high aspirations, sound foundations:

a discussion report on the centre-ground case for building 100,000 new public homes

By John Healey MP

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T H E S M I T H I N S T I T U T E

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Contents

I have tried to present the argument here in simple terms but well-grounded in the best available data and analysis. In so doing, I gratefully acknowledge the support of Jonny Glyn (a secondee from PwC who helped with the financial modelling which is presented in section 3), John Perry, Professor Steve Wilcox, Matt Keep and Rod McInnes at the House of Commons Library, and the Smith Institute for their contributions and comments. Above all, I must thank and pay tribute to the work that James Hall has done with me on this report. All errors of course remain mine alone.

Preface

Preface

After five years of failure under the Tories, this discussion report aims to kick off part of the new debate I believe is needed in the country about the housing costs crisis. It is not new Labour policy. It is analytical and illustrative, not prescriptive so it makes no recommendations.

But it does show that there are alternatives to Britain's intensifying housing crisis and ever-escalating housing benefit bill. It also shows how government decisions are making the problems worse, not better.

This is the first half of the first year of a new five-year Parliament. It is time for a serious debate about the problems millions of people face with little hope of a decent affordable home to buy or rent. And about the proper responsibilities of government.

Everyone knows the housing market is failing and can see that current policies aren't working. Things must – and can – change.

John Healey MP

Introduction

Introduction

My central proposition for debate is this: we can't build the homes that our country needs to comfortably and affordably house our children and grandchildren without a substantial and sustained programme of public house-building.

Building more new council and housing association homes isn't just good social policy. It's sound fiscal policy too. Because, like any other good investment, spending on these homes yields a return. In this case not just rent from tenants but also lower housing benefit spending, because cheaper rents narrow the gap between housing costs and family income which housing benefit has to fill. It is better for tenants, and better for taxpayers.

For decades we have not been building the new homes we need in Britain. The housing market has failed, is failing and will continue to fail. And when markets are failing, smart state intervention is imperative so there's a good economic policy case for action too.

Government has a duty to act. It's simply indefensible for government ministers to deny responsibility for ensuring people are decently housed and for helping the next generation get on. An affordable home isn't a 'nice to have', it's the bedrock for the lives and futures of individuals and families throughout the country.

Right now the country is going backwards – home ownership has fallen every year since 2010, homelessness is rising, rents are up, 63,000 social rented homes have been lost in the last five years alone and last year only 124,500 new homes were built in England, half the number we need. Instead of stepping up to the challenge, the government have stepped back and made the biggest cuts to housing support and investment in a generation. Ministers are deepening and re-enforcing an orthodoxy that maintains housing is a private problem for private individuals, even as the difficulties people face become increasingly insurmountable however many extra hours they work, or how many more years they save.

The government is, of course, mindful of the ballooning housing benefit bill – up by over £4 billion in cash terms since 2010 and set to rise in every year of this Parliament. But they won't admit that pressures from more costly private rented homes and higher social rents are driving up the benefit bill. Instead, ministers look to deal with the symptoms, not the causes by bringing in the 'bedroom tax', denying housing benefit to 18-21 year olds and freezing housing benefit levels for four years.

Nor is this problem entirely party political. My own party has done too little to reshape the housing debate and and in opposition we were too timid about making these bigger arguments.

Now the election has passed, it is time to think bigger and speak bolder about how we fix the chronic housing problems in this country.

That inescapably means talking about building more council and housing association homes. While the housing crisis and housing aspiration must be met with action in all areas and contributions from all sectors, I concentrate here on affordable public housing to rent and buy that has been most overlooked and run down over the last three decades.

Just as affordability is imperative for renters and for buyers in the private sector, so it must be for public homes too. If as I set out here we make good on the potential of housing association and councils to build many more homes, there is no reason why an increasing proportion of those shouldn't be affordable homes to buy. As with rented homes, what's important in any such scheme, and in contrast to current schemes, is that it be affordable to future as well as current buyers, preserving the public stake and investment for the next generation of home-owners too.

Of course some claim it's no longer possible to think big when it comes to building public homes. But as I saw in my time as housing minister during the wake of the global financial crisis the objections melt away if the political will is there.

In less than a year we switched an extra £1.5 billion of capital funding – from all areas, including transport and the Home Office – to build new homes. Alongside buttressing the private house-building industry to stop developers going under, we set up the biggest capital investment programme in a generation, got councils – Conservative as well as Labour - building again through the local authority new build scheme and set in train the devolution of housing finance to put local authority housing on a sustainable footing for the future.[1]

Just as we learned in the second world war, the tools we use in response to crisis can be put to use in peacetime too.

The fact is that there's a centre-ground case for new publicly funded homes. As politicians of all political persuasion recognised in the decades after the war, housing is pressing enough a concern for millions of people in this country for every part of the housing sector to play a role.

1 See Smith Institute/PwC report on *HRA: one year on* (2013)

Private developers yes, but also councils as the public authorities most aware of housing need in their areas, and housing associations too – still probably the most successful partnership between private and public endeavour since that relationship was formalised at the start of the last century. This case has been neglected in recent years. And, as under this government, neglect has turned into outright opposition.

The aggressive hiking of traditional affordable rents to near private market rates, the phasing out of grant investment for new build, the scaling back of the contribution of private developers to build affordable homes out of the profits that public planning permission allows them to make and the extension of the Right to Buy. These add up to a sustained attack on the existence and future of affordable public rented homes.

It needn't have been this way. David Cameron was faced with a choice when he entered Downing Street in 2010, between two Conservative traditions on housing. The extreme of Margaret Thatcher, under whom the number of new homes built fell to the lowest level then on record and the housing benefit bill trebled to £10bn a year. Or the mainstream of Harold Macmillan, who built a quarter of a million homes a year in England, almost half of which were council or housing association homes for people on low and middle incomes.

Cameron chose the former, shunning Macmillan and rebooting Thatcher, with the same dire results. Fewer homes being built, house prices and rents soaring, home ownership the lowest for a generation and housing benefit costs at £25bn a year and set to rise further. This increased housing benefit bill is not, as the Prime Minister alleges, the fault of tenants or housing providers, but a predictable result of government policy - higher 'affordable' and an increased reliance on the private rented secror at a time when incomes have failed to keep pace with housing costs means that more people rely on state help.

There is now a duty on those of us committed to a future for public housing to make the case that there is another way, and that this deserves cross-party discussion. In this report I make this centre-ground case. I set out first the main arguments for new public housing, before explaining why the public financing of new homes should be seen and treated as investment, not subsidy.

Section one makes five big arguments for new public homes. First, because commercial house-builders simply can't build the homes we need by themselves. There's only been one year since the end of mass public house-building in the early '80s when we've built more than 200,000 homes in England.

