Declining Housing Affordability in a Diverse Society: Trends, Causes and Consequences

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Abstract

UK housing policies are currently failing to meet the needs generated by newly forming households of increasingly diverse income, compositional type and ethnic group. Proper provision of appropriate healthy, safe and affordable housing for these varied needs, in the most cost-effective manner, is vital on grounds of social justice, health protection, economic efficiency and the avoidance of political tensions.

The paper offers first a legally usable definition of 'affordable'. Then evidence is presented of the declining affordability of both renting and owning. Since 1980 the proportion of average male earnings taken by rent has risen by 93% (public sector), 37% (voluntary sector) and 122% (private sector). In terms of owner-occupancy, the house price index has risen at twice the rate of earnings since 1970 and at five times the rate since 1993. The mortgage cost to average incomes ratio has worsened by 43% over the past decade and is highly differential by region.

This sharp worsening of housing affordability in both main sectors is largely explained by:

a) the loss of one half of the former public stock to higher rent tenures and sales
b) the adoption in 2001 of new rent-setting principles for 'social housing'
c) the highly disproportionate growth of house purchase lending since 1980

The last of these has inflated house prices and had the 'knock-on' effect of rapid land price inflation and volatility which adds to the costs of 'social housing' providers.

Because housing is a non-substitutable spending item declining affordability partially negates the effects of anti-poverty programmes and has a spread of other adverse

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Other empirical material in this paper derives from research work carried out over the past ten years in Stepney (east London), Brighton and Hove and Hastings in very fruitful collaboration with Dee MacDonald and Liz Cunningham, both Research Fellows in the Health and Social Policy Research Centre at Brighton University. The author would like to thank them for their care, professionalism and friendship.

non-housing outcomes. Research findings will be presented to show that as housing costs rise, spending on food, heating, recreation and other health-protective items is forced down. Demands on the health services are consequently increased. Household debt is increased and capacity to provide for personal pensions is reduced. Labour mobility is impeded and employers face increased recruitment and retention problems. Finally the cost of state-funded housing support programmes to assist with affordability has risen from £5bn to £18bn over the past 20 years while investment in social housing production has remained stagnant. In the light of these adverse outcomes a number of recommendations are advanced for consideration by policy-makers.

This paper is divided into sections. The first provides a brief note of the international context to show that rising housing costs, especially house prices, are giving rise to concern in many 'advanced' economies. The second section gives some summary data of the increasing diversity of UK society in terms both of ethnicity and income and health characteristics. The next section deals with some definitional issues. The fourth and fifth sections provide evidence of decreasing affordability in the two main UK housing sectors – the rented sectors and the home-owning sector. Each of these sections has three sub-sections:

a) evidence of declining affordability
b) a summary of the reasons for this and
c) a review of various adverse consequences.

The sixth section deals with some 'across the board' cross-sectoral cost effects of unaffordability and poor housing conditions. The final section outlines some strategic policy recommendations for consideration given the seriousness of this situation in the UK. An overall critique of UK housing policies, together with these recommendations, has been more fully written up in the Memorandum to the Prime Minister on Unaffordable Housing (Zacchaeus 2000 Trust, 2005 – also available at www.z2k.org).

1. The International context

At the time of writing rapid upward movements in house prices are a matter of concern, or at least serious discussion, in many countries. These include the US where prices have risen 73% since 1997, France (+87% over the same period), Spain (+145%), the UK (+162%) and Ireland (+192%) - see http://www.usatoday.com/money/perfi/housing/2005-07-20-europe-housing-usat_x.htm for some discussion. The same trends are evident in Australia where prices in Melbourne are still 60% above their 2000 level despite some signs of a 'soft landing' (see, http://www.theage.com.au/news/business/housing-economy-in-soft-landing).

There are several common factors behind these international trends. The recent era of low interest rates, especially in Europe, has cheapened credit. Lenders have become more 'flexible' in extending repayment terms up to 35 years (sometimes under 'interest only' arrangements). Both these factors have facilitated the borrowing of a larger capital sum in relation to any particular monthly income. Much of the buying is not for owner-occupancy. Many investors have turned to acquiring rentable residential property following some bruising experiences on the stock market.

The more widespread this trend, and the greater the dependence of influential investors on further property price rises, the more politically difficult will it be to take measures to regulate these tendencies and the keep house price trends in some sort of long term relationship with earnings and other consumer prices. Whether all this is a problem, or simply the acceptable workings of 'the market', is a matter for political judgement – so long as that judgement takes appropriate account of issues such as those raised later in this paper.

2. The UK as a diverse society

Diversity of incomes and health

The most recent edition of *Social Trends* (National Statistics, 2005) presents evidence that the high level of income inequality in the UK is not being reduced. Between 1994/5 and 2002/3 the real disposable incomes at the 90th decile and at the 10th decile grew at much the same rate leaving the degree of inequality unchanged (Figure 5.13). International comparisons show that the UK has the fifth highest proportion of children living in poor households of fifteen EU countries (Table 5.21). In terms of absolute dispersion inequalities are increasing. The incomes of the top 1% of UK earners grew fastest of all. In the 2002/3 the top decile had 28% of total income and the bottom decile 3% (Figure 5.14).

Several recent studies have indicated increasing divergence of health standards and life expectancy between richer and poorer groups and areas on the UK (see, Shaw, et. al., 2005). Differences have widened in the 1980s and 1990s and into the 2000s, latterly under New Labour administrations. These increasing divergences are linked to decreasing rates of intergenerational social mobility in which differential access to post-school education is deeply implicated (see, Blanden, et. al., 2005).

Increasing cultural and ethnic diversity

The most recent in the series of studies on the ethnic composition of the UK (see, Modood, T. et al., 2005), as well as the 2001 Census, has shown a strong tendency towards greater diversity. Apart from the sheer growth in numbers of non-white populations the Madood study showed the dramatic differences between the economic and social positions of the various non-white groups. These are in some ways as striking as the former 'white/black' divide. As a generality Pakistanis and Bangladeshis are among the poorest groups in Britain with 80% of households living at half or below average incomes. Those of Indian and Caribbean origins have had mixed experiences while many African Asians and Chinese are doing as well materially as any groups and are more likely than whites to be earning more than £500 per week (ibid.).

Many of the differences in health standards derive from socio-economic rather than biological characteristics. Comparatively Pakistanis, Bangladeshis and Caribbeans have very poor health, while African Asians, Indians and Chinese are as healthy as white people. In terms of career advancement the education system is failing young black men and Bangladeshi and Pakistani men and women, who continue to be disproportionately without qualifications.

