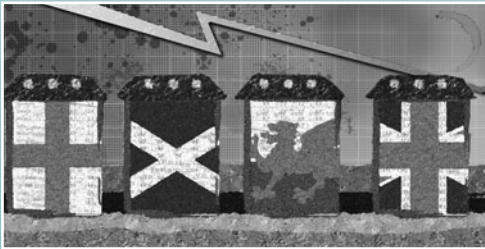


Section 2 Commentary



Chapter 4 Housing expenditure plans

A number of the topics that potentially fall within the remit of this chapter are dealt with in Contemporary issues chapters this year. The right to buy and investment in stock condition improvements are discussed in Contemporary issues Chapter 1, stock transfers in Chapter 2, and council housing finances in Chapter 3. In each case the chapters consider these issues across the whole of the UK.

Housing investment

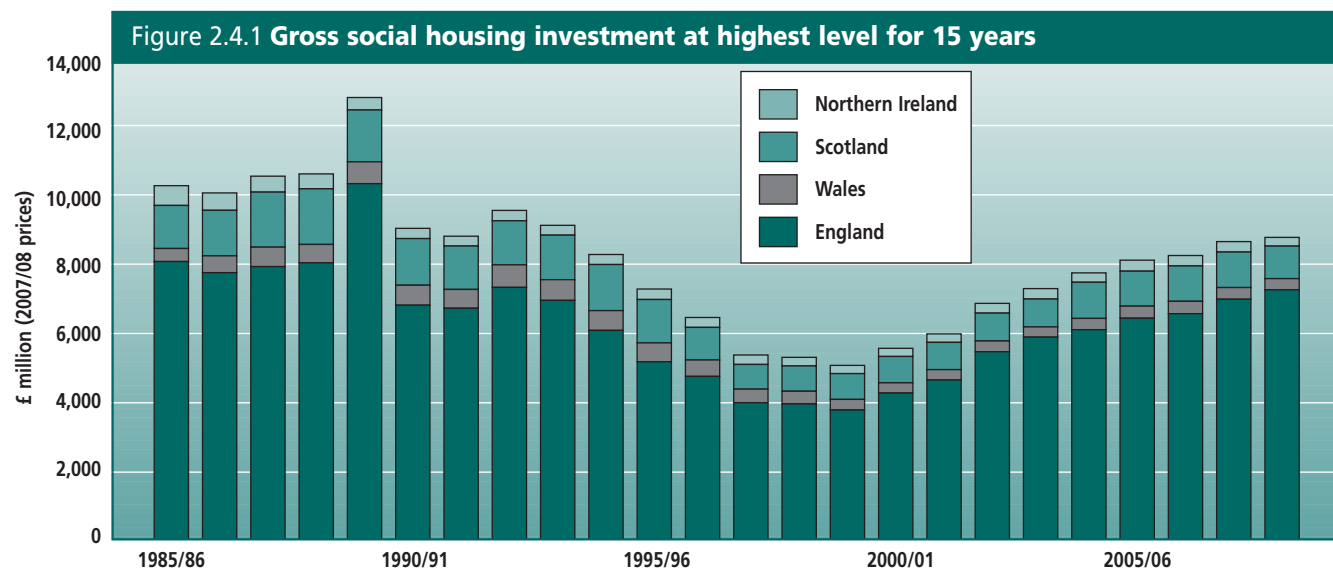
Overall gross social housing investment in Great Britain rose again slightly in 2008/09, to the highest level in real terms for 15 years. Within that total, an increase in investment in England in 2008/09 more than offset small reductions in Northern Ireland, Scotland and Wales (Figure 2.4.1).

It should be noted, however, that the figures do not include the private finance which is now such a substantial part of the investment programme for new housing association dwellings (£2.4 billion for Great Britain in 2008/09). Nor do they include the substantial investment in stock improvements by stock transfer landlords. If these two factors are taken into account, then the data in Figure 2.4.1 suggests that overall investment provision in social sector housing is now higher in real terms than it has been in any year since 1980 – with the sole exception of 1989/90 when investment spiked, buoyed by high levels of right to buy receipts from sales in the years of the last housing market boom.

However, investment fortunes in the years ahead will be mixed. Local authority investment is likely to decline, largely as a consequence of the very sharp

fall in the receipts available from right to buy sales (Compendium Table 60). Recent trends in housing capital expenditure in England are shown in Table 2.4.1, and this also shows that investment is forecast to fall to £4.3 million in 2009/10, from £4.9 million in 2008/09.

