuilding industry operates receives less attention than the institutional questions already discussed. Yet economic instability and the volatility of the housing market since the 1970s are important factors in explaining the shortfall in housing supply from the market.

Clearly the more volatile are prices and transaction volumes, the greater the uncertainty and the greater the risks facing housebuilders. These risks provide the possibility for both very high returns and catastrophic losses in terms of sales, and for these swings to be reinforced by the pro-cyclical fluctuation of asset values on balance sheets. Figure 1.1.3 illustrates the pattern of volatility in terms of house prices, residential property transactions and housing completions since the 1980s. When examined alongside Figure 1.1.1 it is clear that with each boom-bust cycle the number of housebuilders falls, alongside output.

Risks most clearly crystallised as a result of the GFC when, as Lyons reported, between 2006 and 2009 the industry's turnover halved and an operating profit of £2.2 billion in 2006 became a loss of £2.2 billion in 2008. This seems to have intensified the behaviour of the industry, according to a study by Sheffield Hallam University: housebuilders prioritised profit over volume during the recovery and distributed a higher proportion of surpluses to shareholders, rather than reinvesting them in the business.[15]

A further consequence of the GFC is the extent to which the state has become embedded in supporting the housing market. In addition to the Bank of England's monetary policy, the government has through its agencies become an owner of residential property through Help to Buy, which now accounts for between 36 per cent and 48 per cent of the total sales of five of the six largest housebuilders. Consequently, as discussed in Commentary Chapter 6, the state now has a vested interest in house prices.

Housing associations

Housing associations remain the largest non-market developers across the UK. They assumed this role as a result of the 1988 Housing Act (and its equivalents across the UK) in which the government made housing associations the principal providers of new social rented and other affordable housing. Grant per unit has generally been reduced over time, leading associations to become increasingly dependent on the ability to raise retail and wholesale finance. These changes have also driven a restructuring of the sector, with a strong tendency towards merger, which means that in terms of units under management, the largest housing associations manage stocks in excess of 100,000 units and have become national providers. These issues are explored in more detail in Contemporary Issues Chapter 2.

Assessing the scale of output by housing associations across the UK is complicated by the different statistical sources, but it has been rising and in 2018/19 reached well over 50,000 units in total if open market units, acquisitions and conversions are included as well as affordable new build (for discussion of the difficulties, see Contemporary Issues Chapter 4). Completions (on this wider basis) are rising across the UK. In 2018/19, in England they rose by ten per cent to 45,604 units. In Wales, in the same year, housing associations completed 2,338 units, up 400 on the previous year. In Scotland in 2018/19, construction statistics record housing associations as having completed 4,169 units, a one-third increase on the previous year. Their real output is likely to have been considerably more – towards 5,500 – their contribution to the push to meet an affordable homes target of 50,000 units over the lifetime of the current Scottish parliament. In Northern Ireland, housing associations completed 1,682 units in 2018/19, their highest recent output.

It is important to distinguish the composition of social rented versus wider 'affordable' development by housing associations (and councils). Compendium Tables 20a-20f provide country-level splits between the two types of new provision. Three points stand out. First, there was a further modest decline in the share made up by social rented housing, now less than a quarter of UK output; this is because of its very low share in England, which has bottomed out at around ten per cent. Second, the affordability component is quite varied with a growing role for intermediate or affordable rent in Scotland and with it playing a significant role in England, albeit uniquely here seen until recently as a *replacement* for social rented homes. Across all four countries, shared equity and other forms of low-cost homeownership have also been important, currently accounting for just over 30 per cent of total output. It is also worth saying, third, that the new impetus towards social housing post-2018 from the Whitehall government may be expected to shift these trends modestly back towards social renting, with the proviso that this does of course depend on the new government maintaining this as a priority.

A recent survey by *Inside Housing* of the largest housing association developers ('Insight', June 26, 2019) for financial year 2018/19 indicates that 15 developers produced more than a thousand units, and one, L&Q, delivered more than 2,800 units. This is more than half of the total delivered by the top 50 which in turn is the lion's share (about 84 per cent) of all completions by housing associations in England. Table 1.1.1 shows the output of the top ten broken down by tenure. Among the largest 50 developers, there was a big increase in low-cost homeownership relative to overall completions (21 per cent compared to eight per cent) and grant fell by £432 million compared to the previous year for the largest developers. Concentration of development by this group remains striking. It will be reinforced, broadly, by the partnerships being struck with Homes England and the GLA for multi-year development programmes.

The outputs of the housing association sector are clearly much lower than the private housebuilders – but far from negligible. Construction statistics suggest that for every five houses built by the private housebuilders, the housing associations build one, although as we have seen this likely exaggerates the difference. The housing association sector has also undergone concentration particularly since the need to raise private finance became a significant factor after 1988. In 2019, RSH figures show that grant accounted for 10.5 per cent of development finance in England, whilst half came from sales and other cross-subsidy and the balance from debt. The largest association, L&Q, accounts for 8.4 per cent of completions. The share of the top four associations at 24.3 per cent is much lower than their private counterparts (34.1 per cent), but the top ten's share (47.9 per cent) is very close to that in the private sector (49.6 per cent).