As is well known, the workings of the UK housing system, both in terms of market processes and the allocation of council housing, has tended to segregate out different ethnic and socio-economic groups. As one of the authors of the Modood report commented:

> 'Members of ethnic minorities are more likely than whites to live in run-down neighbourhoods and to say that crime is a problem in the local area. While housing conditions for all groups have improved over the last decade, many Pakistanis and Bangladeshis continue to live in seriously over-crowded accommodation, often with poor amenities. Caribbean and Bangladeshi households continue to be under-represented among owner-occupiers.'

3. Definitional issues

'Social housing'

Some definitions used in the debate about UK housing lack clarity. The term 'social housing' is widely used to mean both rented housing in the local authority sector ('council housing' – about 20% of the UK stock) and housing owned and managed by housing associations or 'registered social landlords' (the RSL sector – about 10% of UK stock).

The adjective 'social' is presumably meant to imply that the housing is provided for 'social' purposes – in fact Mrs Thatcher once characterised council housing as housing for 'social cases'. In one way all housing fulfils a social purpose in the sense that almost everyone in society lives in it. But beyond this the term has no obvious meaning. It certainly does not mean 'housing provided with subsidy' since as will become clear all UK housing attracts elements of subsidy in varying forms. In fact in recent years the 'council' sector has been subsidising the rest of the economy since a net £630 million per annum has been abstracted from local authority Housing Revenue Accounts with obvious pressures on rent levels (see, Audit Commission, 2005).

'Affordable housing'

'Affordable' is also a term frequently used in a cavalier fashion. In Government-speak it appears to mean any housing that is available at something below the full market rent or price in any given locality. This is a distortion of language because the price or rent so defined bears no relationship to what the user household or person can actually afford. What is deemed to be 'affordable' in the former sense may be 'affordable' in the latter sense to households at one income level, or in one part of the country, but may well not be in other circumstances.

In the recent memorandum on housing unaffordability presented to the Prime Minister (see, Zacchaeus 2000 Trust, 2005) a definition on the following lines was offered:

> 'Affordable housing' means that once necessary payments on rent or mortgage (including service charges and Council Tax) have been made, be the household an individual, a family or people of pension age, there remains sufficient income to sustain safe and healthy living, support the needs of

any children of the household at school and participate in the life of the community. ‘Unaffordable housing’ means that the residual income left after all housing costs have been met is not sufficient for these purposes.

This definition meets the criteria of both common sense and legal defensibility but it is not the basis on which affordability is discussed in the next two sections. This discussion is necessarily based on official definitions and data.

4. Affordability in the rented sectors

Trends

Over the past century the degree of correspondence between income range profiles on the one hand and the spread of housing access costs on the other has weakened. It was found in the Central Stepney Single Regeneration Budget study of ‘health gain’ study resulting from the urban renewal (see, Ambrose, 2000) that the inhabitants of the streets undergoing redevelopment in the mid 1990s were, a century earlier, engaged in a wide variety of occupations, no doubt with widely varying rates of pay and levels of job security (1901 Census data). The Charles Booth poverty map of 1889 shows a wide range of housing standards in the area (from his Category 3 to Category 6 in a seven category scheme). Clearly if one’s income went up or down with a change of job there was housing of a wide range of quality (and therefore rents) that could be accessed locally – perhaps by means of a ‘moonlight flit’. By the mid 1990s not only had the local employment market collapsed (only 10.5% of the sample population were in full-time employment in 1996) but the housing choice was virtually limited to local authority housing. Given the rising trends in local authority rents an increasing dependence on Housing Benefit was inevitable.

Generalising this situation over a similar timescale it was found by Glennerster et al. (2004, Table 6) that rent as a proportion of expenditure for the poorest fifth of the population had risen from 18% to 28%, although allowing for housing support payments the net cost for the poorest was 6% of expenditure. This means that this net cost has to be found from the already inadequate income support payment and necessarily reduces expenditure on other necessities such as food. They conclude that ‘…while the quality of housing has improved enormously the variation in its cost has greatly increased.’

These different rent-setting mechanisms have in the past produced a clear ‘rent gradient’ – council rents have normally been lowest, then RSL rents then private rents. Weekly rents in 2003 as a proportion of average male earnings were (Wilcox, 2004, Table 72):

Local authority	13.3%
RSL	15.3%
Private	22.2%

Local authority rents for comparable properties are still lower than RSL target rents in all regions of England by a margin of typically 15-20% (see, Wilcox, 2004, Table 74). But the differential between council and RSL rents is narrowing. From 1980 to 2003 the percentage of average male earnings taken by rent rose differentially in the three rental sectors (see, Wilcox, 2004, Table 72):

Local authority	93%
Housing association fair rents/assured rents	37%
Private 'fair rents'/market rents (to 2000 only)	122%

In absolute terms average rent levels have risen sharply in all three tenure groups since 1980 (see, Wilcox, 2004, Table 72, not corrected for inflation):

Local authority	+666%
Housing association fair rents/assured rents	+464%
Private 'fair rents'/market rents (to 2000 only)	+685%

With the narrowing of the differential and the sharp rises in local authority rents the availability of decent quality housing at rent levels affordable by the very poorest is falling sharply with obvious consequences for affordability.

Given the trends towards widening income inequalities set out earlier and the severe reduction of state financial support to develop lower rent stock to match lower end incomes there is a growing structural problem of non-match between household incomes and housing availability. This is especially evident in 'high demand' housing areas. This structural problem is at present being dealt with by an ever-increasing reliance on Housing Benefit payments plus increasing dependence on high cost and socially damaging emergency solutions.

Reasons for the trends

The three main rental tenure groups in the UK formerly had sharply differing sets of processes for determining rents:

1 - Local authority rents

The main factor producing relatively low rents for council housing over many decades was not the subsidy from central government but the arrangements by which rents were averaged or 'pooled' across the stock of an authority.

Given, say, an eighty year life for a property the interest and loan repayment costs of any unit decay in real terms over time with inflation and then end altogether when the loan is fully repaid after perhaps thirty years. For the remaining years of its life, which may well be fifty years or more if the housing is properly built and maintained, the property attracts only management and maintenance costs but continues to produce rents that can rise with inflation. Given a local authority with a stock with a wide spread of building dates the average rent charged across the stock could be much lower than if the rent has to reflect current or recent building costs and debt servicing or has to be related to market rents or current capital values in the area.