Second, because Britain has a housing costs crisis that affects millions of households, made significantly worse by low building rates.

Third, because affordable housing helps increase the incentive to work, making work pay more for many households on low incomes.

Fourth, because public investment in house-building provides an important economic boost in all parts of the country, still important at a time when the economy is operating below capacity and for smoothing wider economic swings.

Fifth, because new public housing investment can pay for itself, which is perhaps the most critical element of the case for re-launching large scale public house-building. This was the purpose of the economic modelling project I undertook last year and is the central argument that I develop in more detail in the rest of the report.

Section two examines housing's 'canary in the mine' – housing benefit. Central government spends a lot of public money on housing, but it doesn't spend it efficiently. In this Parliament, central government spending to meet housing costs through housing benefit is forecast to be £120bn – almost 40% of which goes to landlords in the private rented sector. Investment funding in grants for building new affordable homes over the next five years will be little more than £5bn.

The core of the investment case for the Exchequer is that we can help people on low and middle incomes get affordable accommodation much more efficiently by rebalancing this split in spending. I show how the recent history of rising housing benefit spending has gone hand-in-hand with the decline of public house-building and chart some of the causes of ever-escalating cost.

Section three presents the results of a financial model we designed and constructed to test the sensitivity of housing benefit spending to a range of policies, and in particular the financial effect of a new programme of public homes. I set out a combination of tried and tested policy changes which could build 100,000 new public homes a year by 2020, and make the taxpayer a profit at the same time. I outline two big changes made in the last Parliament. First the de-linking of housing benefit for private tenants from local rents; and second the shift to near-market 'affordable' rents in the social sector. I also offer some options for how the machinery of government itself must change in order to deliver a new approach to housing investment.

I conclude with three challenges for advocates of affordable public homes that must be met.

1. Cost
Even though, as I show in this report, the long-run benefits of more public homes outweigh the upfront costs of building them, advocates need to find the language and arguments to justify that investment.

2. Public support
Public housing once offered homes for all and a sound start in life for people on low and middle incomes, but in more recent decades it has been increasingly reduced to welfare provision for the poor so advocates have hard work to do in persuading voters – most of whom own their home – that investment in new affordable homes is a good use of public money and worthy of support in their local areas.

3. Delivery
Scaling up our public house building from the current low base (and the skilled work force to deliver it) will be a significant administrative and organisational challenge, one which will require the efforts and innovation of all parts of the housing industry.

A short appendix outlines some technical details on the modelling exercise reported in section three.

Finally a question - why write a report on affordable public housing now, when the prospects of such a programme seem more remote than at any time in our recent history?

The answer is that now more than ever the case for public housing must be made, both because of the pressing need for new affordable homes and the existential crisis now confronting public housing.

Each generation faces the responsibility to redefine a vision for the future, renew the arguments for progressive change and refresh a public conviction that things can be better. It falls to us now as politicians, housing professionals and campaigners to remake the case for public housing in these most testing times.

For as the post-war health and housing minister Nye Bevan said of the NHS, so it is for public housing – it "will last only as long as there are folk left with the faith to fight for it".

Section 1

The need for affordable public homes

The need for affordable public homes

We face a housing and cost of housing crisis greater than at any point since the aftermath of the second world war. Britain is not building enough new homes, and the accommodation that is available is increasingly unaffordable to millions of people. It is a measure of a nation's politicians whether they can rise to the big challenges their country faces. And a measure of wider civil society whether they demand our politicians do so. Housing is now such a test.

Experts say we need to build around 250,000 homes a year, but we are currently managing less than half that. One in five homes is classed as 'non-decent', rising to one in three in the private rented sector. Housing is the largest single cost for many households, and poorer families face the highest costs as a proportion of their income.[2] More than a quarter of a million households now face homelessness each year, and the figure is rising.

Meeting the challenge of this housing crisis means more is required of all who can make a contribution – commercial house-builders, housing associations, councils and institutional investors. Above all, strong leadership and smart action from government is imperative. And mixing public and private investment to build new public housing – council and housing association homes at a genuinely affordable rent – must be a central part of a new national political mission.

Almost everyone concedes there's a serious problem, across the political spectrum. Even David Cameron has admitted many young people now watch the TV show *Location, Location, Location* "not as a documentary, but as a fantasy". SHOUT, the new campaign for social housing was launched last year with backing from all political parties. And Conservative pressure group 'The Good Right' has recently advocated "a Harold Macmillan-sized, state-supported housebuilding programme".

But the government's policies are falling far short. Having promised that 'we will become a nation of homebuilders' before 2010, just 125,000 homes were completed in 2014/15. Incredibly, during the last Parliament the number of new homes built dipped to levels last seen in peacetime in the 1920s, almost a century ago.

Current government policies are also intensifying rather than relieving the housing crisis. Government capital investment in social rented housing was cut by two-thirds in 2010 and by shifting the remaining subsidy to build only at so-called 'affordable rents' – a

2 http://www.ons.gov.uk/ons/publications/re-reference-tables.html?edition=tcm%3A77-370146

perversion of traditional social housing at up to 80 per cent of market rents – the provision of truly affordable social rented homes has been choked off. The effects of this shift are profound, and discussed further in section three below.

The prospects for social housing in this Parliament look worse still with further cuts in investment, and unprecedented sales of existing homes mooted. Turning the tide starts with putting the overwhelming case for social housing to politicians and the public. Here's the five reasons why I think everyone should back more social homes.

1. To build enough homes

There's now a broad-based consensus that we must build substantially more homes. There is a wide agreement amongst housing experts that we need to build 250,000 extra homes a year in England, but under the Coalition average build-rates were only 114,000 a year. Under 13 years of Labour government until 2010, the average was 143,000 – higher, but still far too few.