Table 1.1.1 **Top ten housing associations in England 2018/19 by number of completions**

Name	Total completions	Social rent	Affordable Rent	Intermediate rent	LCHO sale	Market	PRS
L&Q	**2,862**	**255**	**641**	**29**	**657**	**757**	**523**
Places for People	**1,876**	**212**	**401**	**34**	**204**	**696**	**329**
Notting Hill Genesis	**1,856**	**183**	**241**	**0**	**617**	**95**	**720**
Home	**1,660**	**4**	**731**	**0**	**554**	**371**	**0**
Platform	**1,598**	**458**	**681**	**0**	**459**	**0**	**0**
Sovereign	**1,543**	**241**	**639**	**0**	**530**	**70**	**0**
Orbit	**1,266**	**189**	**544**	**0**	**343**	**190**	**0**
Clarion	**1,243**	**13**	**641**	**0**	**454**	**135**	**0**
Bromford	**1,236**	**240**	**501**	**30**	**431**	**34**	**0**
Aster	**1,156**	**156**	**444**	**0**	**453**	**103**	**0**
TOTAL	**16,296**	**1,951**	**5,464**	**93**	**4,702**	**2,451**	**1,572**

Source: Inside Housing, June 26, 2019.
Note: Totals include some uncategorised units.

Housing association development continues to face a number of constraints and drivers as well as emerging themes which may shape the scale and pattern of what they build in the future. Non-market supply is constrained by financial reserves, the ability to raise private finance efficiently and investment needs in the existing stock (see Contemporary Issues Chapter 2). It also depends on the supply of affordable land in the right locations and on the capacity of the construction industry. With planning over a period of years it depends on partnership programmes with grant-funding agencies and also the certainty of the form and scale of public funding. Indirectly, housing association development also depends on effective partnership with local authorities and the specific functioning locally of developer contributions (see below) where these apply.

Homes England (HE) is still a relatively new organisation, empowered to be a housing accelerator and market disruptor in housing development, land and construction markets.[16] Primarily operating outside London (where the equivalent body is the GLA), in addition to the aforementioned multi-year partnerships with housing associations, HE is directly making land available for the market and for non-market sectors and funding affordable housing delivery. In its first three years, HE has directly funded an increasing volume of affordable homes, rising from 22,000 in 2016/17 to 28,710 in 2018/19. HE also released sufficient land in 2018/19 to provide forward capacity for 35,000 further homes (market and non-market). Commitments by it and the GLA under its current programme are covered in detail in Commentary Chapter 4.

The ongoing developer contributions for affordable housing made via section 106 agreements in England and Wales (section 75 in Scotland) remain important. Moreover, in England, their significance numerically is growing. Evidence from the MHCLG live tables indicates that between 2015/16 and 2017/18, the number of affordable homes provided in England with section 106 support rose from 12,904 to 23,052. During the same period the proportion of all new affordable homes in England supported by section 106 rose from 40 per cent to 49 per cent. Taking these three years together we find that most of the units were for Affordable Rent (22,316), shared ownership (14,855 units) and social renting (9,821). Another 5,121 were for affordable homeownership (i.e. sale at a discount) and 2,399 units for intermediate renting.

Housing associations have long and deep connections with private commercial interests such as property professions, the construction industry and private finance. But there is something quite different and distinct about for-profit providers operating in the housing association development sector and attracting public funding support. In 2019 Savills reported that 46 for-profit registered providers submitted returns to the social housing regulator.[17] They are mainly active in shared ownership and also constructed just under 3,000 sub-market general needs units in the year to March 2019. Much of this housing is provided as part of section 106 agreements and block purchases but by offering new money where housing associations may have hit financial capacity, though these for-profit providers remain contentious in the wider sector.

A challenge in Scotland is funding uncertainty arising from the government's long-term policy consultation 'Housing to 2040' which clearly trails, post-2021, that Scotland cannot afford to carry on with the scope and scale of public funding for housing given other commitments to, for example, tackle child poverty and achieve carbon reduction targets. This is causing much more focus by the sector on funding continuity and the immediate future after the 2021 Scottish parliamentary election, to the detriment of the ambitious and radical long-term vision represented by the Scottish Government's consultation. It has, nevertheless, announced provisional funding of £300 million for 2021/22.

While there are signs of growth in the housing association development programme across the UK and in resourcing such growth, and there is some degree of innovation, uncertainties remain. One challenge in the near future is the risk of adverse changes in public funding. This is a concern, for different reasons, particularly in England and Scotland. A second concern relates to the impact of the Brexit transition year and how this in turns leads to a highly uncertain economic future post-2020/21. This is part of a wider concern about difficult economic circumstances ahead. One thing that is abundantly clear is that the housing association development model is pro-cyclical in important respects and is likely to remain so. Thus, and despite the positive signs, there is no end to uncertainty for the sector.