This 'pooled historic cost' principle appears the soundest way to produce decent standard housing at affordable rents but it does depend on:

a) producing units of a quality such that their life will long outlast the period of debt servicing and
b) keeping the older stock more or less intact so that the costs of recent additions can be averaged with the historic costs of earlier units to produce an affordable average rent across the stock.

The costly technological errors of the 'high rise' era, the 'right to buy' and transfer policies of recent decades, the partial withdrawal of central subsidy and the policies forcing local authorities to rely increasingly on the private capital market for funds (see, the diagram in Appendix 1 of Zacchaeus 2000 Trust, 2005) have all worked to erode the formerly low rents of the council sector.

2 – Registered Social Landlords' rents

Rents in this sector were previously set to reflect the capital and running costs development by development. The costs were partly offset by government grant via the Housing Corporation, but they were not averaged with older stock in the ownership of the same landlord. So the 'historic' element of cost-pooling across units of widely varying age was absent and rent profiles were consequently higher than council rent profiles for similar properties.

3 – Private sector rents

Rents for private sector lettings have always been, and still are, set largely to achieve a competitive rate of net annual return on a particular property in the light of its current capital value and the ruling interest rate for investments of comparable risk. There need be no logical connection to building costs (the property may well be 100 or more years old) or to any requirement to average rents over a stock.

Recent rent re-structuring in the LA and RSL sectors

The new rent-setting principles set out in 2001 (*Guide to Social Rent Reforms,* Department of the Environment, Transport and the Regions) and 2003 (*A Guide to Social Rent Reforms in the Local Authority Sector,* Office of the Deputy Prime Minister) lead to the application of the same formula to both the local authority and RSL sectors. The details are complicated but in essence the weekly rent is based 70% on the average rent for the sector (LA or RSL) multiplied by a factor relating local earnings to national and then multiplied again by a bedroom weighting factor to reflect the size of the unit. The other 30% is based on the average rent for the sector multiplied by a local property value factor. This last element is significant because rents in these two sectors are now related to some degree to house prices in the area.

The intention is to move to these rent levels over a ten year period in equal annual steps with a limit on real terms annual increases of 1.0% in the LA sector and 0.5% in the RSL sector. Where high capital values produce excessively high rent levels a cap is applied on the annual rate of increase. The Government's intention is for LA and RSL rents, which were markedly different before the strategy was introduced, to converge over the period. The intention was to hold a three year review of how the system is working so as to feed into the setting of rents in 2005/06 but the review has not yet reported.

Adverse impacts of decreasing affordability

Since housing is clearly a non-substitutable element of consumption it is axiomatic that if affordability declines, i.e. housing costs rise in relation to income as has been shown, then expenditure on other items of household expenditure, for example food, clothes, transport, pension provision and recreation, will necessarily be reduced.

This effect was found in the study of 'health gain' associated with the renewal of some very poor standard housing in east London (see, Ambrose, 2002). The population of the two estates where the work was carried out are about 80% Bengali in origin but have mostly lived in the UK for several decades. The area is located in the London Borough of Tower Hamlets, an area of great ethnic diversity where almost half the population are non-white.

While some dramatic improvements in self-reported health were recorded following the housing improvements a detailed assessment of the household budgets of a sample of households revealed that living costs had risen by 27% as a result of higher rents, Council Tax and water rates (see, Ambrose and MacDonald, 2001). A number of responding households reported necessarily reduced spending on food, clothes and recreation – all forms of expenditure important for health protection. Ironically the increased housing costs following regeneration may well be detracting from the health gains noted.

Declining affordability is bound to squeeze expenditure on other key items unless payments from the state in the form of housing benefits and allowances exactly make good the decline in affordability. In the UK there is a complex array of means-tested benefits and allowances to help cover housing costs. But the growing dependence on these housing benefit payments, while currently necessary for millions of people, brings its own difficulties for recipients. These come under three main headings:

a) stress arising from the errors and pressures exerted by benefits agencies
b) very high marginal tax rates when moving into work and
c) take-up rates below 100%.

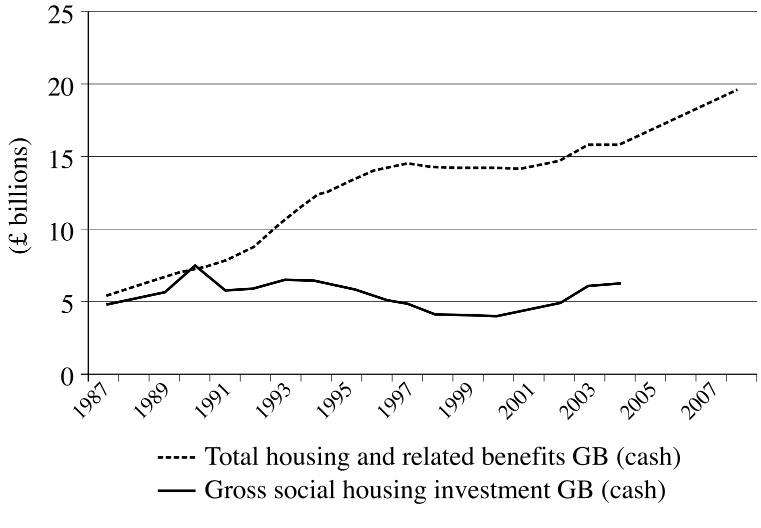
There are constantly occurring examples of stress stemming from bureaucratic errors and the 'blind' computer-driven forms of dealing with vulnerable recipients (see, Zacchaeus 2000 Trust, 2005, Appendix 7). The situation is exacerbated because, when dealing with those in arrears, RSLs and local authorities are often unaware of the National Standards for Enforcement Agents issued by the Lord Chancellor's Department in April 2002. These seek to provide a degree of protection for vulnerable and socially excluded debtors in a number of ways but they are not always observed.

When moving from benefit-dependence into employment the tapers on the benefits and the need to make tax and National Insurance contributions work in such a way that marginal rates of taxation become very high. In carrying out research on the 'Low Cost but Acceptable' wage level required for living in the Brighton and Hove area of southern England effective marginal tax rates of up to 97% were found when moving from benefits into work at the national Minimum Wage – in such cases the gain from working was just 11 pence per hour (see, Ambrose, 2003, Table 14). When so many households have to depend on housing benefit payments to enable them to access appropriate housing there are clearly disincentive effects to moving into employment. This runs counter to Government 'welfare to work' intentions.