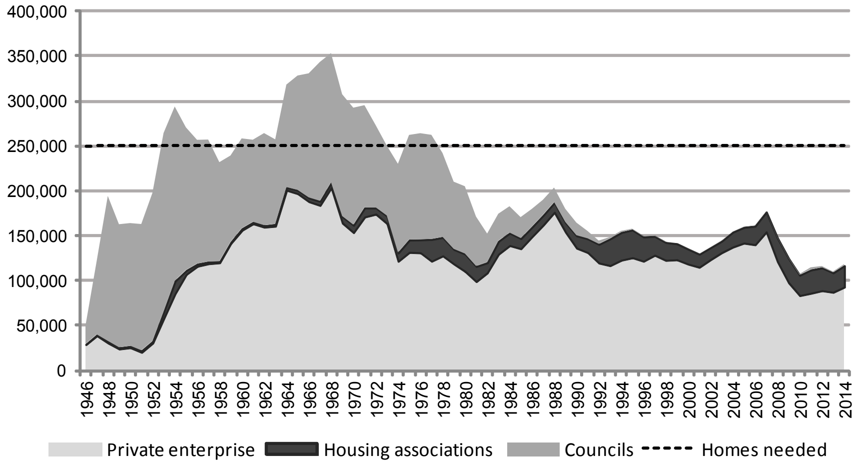
Absent from this housing debate is an honest admission that we have no chance of coming anywhere close to building 250,000 homes a year through the private market alone. Nor is this a route to reach the more modest annual target of 200,000 new homes by 2020. There has only been one year since the end of high-volume council house-building when we have managed to build 200,000 homes in England, and that was at the height of the unsustainable 'Lawson boom' in the late 1980s. Even then, councils were still building 15-20,000 homes a year.

Social housing used to make up a large part of the new overall housing supply each year. After big reductions in the 1980s, the figures flat-lined for two decades until a brief revival began, boosted after the global financial crisis by the extra investment as part of Labour's economic stimulus and the reform of council housing finance begun by Labour in 2009/10 and completed by the coalition. If we are to build the houses our country needs, the government must ensure many more council and housing association homes are built.

2. To make homes affordable

The cost of the housing crisis blights the lives of at least three groups of people. First, it is estimated that there are 1.3 million households in low- to middle-income groups who spend more than 35 per cent of their income on housing – an internationally recognised threshold of affordability. Second, there are those who cannot buy or rent at all. There are over 4.6 million 'concealed' households: single people or couples living with others, such as parents, relatives or friends. There are 1.4 million *fewer* young households buying their own homes compared with ten years ago. Third, there is rising homelessness. In 2014/15, some 275,000 households were assisted as homeless, 38 per cent more than in 2009/10.

Figure 1: Housing completions in England



Source: DCLG Live Table 244

So several million households are hit by the lack of affordable housing, paying excessive costs, denied a home of their own or actually homeless.

More social homes would help all of these people. But policy changes made by coalition ministers now mean that what used to be affordable housing, is often no longer genuinely affordable.

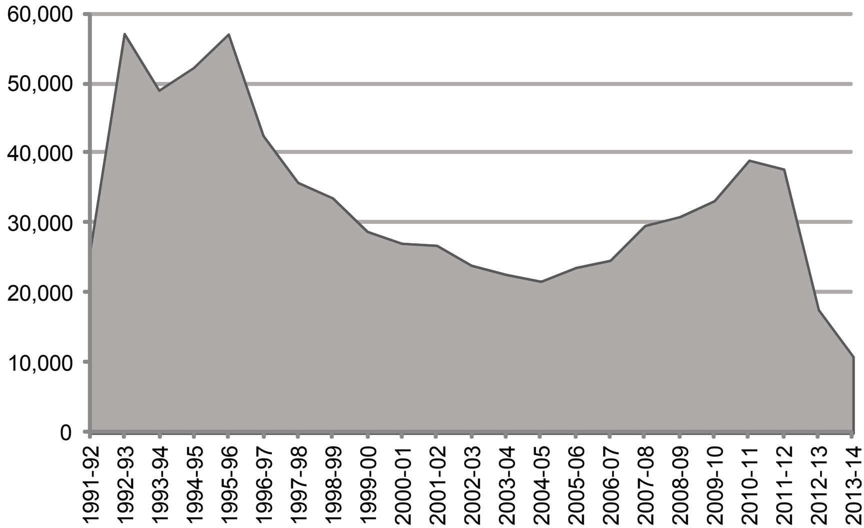
Up until 2011/12, the majority of affordable housing was built to let at 'social' rents linked to local incomes as well as building costs, which averaged around 50 per cent of market rents. But current government policy has aggressively reduced the level of public subsidy in such homes and replaced this with increased 'affordable' rents to as high as 80 per cent of open market prices. Starts on site to build new social rented homes have fallen by two-thirds – from 39,000 to 11,000 - since 2010 and on current plans will soon be close to zero.

To further fill the subsidy gaps, the government have also forced 'conversion' of existing homes at social rent levels to the new affordable rents, and increased right to buy discounts without replacing those social homes lost through sales. As a result, we've lost 63,000 more social rented homes than we've built in just two years.[3]

3 Analysis by John Perry for the 2015 UK Housing Review. Estimate based on local authority and HCA statistical returns.

The impact on affordability is severe. In some parts of the country, hiking social rents to 80 per cent of market prices can mean that they are double average take-home pay, putting them completely out of reach for families on low incomes. In the London Borough of Camden for example, raising rents to 80 per cent of the market necessitates an after-tax household income of around £50,000 to remain affordable.

Figure 2: Social rent completions



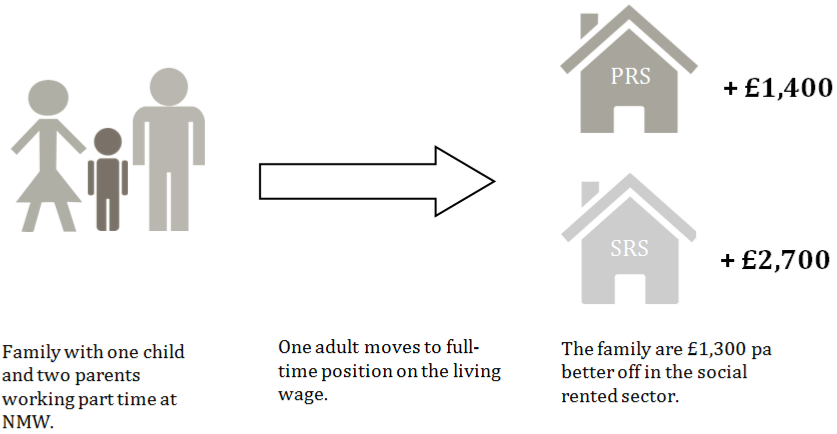
Source: DCLG live table 1000

3. To increase work incentives

Housing costs are a critical factor in making work pay. The steep taper on housing benefit withdrawal is a disincentive to earn more, and higher rents mean that disincentive lasts for longer. This problem is built into and will continue under universal credit. Lower, social rents can make it more worthwhile for people to work by increasing their take home pay.

For example, take a family with one child and two parents who are both working part time at the national minimum wage when one of the parents is offered the chance to work full time. If they are living in private rented accommodation paying an average private rent, their net income will increase by £1,400 per year as a result of the extra hours. But if they are living in social housing, paying an average social rent they will take home an increase of £2,700.