In contrast, housing association investment is set to rise sharply in 2009/10, boosted by the various programmes the government has initiated in response to the post-credit crunch collapse in the housing market (see Contemporary issues Chapter 4). The Homes and Communities Agency capital budget will rise from £3.9 billion in 2008/09 to £5.7 billion in 2009/10, before settling back to £4.6 billion in 2010/11. There have been similar boosts to housing association budgets and programmes in 2009/10 across the UK.



Sources: Compendium Tables 57 and 88.

A breakdown of the HCA programme is shown in Table 2.4.2. It should be noted that this includes programmes that were not included within the Housing Corporation programmes for preceding years, and care should therefore be exercised in comparing the capital provision figures in Table 2.4.1 with those for the Housing Corporation in Compendium Table 64.

Housing associations have faced their own challenges with the credit crunch, particularly in terms of difficulties with unsold new shared ownership stock – much of which has now been switched into intermediate renting or ‘rent now – buy later’ schemes. The credit crunch has also impacted adversely on the terms on which housing

Table 2.4.1 Analysis of English local authority housing capital expenditure*£ million*

	2003/04	2004/05	2005/06	2006/07	2007/08	2008/09	2009/10 forecast
Capital expenditure							
Acquisition land/buildings	95	276	292	297	424	343	310
Building works	2,671	2,989	3,471	3,441	3,306	3,299	3,271
Other assets	55	72	88	56	41	51	42
Grants	607	622	636	671	1,158	1,169	602
Loans/other	56	29	47	42	79	38	30
Total	3,485	3,987	4,534	4,507	5,008	4,901	4,255
Capital receipts	3,622	3,193	2,183	1,769	1,696	487	539

Source: Local Government Capital Expenditure and Receipts, Annual Statistical Releases.

associations can raise private finance, although at the time of writing the market for housing association private finance does appear to be improving.

However, further challenges lie ahead beyond the current expenditure round. The sharply rising levels of government debt (see Commentary Chapter 1) have already cast a large shadow over the future prospects for funding in the next expenditure round, to which is added an element of political uncertainty given the forthcoming general election.

If the future is more problematic then housing associations will inevitably become far more concerned with issues around asset management. The potential role of asset management in tackling those issues is addressed in the short article by Savills in Box 2.4.1 overleaf.

Devolution and social sector rents

To complement Contemporary issues Chapter 1 on Devolution and housing, this chapter provides an account of the movements in social sector rents in each of the four countries of the UK in the decade since the 1999 devolution settlement.¹

The devolved administrations have full formal control over social sector rent levels and policies. They are, however, subject to financial constraints under the various 'concordats', that in effect would mean that if they chose to increase council rents more rapidly than was the case in England, then the devolved administrations would be required to meet the consequential additional housing benefit costs from within their own budgets. That constraint does not apply, however, to housing association rents.

Table 2.4.2 Homes and Communities Agency programme expenditure*£ million*

Programmes	2008/09	2009/10	2010/11
Baseline programmes			
National Affordable Housing Programme	2,632	3,248	2,480
Property and Regeneration	38	406	211
Growth Funding	265	278	190
Thames Gateway	44	79	79
Community Infrastructure Fund	37	132	160
Places of Change	33	24	23
Gypsy and Traveller Site Grant	0	32	32
Decent Homes – Gap Funding	123	100	80
Housing Market Renewal	381	346	311
Other	14	21	27
Programme Efficiencies	0	- 108	- 75
Housing Stimulus Package			
Kickstart Housing	0	320	80
Local Authority Build (Grant)	0	15	35
Housing Environment	0	75	29
Mortgage Rescue Scheme	0	40	40
Housing Pledge			
National Affordable Housing Programme	0	375	381
Kickstart Housing	0	252	252
Local Authority Build (Grant and Borrowing))	0	36	204
Public Land	0	0	16
Total HCA controlled programmes	3,912	5,671	4,555

Source: Homes and Communities Agency Corporate Plan 2009/10–2010/11.

Box 2.4.1: A proactive response to the credit crunch

The direct consequences of the credit crunch for housing associations have been well documented: unsold shared ownership and outright sale properties, cash flow difficulties, cash or margin calls, funders repricing old loans, deflation, the highest real interest rates in 20 years and impairment of value in annual accounts.