Finally there is the take-up problem. While take-up rates for housing benefit and Council Tax benefit are high they are significantly below 100%. In 2001/02 housing benefit take-up rates for local authority tenants were in the range 89-94% and for private renters in the range 80-89% (see, Wilcox, 2004, Table 117). Take-up rates for Council Tax benefits were marginally lower than these and as low as 39-44% for eligible owner-occupiers. Take-up rates for both forms of benefit were especially low for non-child households and for pensioners.

There is a further problem arising from heavy dependence on housing benefits and allowances – the massively increasing cost of these payments to the state. As Figure 1 shows this is increasing very sharply while investment in the production of social housing has been static or declining in real terms. This raises the strategic issue of how best to achieve the most cost-effective balance of housing support (see, Zacchaeus 2000 Trust, 2005, Strategic Issue 4 in Appendix 1).

Figure 1: Social housing investment and housing benefit costs – 1987-2007



5. Affordability in the home-owning sector

Trends

There are a number of historical indices of UK house price changes and all tell much the same story. The Nationwide historical index shows an approximately eighty-fold growth in the current all-house price index from the end of 1952 (average price £1,891 = 100.0) to the end of 2004 (average price £153,778):

All houses	8,132.1
New houses	7,711.3
Modern houses	7,575.3
Older houses	9,880.4

These figures need to be compared to rises in earnings. The Nationwide average gross earnings index dates only from 1970. The changes in the gross earnings index and the all-house house price index since then are:

Gross earnings index	x 18.7
House price index	x 34.5

Thus house prices have risen at nearly twice the rate of earnings over the past 35 years.

Much of this divergence between the two indices has occurred over the past decade when house prices have outpaced earnings by a factor of over five:

1993-2004 change in gross earnings index	+59.1%
1993-2004 change in house price index	+306.8%

The same Nationwide source provides a series on the ratio of house prices to gross annual earnings. For much of the period since 1953 this has ranged between about 2.5 and 4.0. In periods of sharp house price inflation, for example in 1972-3 and 1988-90, the index moved up very close to 5.0. Since the second quarter of 2003 the index has been above 5.0 and it stood at 5.95 at the end of 2004. For London in particular the index has been mostly in the range 3.0 to 4.5, reached over 6.0 briefly in the 1988/89 period of inflation and has been over 6.0 for the ten quarters up to the end of 2004. Housing affordability is therefore worse in London than at any previous time since records began.

The ratio of mortgage cost to incomes devised by Wilcox (2004, Table 2.3.2) calculates the proportion of average incomes for all working households required to access an average first-time buyer home. This proportion for the whole of the UK has worsened from 12.5% to 16.1% over the ten years and from 13.3% to 19.0% for London – a worsening of nearly 43% in affordability over a decade.

The Barker Review (2004) noted that only 37% of new households could afford to buy in 2002 compared to 46% in the late 1980s. Similarly ODPM statistics (2004) show that the proportion of first time buyers aged under 25 has fallen from 25% in 1993 to 16% in 2003 and that the proportion of first time buyers paying in excess of £100,000 has risen from 6% to 46% over the same period. Clearly affordability for this group has diminished sharply.

The latest ODPM document (2005) seeks to address this issue with a First Time Buyers Initiative. The intention is to provide 15,000 new homes for first time buyers up to 2010 on land to be provided by English Partnerships from former National Health Service and other public sources. Half will be for ‘key service workers’. The homes will be sold at construction cost plus and there will be provision for occupiers to acquire equity shares. The landowners will have first refusal on resale.

The same document announces a Design for Manufacture competition to build up to 1,000 homes on English Partnerships land for a target cost of £60,000, 'without sacrificing quality' and with a view to mainstreaming 'high quality modern developments for volume developments'. This has been interpreted in some quarters as meaning homes will be available for £60,000 but unless firm steps are taken to ensure that resale prices are cost-related and rise only in relation to general inflation, rather than behaving in the same way as the general run of house prices, any affordability gain is likely to be short-lived.

Regional variations in affordability

The current regional variations in affordability are evident from the latest Joseph Rowntree Foundation data (Joseph Rowntree Foundation, 2004). This compares the local price of two and three bedroom houses with the gross income of households that include working people aged 20 to 39. The price/income ratios are:

England	4.11
London	4.69
South West	4.66
South East	4.61
East of England	4.27
West Midlands	3.80

Of the 10 local authorities with the highest ratios, five are in the South West, two (Westminster and Brent) in London and three (Chichester, Adur and Lewes) in the South East. All these except Lewes have a ratio over 6.0. It should be noted that the mortgage ratio of loan approved to income for a multi-earner household is rarely over 3.5. On this evidence access to home ownership is difficult, if not impossible, for first time buying households of this type in very large areas of England.

The area with the lowest ratio, 1.97, is Sedgefield (the Prime Minister's constituency).

Affordability and take-home pay

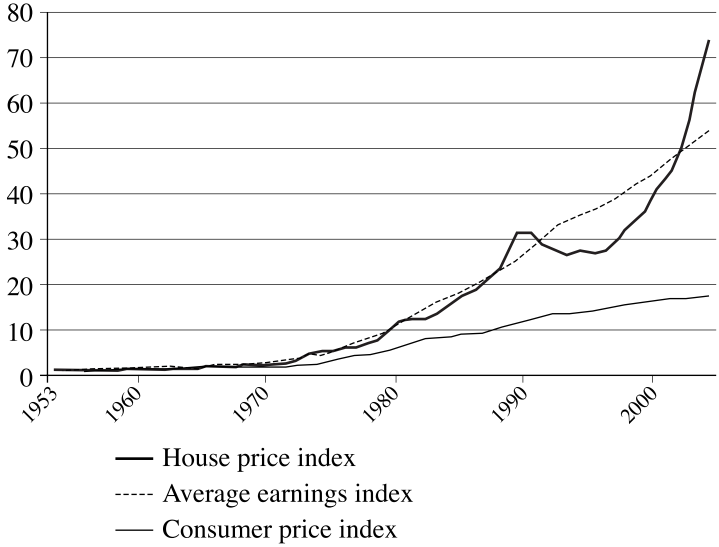
Affordability can also be measured in terms of the percentage of take-home pay required for mortgage repayments. The Nationwide series of this indicator runs from Quarter 1 of 1985 (index = 100). For the UK as a whole this index rose into the 150s during the 1989 house price inflation but was running in the 50s and 60s for much of the mid-1990s. It has now risen again and at the end of 2004 stood at 107.4.