Figure 3: Varying costs to a working household of private and social rented housing



Source: author's calculations

The affordable rent model is working in the same way - dragging many more council and housing association tenants into reliance on benefits, and making it less worth their while to move off: the very opposite of stated government aims.[4]

4. To boost jobs and the economy

The economy is still operating below capacity, and building homes provides a direct boost. Every £1 spent on house building generates £2.84 in total economic activity and, according to government estimates, supports 12 year-long jobs for every £1m of building investment.[5] If we built 100,000 homes a year, it has been estimated that we could create 90,000 jobs.

When the financial crisis and downturn struck, and the private sector was unwilling or unable to build, the Labour government switched spending to housing as a stimulus. That direct stimulus is less needed now, but a big programme of social housing now would still have a direct positive economic impact as well as helping provide jobs and apprenticeships.

What's more building enough homes is necessary to help even out the cycle of boom and bust – we know that wider economics swings are often driven or exacerbated by a volatile

4 See also Affinity Sutton (2015) *Affordability: a Step Forward*
5 L.E.K. Consultants (2012) *Construction in the UK: The benefits of investment*. London: UK Contractors Group (see www.ukcg.org.uk)

housing market. Ensuring more consistent and substantial investment will help moderate these swings to the benefit of the wider economy too.

5. To secure value-for-money from public spending
Finally, public spending on social homes pays for itself.

Despite the deepest cuts to housing benefit *ever* in the last parliament, spending on housing benefit has risen by £2.3bn or 10% in real terms, and is set to continue to rise significantly over the long-term according to Office for Budget Responsibility forecasts. Cutting back on investment in social housing and raising rents is a false economy for the taxpayer: savings made in one department only push up costs in another.

So, by contrast, an ambitious public housing programme would save the exchequer money over the long term. As I show in the following chapters, working up to building 100,000 new social rented homes a year by the end of this parliament would not only pay for itself in less than 30 years but provide a *net* benefit to the public purse of almost £6bn through lower housing benefit costs. Continuing to build at this scale beyond the present 5-year parliament would multiply these savings.

But before coming to what could be done differently, we must first diagnose the problem.

Section 2

Housing benefit and affordable homes

Housing benefit and affordable homes

A big part of the case for public investment in new homes turns on the saving to the Exchequer through lower housing benefit spending. High housing benefit spending is housing's 'canary in the mine' – signalling that for far too many families, their incomes simply don't cover their high housing costs.

It is also by far the most significant way in which government helps families with high housing costs. More than one in six households claim housing benefit.[6]

This wasn't always the case. The almost £25bn we spend every year on housing benefit now is eight times higher in real terms than 35 years ago.[7] It's an increase in public spending not matched by any other social security benefit.

To be clear what that means - if unemployment benefits had grown at the same rate per claimant as housing benefit the average award wouldn't be around £65 per week as it is now, but £275 per week.

Over this same period in which housing benefit costs have soared, the number of new council and housing association homes being built in England has fallen dramatically, by 67% since 1978/79 to only 28,400 completions last year.[8]

This is one of the great social policy shifts of the last century – a conscious decision to let the cost of renting rip and to try to balance household books by relying on spiralling housing benefit spending.

Today, the mismatch in public housing support means that in this Parliament the present government has committed £3.3bn of public money from 2015 to 2018 under the latest round of the Affordable Homes Programme, and in the Autumn Statement it pledged a further £1.9bn for the two remaining years of the Parliament. But if we compare this with government forecasts for housing benefit then this means that 96%, or around £120bn, of the central government expenditure on housing in this Parliament will be on housing benefit with only 4%, or around £5bn, spent directly on building new homes.

Even if we take into account local authority capital spending on housing as well, over which central government no longer has direct control, alongside general capital spending

6 Labour Force Survey household estimates (used as a proxy for benefit units) and DWP administrative data
7 DWP administrative data, consistent with the March 2015 Budget
8 CLG live table 213

on maintenance and upkeep of social homes too, gross public investment is still below £5bn per year, down from around £14bn at the end of the 1970s in today's prices.[9] It's the polar opposite of the trend in housing benefit spend.

Figure 4: Public expenditure on housing benefit and investment in social housing

Source: UK Housing Review, DWP administrative data

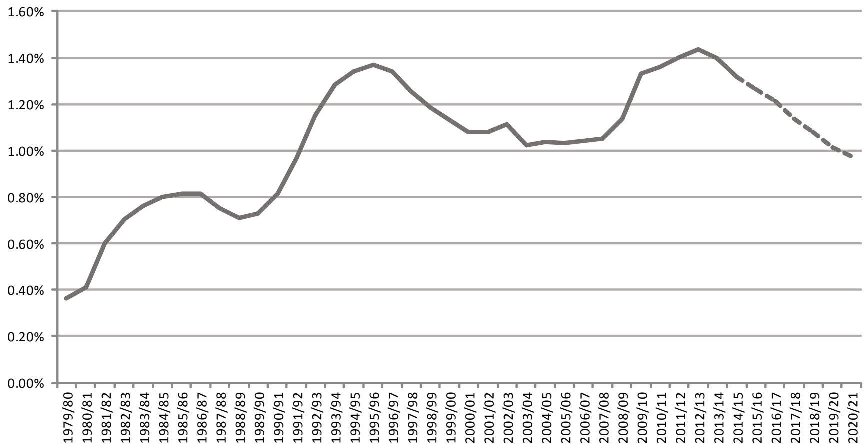
For some commentators the only answer to this trend is to declare that housing benefit spending is 'unaffordable'. So is it? The best measure of what a country can afford is to express spending as a proportion of the country's national income, or GDP.

While there was a steep rise in housing benefit spending in the 1980s and early 90s, the facts show that since then expenditure as a proportion of national income has broadly risen and fallen with the economic cycle – rising in the downturns after 1992 and 2008, but falling in the intervening period. Departmental projections are for falling expenditure over

9 See figure 4 for sources. In-keeping with the responsibilities of the Westminster government, the housing investment figures are for England-only, the housing benefit figures are for Great Britain.

the next few years, and the central OBR forecast is that spending will be flat as a proportion of GDP over the longer term.

Figure 5: Housing benefit spending as a percentage of GDP



Source: DWP administrative data and ONS/OBR

But even this response misses the bigger point: simply cutting housing benefit is just blaming the canary rather than making good the mine.

The charge against housing benefit spending is less that it's unaffordable and more that it's inefficient.

There's a much more cost-effective way of using the public money we currently spend on housing benefit to deal with the root causes of high spend, not just addressing the symptoms.

A brief history of when, and why, housing benefit has risen shows this to be the case.