The valuation effects of the credit crunch have been felt differentially between tenures:

- Market Value Subject to Tenancy, used for market and intermediate rent – has drifted down from 60–75 per cent of VP to 55–65 per cent because of lower future values. Net initial yields have moved out from 3–6 per cent to 6–8 per cent.
- Existing Use Value for Social Housing has remained stable – Savills uses relatively soft NPV discount rates to smooth out variations. The values are supported by initial market evidence from stock rationalisation.
- Existing Use Value for Social Housing ‘Basis Two’ assuming sale of units falling vacant are down because the market can’t absorb the volume of properties and values are depressed.
- Value of Landlord’s interest subject to Shared Ownership leases – values are down because whilst the income stream is reliable, staircasing receipts are affected by house prices. Many lenders require that receipts are ignored for the purposes of valuation.

The social impact is beginning to be felt, and this will have long-term impacts on landlords’ businesses:

- Sharp increase in market failure in certain areas.
- Economic failure leading to more demand for affordable housing.
- Potential for weakened community cohesion.
- Threats to neighbourhood sustainability.

To date, despite these economic and social impacts, we have not seen the failure of any major social landlords. This appears to be because the additional investment by the HCA to kick-start development schemes has had the effect of recapitalising

landlords. Prospects for 2010 are more challenging as promised reductions in public expenditure feed through.

Savills has advised the TSA on a ‘Regulatory Approach to Housing Associations That Face Viability Issues’. Its own contribution to the research is based around its belief that asset management is key to sorting out these issues. Our only reservation is that work-outs take time, which implies that there is a powerful case for an early warning system to guide timely intervention. This would also permit greater tenant involvement.

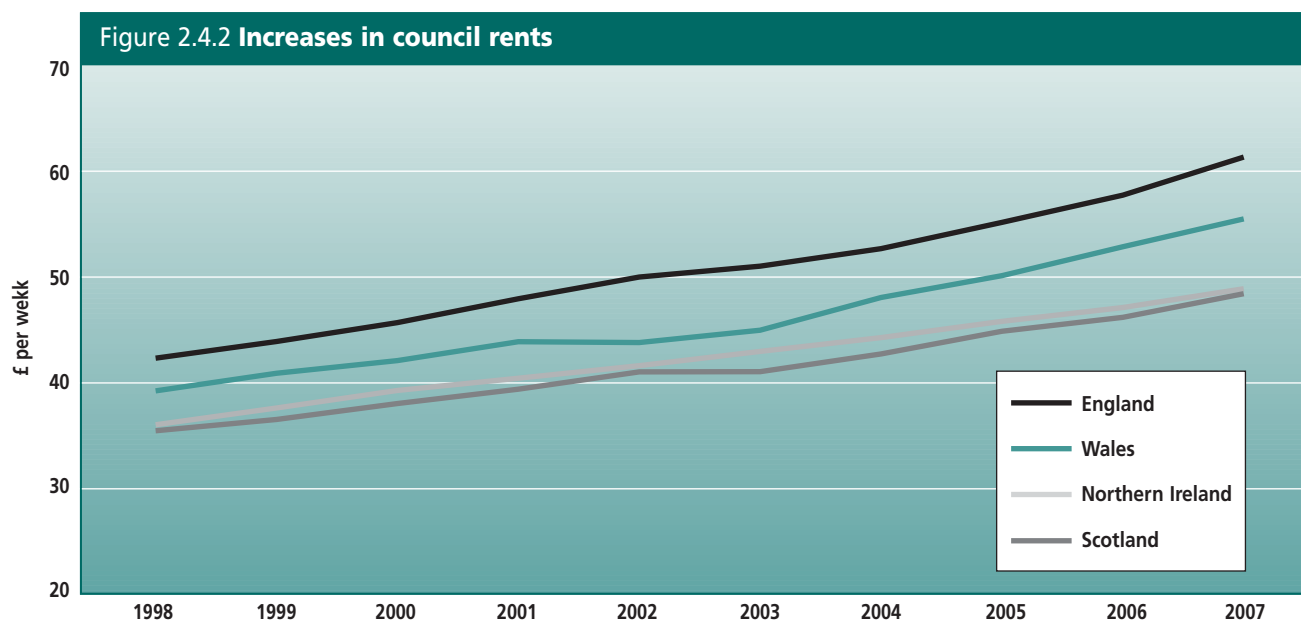
The asset management techniques will include:

- Better asset management to drive down costs or increase income.
- Tackling toxic assets.
- Disposals of voids (although this is not so effective in a falling market).
- Transfer of tenanted property, or stock rationalisation.
- Ultimately, the restructuring of landlords and their assets.