Given the unprecedented rise in house price levels it may seem surprising that affordability, in terms of take-home pay used to pay the mortgage, should have remained relatively low in the early 2000s. The explanation probably lies in a combination of factors – historically low interest rates, 'low-start' mortgage products and lengthened repayment terms are all possible factors that reduce the month by month impact of expending higher capital sums on house purchase. Clearly there are dangers here if interest rates rise and/or disruptive life events such as unemployment, disability or relationship break-up occur during the extended repayment period.

Summary – earnings, retail prices and house prices since 1952

Figure 1 shows the movements in gross earnings, consumer prices and house prices since 1952. The gross earnings and house prices data are derived from the Nationwide website www.nationwide.co.uk/hpi/downloads/UK_house_price_since_1952.xls and the consumer price data from the Economic History Resources site www.eh.net/hmit/ukearncpi. All three series have been reduced to 1952=1.00. It is possible to take issue with the particular measures used and no doubt changes in definitions over half a century have produced some inaccuracies. But the main features of the comparative movements in the three indices are clearly discernable.

Figure 2: Earnings, Prices and House Prices 1952-2004



Until about 1970 the three indices remained in close touch and grew only very slowly. From about that year there has been a growing divergence between the consumer price index and the other two. Earnings have risen much faster than consumer prices until they now stand at about three times the prices index. This reflects the approximately threefold rise in real earnings and living standards that has occurred since the second world war and primarily since about 1970.

The house price index has behaved in a much more volatile fashion. It remained in close touch with the earnings index until about 1987. Since then it first rose faster than earnings, then fell back to well below the earnings index by the mid 1990s then rose more steeply than earnings until finally since 2002 it has risen to nearly 84 compared to the earnings index of about 55 (1952=1.00). Rough calculations show that if the average house price in 1975 (£10,000) had inflated in line with earnings the average 2005 price would be £98,000. If it had risen in line with the Retail Price Index, which as a consumer item one might reasonably expect, it would be £60,000. In fact the 2005 average house price is £154,000.

Why should this be? And why in particular should house prices get so out of touch with earnings and other prices?

Reasons for the trends

The historical context

When seeking to understand these trends some attention should be paid to historical context. Home ownership in Britain has a particular history. The value of mass owner-occupancy as a 'bulwark against bolshevism' had been argued explicitly in Parliament following the 1917 Russian Revolution and the 1926 General Strike (see, Bellman, 1928). In the 1930s Neville Chamberlain made the point that:

> '…every fruit tree planted [in the garden of a newly purchased house] converted a potential revolutionary into a contented citizen.' (see, Feiling, 1946)

The 1930s was marked by a massive growth in house purchase lending by the rapidly growing 'building societies' - from a total debt outstanding of £120 million in 1924 to £636 million in 1937 (see, Bowley, 1945). By the beginning of the Second World War home ownership had risen to about 40% of all households.

Following the heavy emphasis on building council homes by the post-1945 Labour Government, and the successor Conservative administrations till the late 1950s, it was the 1964 Labour Government in its White Paper *The Housing Programme 1965 to 1970* that advanced home ownership as a 'normal' tenure and part of a 'long-term social advance', to quote the White Paper.

Within a decade the political implications were once again spelled out by the Secretary General of the Building Societies Association when he made the point in the mid-1970s that owner-occupancy was now the majority tenure and that 'The greater proportion of owner-occupiers the less likely were extreme measures to prevail.' (quoted in Ambrose, 1976). He might have added that from that point on no General Election could be won on any programme that appeared to harm the interests of owner-occupiers.

'Price rise equals good'

Housing is the only ubiquitously used commodity where price rises are universally and uncritically welcomed as a good sign. The owner's personal calculation is almost always about the rising paper value of the property not about the rising proportion of lifetime earnings given over to buying it, the rising level of debt involved and the effects that debt may have on other aspects of life.

Similarly in urban regeneration schemes house price rises are seen as an indicator of 'success' although every price rise makes it that much more difficult for non-owning local residents to access ownership. More generally in discussions of the economy the headline 'Good news – housing market recovers' simply means prices are rising again with implied benefits for existing owner-occupiers. Economic benefits are also deemed to come out of increased spending deriving from equity withdrawal – while perversely the rising level of total debt gives rise to worried comment.

It is vital to re-examine this piece of conventional wisdom as it seems clear that the 'taken for granted' that rising prices equals good is in fact a highly partial interpretation of meaning by the more prosperous members of society (owners) against the interests of the less prosperous (non-owners).

Financial deregulation in the 1980s

The Thatcher administrations of the 1980s introduced a number of measures to deregulate and liberalise financial services and institutions. This formed part of a move in many western economies towards deregulation. In 1981 many restrictions on bank lending were abolished, in 1983 building societies were allowed to borrow from the money market and in 1986 the Building Societies Act introduced a more self-regulatory regime. Regulation was reduced on matters such as reserve ratios, interest rates, down payments and so on. Significant changes, including trends towards de-mutualisation, also occurred within the building society sector itself (see, Cook, Deakin and Hughes, 2001).

Deregulation led to increased competition in the home loans market, more house purchase lending from the clearing banks and the vigorous selling of endowment-linked mortgages where the capital debt is paid off at the end from the product of stock market investment. The vast majority of these have subsequently under-performed and it is estimated that over 60% of the 11 million endowment policies will not cover the full debt on maturity (http://www.uk-endowment-mortgages.com).

The growth of house purchase lending

One of the outcomes of the new deregulatory regime was a rapid growth in house purchase lending and thus in the effective demand for houses. As Baddeley (2004) points out:

> 'The increasing availability of mortgage finance will encourage self-propelling increases in house prices: the demand for residential investment will increase as liquidity builds up in mortgage markets and more mortgage financing becomes available on increasingly favourable terms.'

Since the supply of both new and second-hand houses in the market is relatively inelastic it is inevitable that increases in demand will have an effect on prices. The explosive growth in total house purchase debt between1980 and 2003 is shown in Table 1.