Housing benefit hasn't risen at a uniform rate. Setting out the record of political administrations of the last 35 years on housing benefit shows this to be the case, and runs contrary to much perceived wisdom.

As figure 5 shows, it was the Thatcher and Major governments who added the most to the housing benefit bill - over £13bn in real terms and an extra 1.3m claimants. The Blair/Brown governments compare much more favourably, even given the impact of the recession and subsequent downturn after 2008. The number of claimants fell over the 13 years of Labour government by almost 200,000, and by more than 700,000 before the crash.

Given varying lengths of time in office, it is instructive to compare the annual change in housing benefit spending. The findings here re-enforce this message. Huge rises in the 80s and early 90s equate to an astonishing average real year-on-year increase of 9% during the Thatcher/Major period. By contrast, the Blair/Brown years saw an average increase of only 2% despite the crash.

Bringing the analysis up to date, the housing benefit bill has risen faster under Cameron than under the last Labour government, on the most recent official data.

Table 1: Housing benefit caseload and expenditure under different administrations

	Caseload change by administration	Change in real HB spending (%)	Average annual real change (%)
Thatcher	+ 542,000	+ £5.7bn (172%)	+ £475m (9%)
Major	+ 790,000	+ £7.7bn (85%)	+ £1,275m (11%)
Thatcher/Major	+ 1,332,000	+ £13.3bn (445%)	+ £741m (9%)
Blair	- 719,000	+ £0.9bn (5%)	+ £90m (1%)
Brown	+ 526,000	+ £4.3bn (24%)	+ £1,430m (8%)
Blair/Brown	- 193,000	+ £5.2bn (31%)	+ £399m (2%)
Blair/Brown before crash	- 704,000	+ £1.4bn (9%)	+ £129m (1%)
Cameron (part forecast)	+ 482,000	+ £2.3bn (10%)	+ £454m (2%)
Cameron (actual, to 13/14)	+ 479,000	+ £2.5bn (11%)	+ £928m (3%)

Source: DWP administrative data, 2015/16 prices. Figures are rounded.

To better understand why these changes have occurred we need to first understand who the claimants are.

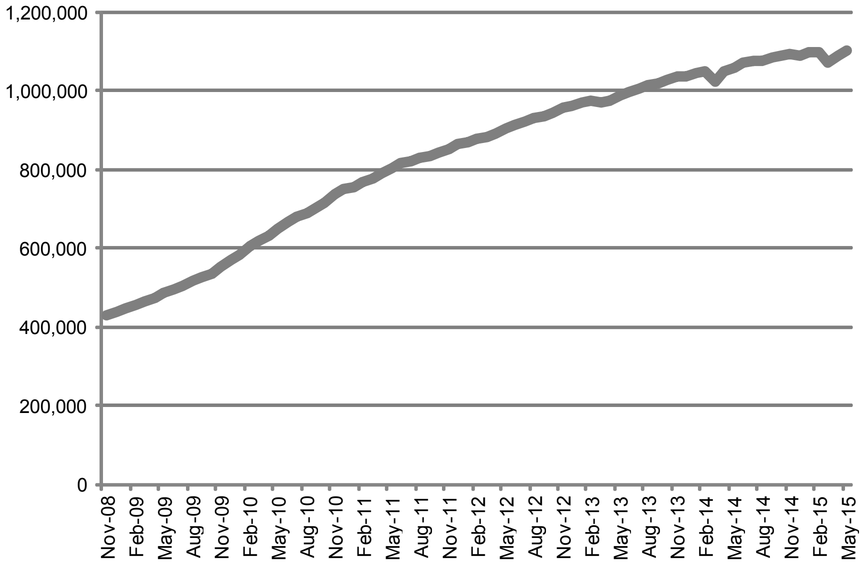
Most housing benefit claimants (61%) are recipients of other low-income benefits and as a result 'passported' on to housing benefit. The largest passported groups are pensioner households receiving the guarantee credit element of pension credit (19% of all claimants) and households receiving disability benefits (23%). Less than one in 10 (8%)

claimant households are receiving jobseeker's allowance – the main out of work benefit.

One of the most striking recent changes has been the growing number of people who claim housing benefit despite being in work.

The number of working families claiming housing benefit more than doubled between 2009/10 and 2014/15 and now stands at over 1.1 million – the highest number since comparable records began.[10]

Figure 6: Working households claiming housing benefit



Source: DWP administrative data, via Stat-Xplore

Most in-work claimants rent privately, but overall it still remains the case that a greater number and proportion of housing benefit claimants live in the social rented sector – inevitable given that increasingly public rented homes are only available to those on the very lowest incomes. In total some 3.3m families claim housing benefit in council and housing association homes, compared to 1.6m in the private rented sector.

10 Even these statistics are likely to underestimate the number of in-work recipients given that benefits such as income support and JSA allow recipients to work a small number of hours and retain eligibility.

Across the country, big differences in local labour and housing markets means there is a significant divergence between housing benefit spending. The average housing benefit award in London is a third higher than even the South East and almost double the average award in the North East. Around £6bn, or more than £1 in every four, of total housing benefit expenditure is in London.

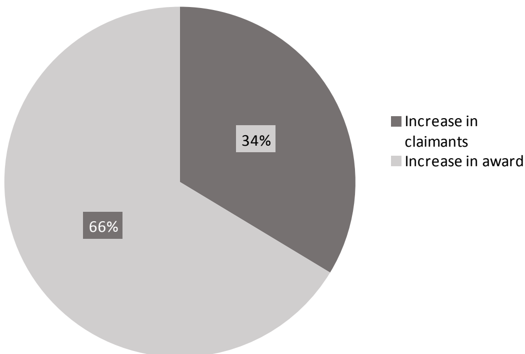
This divergence largely reflects the big geographical differences in social and private rent levels, which is also mirrored in the stark contrast in house prices between London and the rest of England.[11]

So why has housing benefit expenditure grown so significantly over the last thirty-five years?

By disaggregating the Department for Work and Pensions' administrative data we can assess the contribution of the two proximate causes of increasing expenditure - higher award per claimant and higher caseload of people claiming.