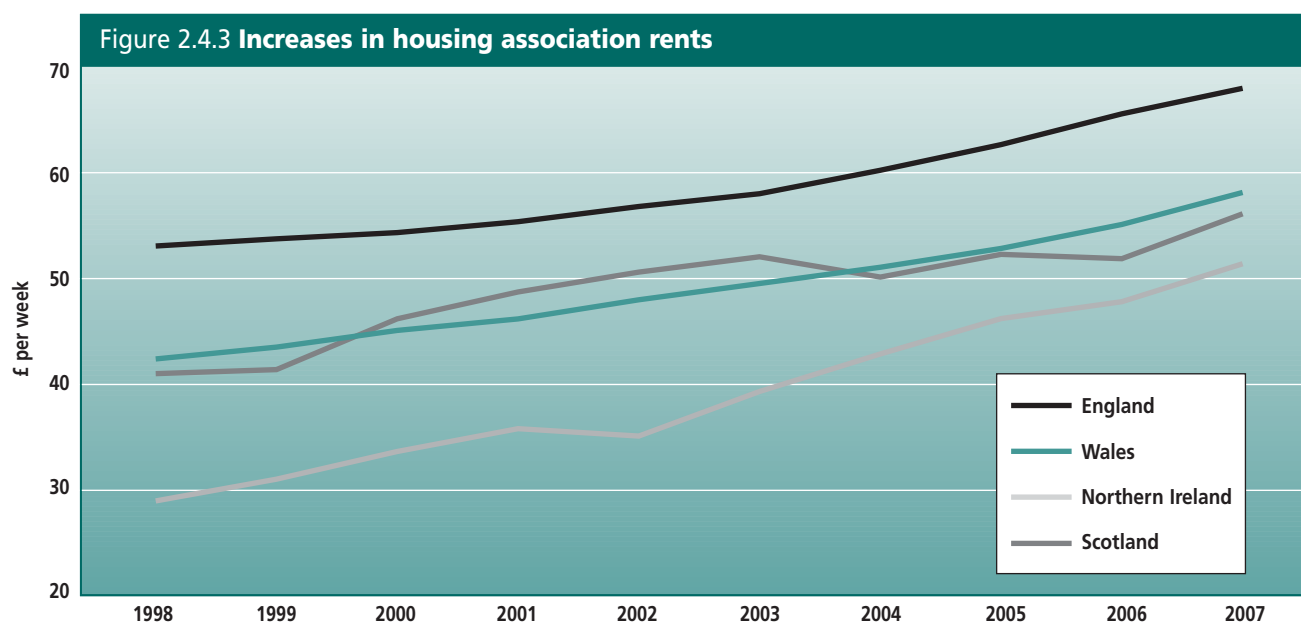
We have managed the transfer of over 4,000 homes. Our experience is that prices average £55,000 per home, which represents a premium over EUV-SH that this is fairly consistently in the range 20-50 per cent. Feedback from tenants is positive. The transferors enjoy increased liquidity to invest in other assets or simply to weather the recession. There are other advantages too; the recipients tend to be middle-scale associations with cash or undrawn facilities that the sector as a whole needs to mobilise.

Ultimately, the credit crunch may claim scalps. Savills’ long-term view is that the sector needs to be self-reliant and, to achieve this, will need a rescue fund based on the Dutch model.

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Sources: Compendium Tables 72, 79, 86 and 89.



Sources: Compendium Tables 72, 79, 86 and 89 and DSD Northern Ireland.

Notes: Rents are net of service charges. Northern Ireland figures for 1998 and 1999 are estimates.

In practice, council rents in Scotland and Wales, and NIHE rents in Northern Ireland, have increased less rapidly than those in England over the devolution decade. However, while in the initial devolution years this led to the UK Treasury making additional payments to the devolved administrations (for the consequential housing benefit savings), that arrangement was subsequently suspended, on the grounds that it was only intended to protect HM Treasury in the event of higher rent increases by the devolved administrations.