Table 1: The growth in house purchase debt 1980-2003

Year	HPD@RPI House purchase debt had it risen at the rate of RPI (1980 debt = £53 billion)	ADJUSTED HPD@RPI (to allow for the rise in owner-occupancy since 1980 – £ billion)	ACTUAL HPD (£ billion)	EXCESS OF ACTUAL OVER ADJUSTED HPD (£ billion)	HPD as % of GDP
1980	53	53	53	0	23%
1985	75	81	127	46	36%
1990	100	111	295	184	53%
1995	118	137	390	253	54%
2000	135	162	536	374	56%
2003	144	181	774	593	72%

Sources: Wilcox (2004) Tables 17d and 45 and www.ex.ac.uk/RDavies/arian/current/howmuch.html

The growth of total House Purchase Debt had it risen with general inflation is set out in the second column. This has been approximately corrected in the third column to allow for the growth in the number of owner-occupied units since 1980 since clearly the debt outstanding might have been expected to increase given this factor alone. The *actual* level of House Purchase Debt is in the fourth column and the amount by which this exceeds the RPI related figure is shown in the fifth column. The final column shows that as a proportion of GDP the HPD has risen from 23% to 72% in 23 years.

In 2003 HPD was £593 billion more than would have been the case had lending grown in line with retail prices. It is perfectly reasonable to assume that had house purchase lending grown roughly in line with other prices, or with the number of properties coming onto the market year by year, then house prices would also have remained roughly in line with other prices. In that case earnings growth would have outstripped both general and house price indices, thus producing real gains in living standards.

The reality has been quite different because the explosion in lending has massively increased effective demand and pushed up prices. The future seems set to produce more of the same. The Council of Mortgage Lenders *Market Briefing* dated December 2004 forecasts a total outstanding housing debt of around £1,100 billion in 2007 (compared to about £774 billion in 2003). Unsurprisingly the CML expect continuing house price rises, although at lower rates than in the past decade.

Increases in the lending multiple

It has been shown that house purchase lending, and therefore house prices, has risen much faster than earnings for some decades and especially in the last decade. One facilitating factor has been the increase in the multiple of loan made to the current income of the applicant and to taking more fully into the equation the earnings of second and even other members of a household (part of the ‘increasingly favourable terms’ referred to in Baddeley, 2004). The higher this multiple the higher the house price that can be afforded by the purchaser(s) in relation to current income (but of course the higher the debt incurred).

Table 2 shows the multiple has increased considerably since 1984 – by 42% for first time buyers and 39% for movers. This has enabled house price levels to rise disproportionately more than incomes and on the basis of the increase in credit granted. Beyond a certain point increases in this multiple are likely to be unsustainable by a significant proportion of borrowers, especially if interest rates rise or personal circumstances change.

Table 2: Changes in lending multiples

	First time buyers		Movers	
Year	**% of total loans**	**Income multiple**	**% of total loans**	**Income multiple**
1974	44	2.18	56	1.96
1984	50	1.99	50	1.95
1994	55	2.34	45	2.24
2003	29	2.83	71	2.72

Source: Council of Mortgage Lenders website www.cml.org.uk

Another notable feature is the sharp swing over the past decade in the balance of loans away from first time buyers and towards existing owner-occupier movers. This supports the general understanding of the increasing difficulties faced by those seeking to access home ownership. The CML *Market Briefing* forecasts a modest recovery in the first time buyer proportion but only to 34% by 2007.

Government incentives to purchasers and owners

Mortgage Interest Tax Relief which was costing the Exchequer £6 to £8 billion per year in the early 1990s is now much reduced (to £1.6 billion in1999/2000 - Wilcox, 2004, Table 105). But to offset this the value of Capital Gains Tax Relief to owner-occupiers has risen over tenfold since 1997/97. This has been a burden on the national economy. The net gain to the Exchequer from Stamp Duty and Inheritance Tax offset by Capital Gains Tax Relief has fallen from £1.39 billion in 1999/2000 to £0.55 billion in 2002/03 (ibid, Table 1.2.3). In addition Housing Benefit which now costs £12.6 billion annually in Great Britain (ibid, Table 114) is largely a subsidy via rents to landlords and, argues the Henry George Foundation (see, Lloyd, 2004):

> '…a further source of house price pressure, pumping public money into an already overheated market.'

They also argue:

> '…it is futile to improve affordability by increasing salaries or subsidising home buying…While each individual home buying grant – such as those under the Starter Homes Initiative – may help the recipient enter the housing market, the combined effect of such grants is to push the market up further, making entry even harder for the next grant recipient.'

The political barriers to reform

This section opened with a brief reference to the pro-ownership politics of the 1920s and 1930s. All UK governments since then have shown themselves to be wary of the perceived electoral sensitivities of the wealthy homeowners of 'middle England'. In particular, negative equity is seen to be unacceptable in any form. However, the consequences of this position are unsustainable. For negative equity to be avoided, homeowners must be effectively subsidised in perpetuity. The current assumption appears to be that homeowners have a right to profit from rising prices but no corresponding duty to carry the risk of a price fall. This also implies that current owners have a right perpetually to extract wealth from first-time buyers, that speculators on the housing market have a right to keep all their winnings and a right also to state compensation if they lose. It is hard to imagine how any other group demanding such a settlement would be treated.

There may now be some inconsistencies creeping into public attitudes. The British Social Attitudes Survey reported in the latest *Social Trends* (Table 5.15) indicates that 78% of all adults of 18+ think that the gap between high and low incomes is 'too large' but this gap is probably not related in the public mind to housing policies and practices.

Adverse impacts of decreasing affordability

Rapidly increasing house prices, and the heavy debt that underpins them, give rise to a number of adverse consequences and enhanced risks. Some of these have so far attracted little research effort. Others seem intuitively likely or have been identified anecdotally but now require systematic research.

Risk of repossession

Inability to continue servicing a housing debt can lead to calamitous outcomes if the property is repossessed. If it is subsequently sold by the creditors for less than the loan outstanding the occupiers not only lose their home, they also remain in debt.

Repossessions in the UK rose to very high levels in the early 1990s (75,540 in 1991) but have since fallen considerably (7,630 in 2003 – Wilcox, 2004, Table 51). Both this figure and the sharp reduction in the extent of mortgage arrears probably reflect the historically low interest rates of the early 2000s. Nevertheless court actions entered for mortgage repossessions have shown little sign of decline over the period 2000-2004 (ibid, Table 52). Of the total Court Orders made for repossession in 2003, 29.1% were in London and the South East (ibid, Table 53f). In these areas average weekly mortgage repayments including endowment payments in 2002/3 were £138.60 and £133.34 respectively compared to a UK average of £97.41 (ibid, Table 50).

Effects on land values

As has been shown (see, Zacchaeus 2000 Trust, 2005, Appendix 9), the rising prices of newly developed houses feeds through to inflate development land value, with consequent implications for the buyers of land for 'social' purposes.