The chart below shows that since the late 1970s, around two-thirds of the increase in expenditure has been due to the higher amount claimed, with around one-third due to a higher number of families claiming housing benefit.[12]

Chart 1: Why did housing benefit spending rise? 1979/80–2014/15

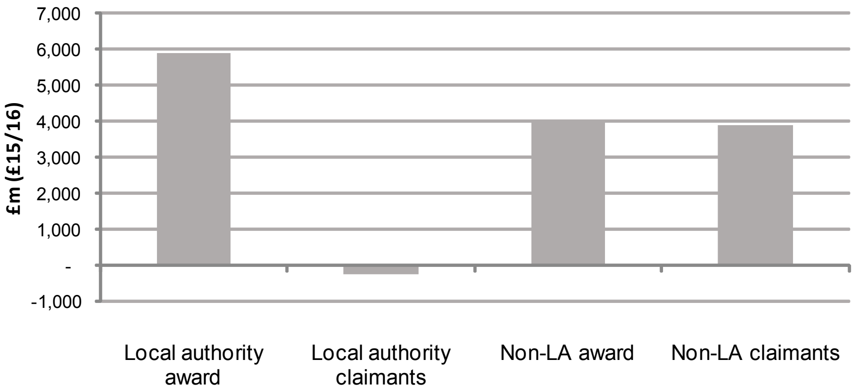


Source: DWP administrative data; House of Commons Library and author's calculations

11 See Smith Institute's report 'The great house price divide' (2013)
12 This calculation, which was undertaken by the House of Commons Library, uses annual housing benefit award and caseload administrative data to assess the relative contribution of each to overall spending. A small residual where a change in spending is the result of a combination of caseload and award has been added to the award category.

To dig deeper into what has happened over time, it is worth breaking this down again by political administration, and by private and social sector. Due to data limitations, before 1995, housing association tenants are grouped together with private rented tenants.

Figure 7: Housing benefit claimants and award under Thatcher/Major (1979/80–1996/97)



Source: DWP administrative data and author's calculations

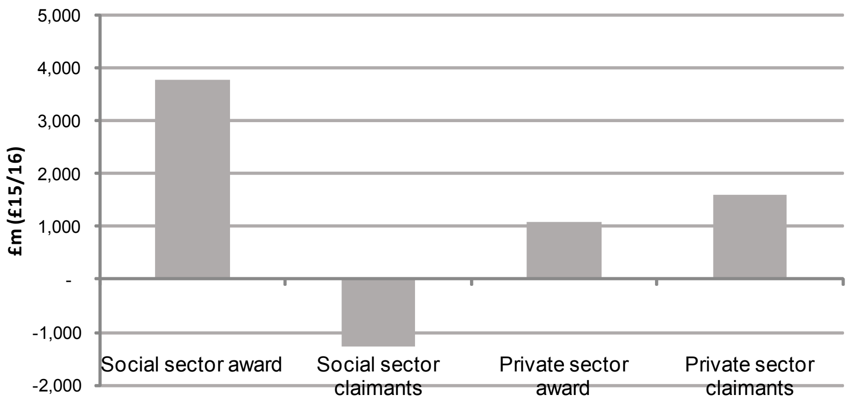
We know that expenditure increased dramatically over the period of the Thatcher/Major governments. In the early 1980s this was largely as a result of a sharp recession increasing the number of claimants.

But the steepest sustained increase in expenditure occurred from the late 80s to the mid 1990s, with a 'perfect storm' of social rent hikes, private sector rent deregulation followed by the recession of the early 1990s. This meant almost a million additional people claiming housing benefit, at a much higher award level. And compared to previous recessions there was much less capacity in the social rented sector to absorb increased demand.

As suggested by the 'local authority award' column perhaps the biggest net contributor to higher housing benefit spending was higher public rents. Average social rents almost tripled during the period 1980-90. And under John Major, the government pursued a policy of social rent increases well above inflation, averaging over 4% in real terms until 1996.[13]

13 Malpass and Murie (1999) *Housing Policy and Practice*, p. 177

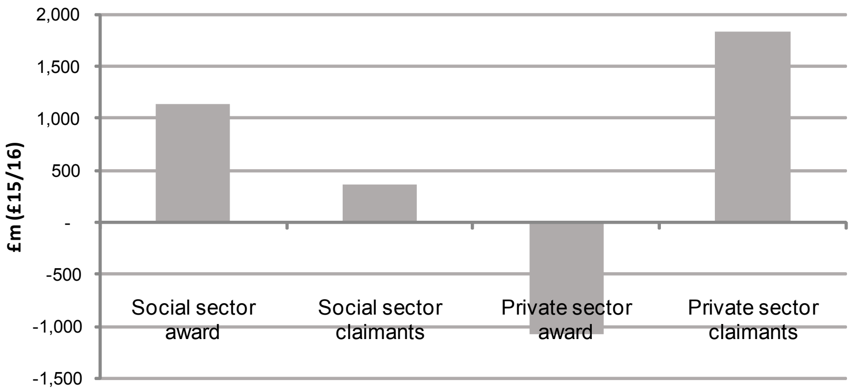
Figure 8: Housing benefit claimants and award under Blair/Brown (1996/97–2009/10)



Source: DWP administrative data and author's calculations

Falling unemployment and rising living standards in the late 1990s and early 2000s meant a significant fall in the number of people claiming housing benefit in that period, and a reduction in overall spending. However, housing benefit began rising once more by the middle of the 2000s, again mainly due to high rent inflation not just in the social sector but the private rented sector too. Spending increased sharply after the 2008 crash as a result of higher unemployment.

Figure 9: Housing benefit claimants and award under Cameron (2009/10–14/15)



Source: DWP administrative data and author's calculations

The sharp increase in caseload as a result of the global recession and downturn continued after 2010, with the private rented sector absorbing the majority of new claimants. Since then, big cuts to housing benefit, and the rise of in-work families claiming only partial housing benefit to top up their wages has depressed the average private sector award. However, this has been more than outweighed by rising social sector rents, and the rising number of people on low incomes living in the private rented sector.

There are a number of important lessons that emerge from this analysis. First, it's clear that rising housing benefit has gone hand-in-hand with the retreat of a public role in building new social homes. The huge and unprecedented rise in housing benefit spending during the 1980s as public investment in homes was being cut back and right to buy introduced is particularly stark.

Second, many of those who claim housing benefit are on disability benefits, or are pensioner households. For many of these households, their income is effectively fixed, and the prospects of them earning more in wages will be remote. So just controlling housing benefit by cutting their entitlements is simply punitive.

Third, the problem of high housing costs not met by household income is increasingly a problem for working as well as out of work households. Any solution to the high cost of housing benefit must cater for these households too.

Fourth, it is unsurprising to see that spending on housing benefit is weighted towards those areas where housing costs and housing need is the most acute, particularly London. It is here that most urgent attention is needed.

Fifth, the effect of lower public investment leading to higher numbers of claimants in the private rented sector is only one part of the story. The other is that a big driver of housing benefit spend in the recent past has been lower investment leading to higher rents, and so higher housing benefit awards in the social sector.

This, then is the problem. The next section looks to see how it could be solved.