A resurgence of council housing?

In the mid-twentieth century, an upsurge in housebuilding was almost unthinkable without a major contribution by local authorities building new council houses. At the post-war peak of new building in England, in 1968, when more than 352,000 new homes were completed, over 40 per cent were built by councils. In Scotland, building was even more dependent on councils: in the post-war years, it was not until 1978 that private enterprise built more homes than Scottish local authorities.

But by 1988, when private building peaked again and output in England topped 202,000, councils' contribution was only eight per cent. By 1995, English councils were building fewer that 1,000 houses annually and this continued until 2011. The fall to negligible output by Scottish councils occurred at the same time, and the similar fall in Wales continues almost to the present day. Northern Ireland has a slightly different pattern, with the Housing Executive taking over most housebuilding that would have been undertaken by councils and, in the 1980s, often rivalling private enterprise in its output. But it too, by the late 1990s, had largely given up its housebuilding role.

Across Great Britain there has been something of an upswing in local authority housing completions, albeit from a very low base. In 2004/05 only 130 council houses were built across Great Britain, but in 2018/19 just over 4,000 had been built (of which 1,880 were in Scotland).

What accounts for the recent upsurge in council building in Scotland and England? A factor in common is access to government grant, which hitherto had only been available to housing associations. In Scotland, councils also have healthy housing accounts, because they have not been subject to government-imposed rent controls, and they were able to keep what (until recently) were the sizeable receipts from right to buy sales. They were also able to combine grant with unrestricted prudential borrowing. Councils in England had to wait until April 2012 for similar freedoms, and even then, were soon subject to new rent controls. Since November 2018 they have had the same freedom to borrow prudentially.

Despite the enormous difference in the size of the sectors in Scotland and England, council house building has recently been running at similar levels in the two countries, although in England a step change is expected because of the recent removal of the borrowing caps on councils and, in April 2020, the ending of enforced rent reductions. Unlike in Scotland, there has also been an increase in right to buy receipts although this of course means that for many English councils their building programmes are simply replacing homes sold to tenants. The Treasury expects the recent changes to lead soon to councils building over 10,000 new homes per year; a CIH study suggests that this target will be met and possibly exceeded.[18]

In Scotland, councils are contributing around 30 per cent of new housing built for social rent (see Table 2.4.6 on page 74), although their proportion of the grant disposed through the Affordable Housing Supply Programme is lower, at about 22 per cent in 2018/19.[19] Proportionally, therefore, they are likely to continue to have a bigger role than their English counterparts. In Wales, where council housing financial reform did not take place until 2015, councils have been slower to undertake new build although three are now doing so (see Commentary Chapter 4). In Northern Ireland, there has been much talk of the Housing Executive regaining its housebuilding role and, with the reopening of the Northern Ireland Assembly, there seems to be some prospect of this happening.

One constraint applying across the UK is access to and the costs of borrowing from the Public Works Loan Board (PWLB), by far the biggest source of council debt. The Treasury has recently raised the cost of PWLB borrowing, and the LGA has said that this has 'stilled' councils' housebuilding plans.[20] However, it remains to be seen whether this has a serious effect: many councils will have priced-in higher PWLB rates in the contingencies of their business planning, and some are already looking for alternative sources of debt.

Conclusions

The challenge of providing sufficient new housing is not being met – and has not been met for a long time. This overview suggests that the current model of housebuilding is unlikely to meet needs and a different business model is required. Clearly such a change could not happen overnight and there is considerable risk that measures taken radically to change incentives might have the unintended consequence of reducing capacity, at least in the short to medium term. Recently, the idea that the state should have a greater role in land acquisition and assembly has gained popularity, although it raises the question of the level of compensation when compulsory purchase is employed. The role of Homes England may represent a start, and one that recognises that in a successful modern and complex economy the roles of the state and market should be complementary.

It is certainly the case that housing need will not be met without an important role being played by the social / non-profit sector. The removal of some of the restrictions on local authority building has led to a revival in this segment of the market, which has inherent strengths in terms of borrowing capacity. However, a lesson from Scotland is that grant is likely to be needed to facilitate development at scale. The housing association sector has grown and now has a number of national players, although development scale is still small compared to the private housebuilders. Finally, the context in which housing providers operate is important. There is considerable evidence that housing market volatility has increased risks and reduced capacity and competition over time. It has also resulted in the undesirable situation whereby the state has a direct stake in the owner-occupied market and an interest in maintaining higher prices. Reducing volatility opens up another set of policy dilemmas,[21] notably relating to land and property taxation, the politics of which are hazardous, but which surely need to be confronted.

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