One impact of sharp cyclical changes in the price of development land is to make such land a fruitful area of speculation by long term investors or by larger housebuilders.

In some stages of the cycle builders can make more profit from land dealing than from actual construction. This provides very little incentive for builders to compete on grounds of innovation and building efficiency (see, Dickens, et. al., 1985).

Effects on private sector rents

Private landlords are seeking to gain a competitive rate of return on the capital value of their assets so the higher capital values go the higher the rent they will seek. The impact of this chain of logic was seen in the figures given earlier about the rate of rent rises in the private rented sector.

There has been an increasing trend in the UK for council housing to be sold to 'buy to rent' investors. The number of 'buy to let' loans has increased sharply (see, Wilcox, 2004, Table 55):

End of 1998	28,700
End of 2000	120,300
End of 2003	408,300

This has the effect of transferring significant numbers of units from council renting to private renting. As shown earlier it is private sector rents that have outpaced the other categories over the past two decades both as a proportion of average earnings and in absolute terms. Finally it is also relevant that the house sales and transfers normally include the freehold land on which the house stands so this becomes a factor precluding the future development of this land for low rent housing by the local authority. It also precludes the local authority from benefiting from future land value rises.

Effects on the bargaining power of organized labour

The relationship between high levels of mortgage indebtedness and trade unionists' potential and propensity to take industrial action has been recognized since at least the 1920s: the commitment to mortgage repayments is the most frequently stated reason for not joining a strike.

Effects on fertility rates and age of having a first child

It was shown earlier that 'mortgage multiples' have been rising, partly by taking more account of the income of second earners in households. The more the income of second earner is taken into the loan calculation the more it is likely that couples will put back the age of having a first child and perhaps further children. The number of live births per 1000 women in the UK has changed as follows:

	1981	**2002**
All ages	**62.1**	**54.3**
20-24	106.8	68.2
25-29	130.4	91.3
30-34	69.5	89.8
35-39	22.4	42.8

Source: *Social Trends 34,* 2004, Table 2.16

Fertility rates are down in total and are sharply down in the under 29 age groups. But in 2002 women in their early 30s produced far more babies than in 1981 and for those in their late 30s fertility has almost doubled.

This pattern is no doubt the product of a number of factors and it is differentiated by socio-economic group. Increased and longer participation in the labour market, often related to the servicing of a mortgage, may well be one of the factors affecting the fertility of those in socio-economic groups able to access a mortgage loan. Given the possible incidence of more complications for older mothers there may well be implications for NHS costs arising from these changing patterns.

Effects on family life

The continuance of both parents in work following the birth of a child, which may be necessary when both incomes have been calculated into the mortgage multiple, may have a range of effects. Some may be judged positive and some negative. Very often the requirement that two incomes continue may close down preference options about patterns of parental care and increase the need for bought in childcare.

Effects on other lifetime spending

As argued earlier it is axiomatic that the higher the proportion of lifetime earnings devoted to property purchase the lower the proportion available for other forms of spending. The shift is towards capital spending and away from revenue spending at the household level.

Complications when life goes wrong

Higher loan multiples and longer lending periods mean increased exposure to risks when household finances are disrupted by frequently occurring factors such as relationship breakdown, redundancy, poor health or disability. Increased stress may be felt not only when these events occur but also in the period when they are clearly on the horizon.

Effects on the quality of life of older parents

In the latest burst of house price inflation since the later 1990s it is clear at least anecdotally that many older parents are making use of their own capital to help children in their 20s and 30s to get on the 'property ladder'. This issue appears to have been little researched so its precise extent and effects are not known although one survey carried out in 2004 by MORI for the Joseph Rowntree Foundation found that parents now expect to contribute on average £17,000 to help their children get onto the property ladder.

Equity withdrawal and increased consumer debt

Steeply rising house values have given more 'headroom' for owners to borrow for other purposes. It has been pointed out (see, Wilcox, 2004, Section 2) that the recent rise in house prices has permitted record levels of equity withdrawal. This rose from £45.6 billion in 2002 to £60.8 billion in 2003. It amounted to 8.77% of all consumer spending (ibid, Table 7), a much higher proportion than that reached in the house price boom of the late 1980s. As the previous appendix made clear there is considerable scope for increase in this proportion.

This has a number of effects on the economy and the society. It clearly contributes to economic growth and indirectly to employment levels. But equally it has an inflationary effect and has been one reason behind the five increases in the Bank of England base rate since October 2003. Increased spending is conventionally seen as an unmitigated economic benefit. But at a time of deep concern about the social and cultural implications of very high borrowing levels, especially when the debt is incurred by more vulnerable borrowers, 'economic growth' may well not be the prime indicator by which the health, morality and cohesion of a society will be judged.

Constraints on use of the interest rate as a cyclical regulator
Governments of all political colours have in the past used the base rate as a regulator either to lift the economy out of recession or to dampen down an overheated economy. The facility with which base rate can be adjusted upwards is significantly restricted when the financial viability of millions of heavily indebted households is put at risk by upward movements in mortgage interest rates. The issue may well become more a matter of electoral calculation and less of economic judgement.

6. Cross-sectoral consequences of unaffordability – the 'exported costs'

> 'If property prices rise more than in proportion to incomes then, given the unequal distribution of property ownership, there will be an increase in the degree of income and wealth inequality…The distribution of wealth, unless offsetting forces are put in motion, will move secularly in favour of the owners of property.' (Corry, 1972)

The evidence presented in this paper confirms Corry's prescience. It has shown that increased housing unaffordability and shortage has a range of consequences, many of which may be judged to be adverse. It appears that some of these effects impose heavy 'exported costs' on a range of non-housing budgets (for a fuller discussion see, Zacchaeus 2000 Trust, 2005, Appendix 14).

The consequences include:

Regressive effects on the distribution of income and wealth
The Government has spent massive sums on the anti-poverty measures to supplement low incomes for families and pensioners since 1997, the year in which the numbers of children in households under the poverty threshold peaked. But inequality may well depend as much on the relative size of necessary outgoings as on adjustments of income. The proportion of income devoted to housing costs tends to rise as one moves down towards the bottom of the income scale and this may well indicate that the lack of affordable housing is a factor in the persistence of inequality. Regressivity in housing support and Council Tax costs may be a factor partially negating anti-poverty measures based in income supplementation (see, Zacchaeus 2000 Trust, 2005, Strategic Issue 7 in Appendix 1).