Section 3

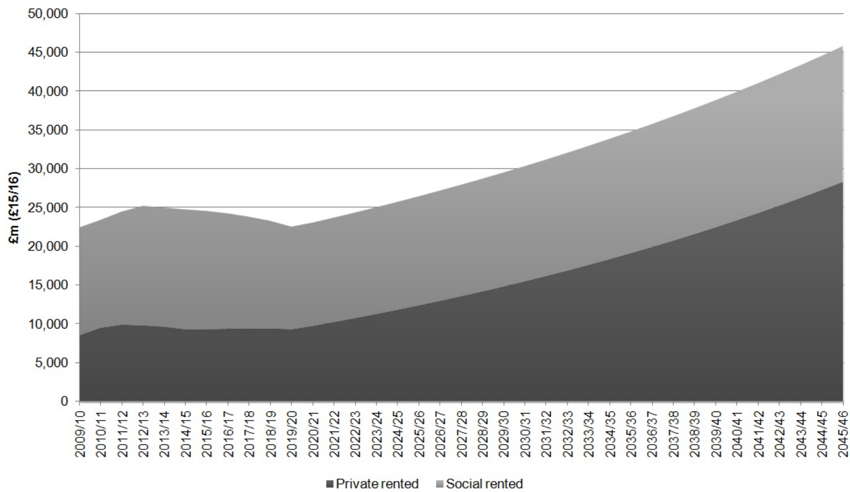
Invest to save: how could we build 100,000 affordable public homes?

Invest to save: how could we build 100,000 affordable public homes?

Not only has housing benefit spending risen dramatically over the last 35 years, it is also set to go on rising. Using OBR long-term forecasts and assumptions about award and caseload change over time, we project that on current trends total annual spending on housing benefit of around £45bn in thirty years' time in today's prices. The majority of this will be spent on tenants in the private rented sector. This is almost double the spending forecast for the end of this Parliament.

Reducing the spiralling cost of supporting people in private rented homes by providing affordable public housing offers a better way forward. The long term savings could be substantial, with those on low pay better off too. And because social landlords recycle their surpluses, rather than take them as profit, the public money we spend goes further.

Figure 10: Long-term housing benefit projection



Source: OBR fiscal sustainability report and author's calculations (see appendix for further details)

To his credit, Labour's previous leader Ed Miliband was acutely aware of the long-term problem of a rising housing benefit bill. In a speech in June 2013, he rightly said: "Today the welfare state, through housing benefit, bears the cost for our failure to build enough homes. We can't afford to pay billions on ever-rising rents, when we should be building homes to bring down the bill. It's time to tackle this problem at source".

In 2014, Ed commissioned me to do some private work on how we could use the power government has over housing and labour market policy to bring down the housing benefit bill, and build more homes at the same time.

Working with PricewaterhouseCoopers, I developed a detailed long-run financial model of housing benefit to enable us to assess the impact of various policy options including boosting the supply of public homes. The results below are drawn from elements of that project.

The 2010-15 Parliament

Before moving on to look at what a committed government could do in this Parliament, it is important to first look at some of the very big retrograde changes made in the last Parliament, which must not be left unchallenged.

Two big changes stand out.

First, while the main cut to housing benefit for social sector tenants – the 'bedroom tax' – received the most press and political attention in the last Parliament it was the cuts to housing benefit in the private sector that could have the most significant long-term impact.

Of the eleven separate cuts to housing benefit made in the last Parliament, the majority only affected the private rented sector. And of these cuts, there is one technical change in particular what has very serious long-term consequences - the move to uprate housing benefit for private sector tenants by the Consumer Price Index (CPI) measure of inflation, rather than by local rents.

This decision to change how housing benefit for private tenants is calculated has lead to the perverse situation where a social security benefit that is meant to help with a families' housing costs no longer tracks changes in the very costs it is meant to be meeting.

Research by Shelter suggests that the short-term impact will be severe – with less than 10% of properties available to tenants in high-demand areas like London and Manchester, and less than 30% in most of the rest of the country by 2017.[14] Our modelling suggests that if left unchecked, the long-term effect will be extremely severe, with rapidly growing

14 See Shelter (2015), 'What can 1.4m renters expect from the next round of welfare reforms?' http://blog.shelter.org.uk/2015/05/what-can-1-4-million-private-renters-expect-in-the-next-round-of-welfare-reforms/

swathes of 'no go' areas for families on low incomes – unable to buy, unable to access a depleted stock of social housing, and unable to make ends meet in the private rented sector either.

The second big decision in the last Parliament that stands out is the significant cuts in social housing investment, including the resulting shift to so-called 'affordable' social sector rents at up to 80% of the market rate. It is evident that this will have a serious inflationary effect on future housing benefit spending.

This was a big change from the situation the Coalition government inherited. In the three years from 2008, the Labour government committed some £2.8bn a year in capital investment as part of the National Affordable Housing Programme. But this was cut to just over £1bn a year in the Chancellor's first budget.

By constructing a counterfactual scenario where this investment had been maintained we can estimate the housing benefit effect of the reduction of this funding stream. We model that the loss of new affordable public homes over the four year funding period from 2011-15 is equivalent to an Exchequer cost of some £7.7bn over 30 years in additional housing benefit payments.[15] Even after the additional upfront capital costs the public purse loses out by nearly £1bn in real terms compared to a scenario where this investment had been retained and used to build new homes. And, all this as the result of a measure designed only to cut costs – a truly false economy.

Combined with this move to cut back central grant investment was the government's decision to row back on the more favourable devolution settlement for council housing revenue accounts that I had agreed with the Treasury as housing minister. This roughly halved the number of new homes councils were projected to build over the 2010-15 Parliament. Plugging this into our housing benefit model, we estimate a higher housing benefit bill of about £0.9bn over 30 years as a result.

But perhaps most damaging to future housing benefit inflation of the individual changes that ministers have made to social housing is the shift away from social rents calculated by reference predominantly to local incomes, to one set by reference to the private market.

These so-called 'affordable rents' are not affordable now, and over time will become significantly even less so. We model that over thirty years, the affordable rent units built in just this Parliament will add some £8bn to the housing benefit bill compared to the

15 For comparability, all figures expressed after inflation in 2015/16 prices.

counterfactual in which the homes built and converted since the inception of the affordable homes programme had been built or retained at traditional social rents.