The changes in the levels of average council and housing association rents are shown in Figures 2.4.2 and 2.4.3. In England, council rents increased in line with median full-time earnings over the decade, while in Scotland and Northern Ireland the lower rate of rent increases meant that they declined relative to median full-time earnings over the decade. While rent increases in Wales were less rapid than in England, earnings growth in Wales was lower over the decade, with the net result that Welsh council rents rose slightly relative to earnings over the decade.

While lower council rents are clearly more affordable for tenants, they also represent less income being available for expenditure on repairs and improvements, and in both Scotland and Northern Ireland there would have been the opportunity to increase rental income by almost 1 per cent per annum, without either increasing rents relative to earnings, or more rapidly than in England (and thus incurring budgetary costs).

The relative changes in housing association rents over the period were quite different. Housing association rent increases over the decade were lowest in England, under the impact of the 'rent restructuring' policy intended to create more consistency in rent levels both between the council and housing association sectors, and between individual landlords.

While housing association rents in England remained higher than council rents, by the end of the decade, the gap between rent levels in the two sectors was significantly smaller. In Scotland, housing association rents increased at the same rate as council rents over the decade and consequently also became more affordable relative to earnings.

In Wales, housing association rents increased a little more slowly than council rents, and in consequence moved broadly in line with earnings over the decade. In Northern Ireland, under pressures to maximise outputs from a limited grant budget, housing association rents increased sharply over the decade. However, by 2007 they still remained the lowest in the UK; albeit by then they were some 5 per cent higher than NIHE rents, whereas at the beginning of the devolution decade they had been substantially lower than NIHE rents (Figure 2.4.3).

Future of rent policy

English government policies for both the council and housing association sectors were examined as part of the HRA review (see Contemporary issues Chapter 3). However, at the time of writing, proposals to reform the rent policy regime have not been put forward.

In the short term, discussion has focused around the annual uplift in rents, in a context where the September 2009 Retail Prices Index (used in the current annual rent adjustment formulae) registered a 1.4 per cent fall compared to last year. Under the current rent policy formula this requires an average 0.9 per cent reduction in housing association target rents in 2010/11.

At the time of writing, proposals for council rents in 2010/11 have not yet been made. However, it should be noted that last year the rent increase for council rents that would have resulted from last September's RPI spiking at 5 per cent was abated to just 3.1 per cent. If that abatement was unwound, and rent policy remained unchanged, this would generate a proposal for a 1.6 per cent increase in 2010/11.

However, the government may decide to introduce a policy change alongside its announcement of proposals for council rents next year. Certainly, in the short term, the recent volatility in the RPI measure, which in large part reflects fluctuations in home-owners' mortgage costs, has made its use as a routine indicator for the annual uplift in social sector rents rather problematic. One way of responding to that difficulty would be to switch to the 'Rossi' index, which is a measure of inflation that excludes all housing costs.² This measure is already used by the Department for Work and Pensions to annually uprate welfare benefits (on the grounds that housing costs are dealt with separately through housing benefit).

Further ahead, there will be pressures for more fundamental changes in social sector rent policies given the pressures on government budgets. Any decisions on rents policy in England will impact on the budgetary parameters within which decisions on rent policy are taken by the devolved administrations, that will in turn face similar financial pressures.

While increases in social sector rents raise concerns about affordability and work incentives, the harsh reality is that in net terms they could potentially generate substantial net savings for central government. Savings from reductions in grant rates and subsidies (or indeed increases in rent surpluses in the HRA) would potentially more than offset the direct (housing benefit) and indirect (inflation and work disincentive) costs of higher rents.³

Footnotes

1. This section of the chapter draws on work for the Joseph Rowntree Foundation, published in *What has devolution done for low income households? The case of housing*, S. Wilcox and S. Fitzpatrick, Joseph Rowntree Foundation, 2009.
2. Wilcox, S. (2009) *Baseline Uprating Options*, Housing Revenue Account Review Rents and Service Charges Working Paper, Communities and Local Government.
3. Wilcox, S. (2009) *Costs and Savings from higher rents*, S. Wilcox, Housing Revenue Account Review Rents and Service Charges Working Paper, Communities and Local Government.

Key Reading

Annual Report 2009, Communities and Local Government, Cm 7598, The Stationery Office, 2009.