It also seems clear that the Corry quote at the head of this section is justifiable in that the housing market as it stands is an effective device for channelling wealth away from those who do not have it into the hands of those who do, in other words it has *a systemically regressive* effect. This may help to explain why the share of total UK wealth held by the most wealthy 10% has risen from 52% in 1996 to 56% in 2002 and why the poorer half the population own only 6% of the total wealth (see, National Statistics, 2005, Table 5.25).

Reduction in the level of inequality and poverty may well depend on an acceptance by policy-makers that the housing market as it exists is inefficient, inequitable and ultimately unsustainable and that some fundamental issues have to be addressed. In particular there is a need to recognize the axiomatic truth that to make housing more affordable house prices have to come down, or at least be stabilised, in relation to incomes.

Adverse effects on labour recruitment, mobility and wage costs

The lack of affordable housing in 'high demand' areas reduces labour mobility and causes additional difficulties for employers who seek to attract and retain workers in lower paid jobs. The high cost of a non-substitutable commodity such as housing is likely to find its way into higher pay claims or employers in high housing cost areas may well have to offer higher wages and relocation packages to attract key workers. Having attracted the workers they may experience retention problems as employees find the housing costs unsupportable on their incomes and a high rate of staff turnover imposes its own costs. This has applied especially to the recruitment and retention of nurses. In June 2005 the Royal College of Nurses drew attention to the loss of nurses to the profession for this reason, Edinburgh hospitals reported a crisis of staffing and the maternity unit of a Sussex hospital is likely to be downgraded for the same reason with possible serious implications for maternal health. Equally from the point of views of employees the highly differentiated housing costs in the UK can act as a serious impediment to job mobility.

This understanding that a sufficient affordable housing is a necessary item of infrastructure to underpin the efficient functioning of the economy has found expression in a new campaign, the Campaign for More and Better Homes. This was initiated early in 2005 by an alliance of unprecedented breadth including Unison (a large public sector union), the Confederation of British Industry, Shelter, the National Housing Federation, The Town and Country Planning Association, CABE and two of Britain's largest housebuilders, Wilson Bowden and George Wimpey. The campaign is urging the South East of England Regional Assembly to recognise the acute shortage of housing in the south east and to increase significantly the number of homes built in the light of both market demand and social need.

An increased risk of getting into debt

Clearly the financial pressures on households facing rapidly rising housing costs may well increase the risk of their incurring serious consumer debt. A recent project in Brighton and Hastings (see, Ambrose and Cunningham, 2004) found that the households surveyed, many of them benefit dependent, were in debt to credit card companies, banks and store cards to an average of about £9,500. The 'triggering events' were often housing-related, including accommodation problems on relationship break-up or delays in receiving housing benefit or overpayments by mistake. This had knock-on effects in that debt itself was a frequently quoted impediment to entering employment. Increased debt was also one of the outcomes of the increased household costs in the Stepney study (see, Ambrose and MacDonald, 2001).

Adverse effects on health
There is now a rapidly growing literature on the adverse health effects of poor housing conditions and housing shortage on mental and physical health. Some attempts are now being made around the world to calculate the cost of these housing problems to a range of public budgets but this work is at an early stage (see selective reviews of this literature in Zacchaeus 2000 Trust, 2004 and 2005).

Adverse effects on education
There is also a growing literature examining the nature of the links between housing factors - including conditions, degree of crowding, price and stability of occupancy - and educational achievement at school (for an early review see, Ambrose, Barlow, et. al., 1996 and more recently Clark, et. al., 1999). A spokesperson for Shelter (the UK national campaign for better housing provision) has made the point that:

> 'Reading…takes concentration. If there is no silence, you're in a room with four or five other children and the TV is always on, or if it's freezing cold and damp, you have no chance.'

A recent AHURI study in Brisbane and Sydney (see, Phibbs and Young, 2005) explored the link between movement into improved housing conditions in assisted public housing and a number of positive 'non-housing' outcomes. The populations had previously been housed in privately rented housing with a pattern of overcrowding, poor security and frequent moves. Following the moves surveys indicated more money to spend on food, more space to prepare it (reducing reliance on pre-packaged food), greater tenure security, less mobility and better neighbourhood safety. The better home conditions, residential stability and home space were correlated with better subject performance at school by 53% of respondents. These beneficial effects were confirmed in interviews with teachers.

It seems intuitively evident that the additional investment involved in re-housing families in better conditions had generated a pay-off in terms of a more cost-effective return on educational investment. The next step must be to put some serious research resources into quantifying this financial pay-off in relation to the cost of the housing intervention.

Opportunity cost of the unregulated house purchase lending
It was shown earlier that the amount of largely unregulated house purchase lending over

the post-Thatcher years has been almost £600 billion more than might have been expected had lending volumes risen in line with general consumer prices. The housing debt outstanding has risen from 23% to 72% of GDP.

This vast lending flow has been used to inflate house prices when it could alternatively have been invested in public infrastructure (schools, roads, hospitals, etc.) or in more productive ways such as the updating and capitalisation of UK industry, the research and development of new inventions and so on. It is also instructive to compare this £600 billion figure with the estimated £20 billion now required to bring all social housing to a decent standard or with the estimated £150 billion to modernise the National Health Service.

The modelling of alternative investment flows over the past quarter century would be a complex task but intuitively there seems little to be said for the way in which house purchase lending has come to dominate the use of investment funds in the economy.

7. Policy recommendations

The evidence and analyses presented in this paper summarise those presented in the form of a Memorandum to the UK Prime Minister in May 2005 (see, Zacchaeus 2000 Trust, 2005). This Memorandum offered a number of recommendations for consideration by various departments of state. They include the following:

- instigate and fund some systematic research to assess the cost of poor and unaffordable housing on both housing and non-housing budgets
- adopt the strategic aim of ensuring that rents in all rented sectors rise more slowly than earnings over the next decade
- to help achieve this aim stop all sales and transfers of council-owned housing and move rent-setting strategies back to some cost-related basis
- reconsider the overall balance of supply side to demand side housing support and take steps to shift the balance back towards the supply side so as to stimulate production not rents and prices
- take firmer control of the flow of house purchase lending so that it comes into better balance with the rate of property transactions and with the current earnings of applicants
- develop and support more ethical lending practices that are consistent with the variety of belief systems held in an ethnically diverse society
- consider measures to ensure a better flow of development land, to eradicate land speculation by fiscal means and to maintain more freeholds in public and community ownership
- develop and support more ecologically responsible building technologies and planning strategies

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