Importantly for the on-going discussion about the viability of the near-market affordable rent type of social housing, we model that a social rent unit built this year will pay back the extra up-front capital expenditure needed compared to an affordable rent home within 20 years, in housing benefit savings alone, and is clearly better value for money in the long run. This is concurrent with the Department for Communities and Local Government's conclusion in its own impact assessment that the affordable rent model would end up costing more in housing benefit in the long run, even when the lower up-front capital investment required was taken into account.[16]

Alongside these big steps backwards in policy, the tale of the last five years is partly an organisational and administrative failure – a failure to join the dots across government. Any government that has one department – DWP - pledging to cut down on benefit spending, while another – DCLG – makes policy changes which increases it (like the shift to near-market social rents which actively and deliberately inflates the benefits bill) is not functioning properly.

I know from my experience in government that achieving effective joint-working between departments can be tough. In my year as housing minister, I didn't have a single bilateral meeting with any Work and Pensions minister despite the close interplay between housing and housing benefit. That has to change.

Administrative changes such as shared departmental priorities, a new Cabinet sub-committee or appointing a Minister to sit jointly in the CLG and DWP teams to take responsibility for this area all have merit, but the best guarantor of joint-working is an explicit and substantial commitment to a new financial relationship between the Departments.

One option would be to create a reciprocal relationship between DCLG and DWP formed of two strands. First, for DCLG to commit to changing the remit of the Homes and Communities Agency so that in addition to delivering the number of affordable units required, it also takes into account the impact on housing benefit when allocating social housing grant. In practice, this may mean a bias towards lower rents, and to those regions of the country (principally, our modelling suggests, London, the South East and East of England) where the potential housing benefit saving is the greatest, even given the higher grant costs. There would be some issues of design to overcome to assess that relative saving, and to cope with

16 DCLG (2011) *Impact Assessment for Affordable Rent* https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/6021/1918816.pdf

the lag between Homes and Communities Agency approval and the unit being occupied, but these seem soluble.

The second strand would be a commitment from the Treasury that housing benefit savings resulting from any major labour market interventions would be transferred directly to the Homes and Communities Agency to finance additional affordable house-building. This could prove to be a significant - our modelling suggests that a back-to-work programme like the 'jobs guarantee' suggested by Labour before the last election would yield a housing benefit saving in the region of £1.2bn over this Parliament.

A more comprehensive extension to this proposal would be to recycle the housing benefit savings from affordable housing investment as well – returning the housing benefit savings from investment to DCLG as additional spend for new affordable homes, at least for a limited period. But whichever route is chosen, the most important thing is that the way decisions about housing and housing benefit are made within government is changed.

Could we build 100,000 social rented homes between 2015 and 2020?

Whatever the history of the last five years, the urgent task now is to set out what an alternative on public housing looks like for the five years of the Parliament ahead.

One option, which I detail here, would be to build 100,000 homes for social rent by the end of this Parliament. It can be done. And what's more it can be done with a public spending commitment of around the same magnitude as when I was housing minister 2009/10.

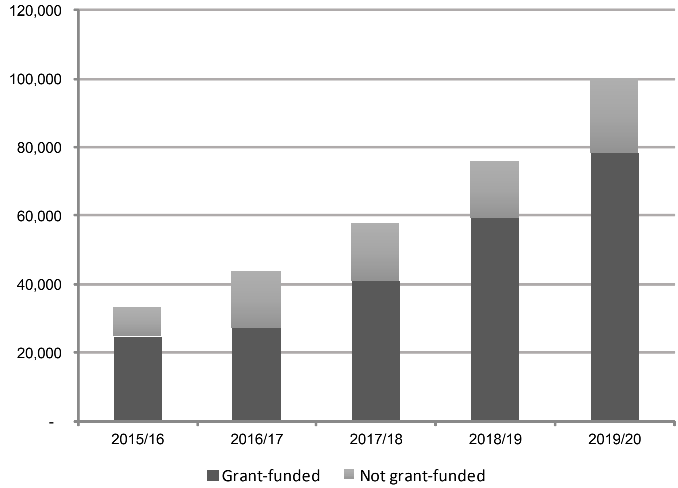
Significantly, because this up-front spending would be a genuine investment on the part of the Exchequer, it can be done in way that pays for itself, purely through lower housing benefit payments, over 26 years – well within the time-frame for a return that many businesses, and public sector bodies plan for.

There are a number of ways that a programme to build the public homes we need could be delivered. For illustrative purposes, we model one potential set of changes that a government minded to revive affordable public housing could take. These changes would:

- Give councils the freedom to borrow against their assets, just as businesses are able to do
- Tighten the obligations of commercial developers to fund more new social homes through the planning system, reconfiguring the 'viability review' policy
- Reform right-to-buy to actually deliver one-for-one replacements

- Use the power of the government balance sheet to bring down the cost of finance for housing associations by extending the guarantee scheme
- Fund a significant HCA grant programme to allow councils and housing associations to build at scale, and lever in private finance

Figure 11: Illustrative build forecast



N.B.: Numbers on left hand side refer to units
Source: author's calculations based on the illustrative interventions mentioned above

Together these policies could bring about a step-change in the number of public homes we build, and are all almost all tried, tested and ready to go.

Give councils the freedom to borrow against their assets.
Currently councils are restrcuted in their ability to borrow and build up to established prudential limits. This change would allow councils to be run like the uniquely accountable, enterprising public institutions that council leaders of all political colours want to be. When we helped councils get building again after the global economic crisis we found councils were able to gear up quickly. We model 60,000 additional homes over five years as a result of this policy change, half of which would require grant funding.

Tighten the obligations of developers to fund more social rented homes
In the last Parliament, the planning system was blamed for the lack of new homes, and the government made it easier for developers to get away with building fewer affordable

homes by introducing a test of project viability. No substantial adjustments to this test were introduced as the market recovered. The granting of planning permission can be hugely profitable for developers, and it's essential that some of this added value is retained for the wider public benefit. It's also a vital way of putting private finance to work in building public homes. Rather than running down the number of homes provided as is set to happen in this Parliament, increasing the number of homes delivered through developer obligations to their pre-2010 peak would enable 16,000 new homes a year. We model that 20% of these are delivered grant free.

Reform right-to-buy to actually deliver one-for-one replacements
Right-to-buy has been a boon for some council tenants, but has had a huge negative impact on the stock of public homes and proved a big disincentive for social landlords to develop. Instead of the nine-to-one replacement ratio achieved so far, we model a policy of a genuine one-to-one replacement. This would reduce the number of homes sold, and bring in 6,000 additional replacement homes per year compared to the status quo.

Use the power of the government balance sheet to bring down the cost of finance for housing associations
One of the good innovations that has become established in this country, though used for some time abroad, is the use of government guarantees to help bring down the cost of finance for private and charitable organisations. We model a modest extension of the current guarantee programme to build an additional 2,000 homes per year. We also model the capitalisation of a housing investment bank which enables around 5,000 additional units in the final year of the Parliament only.

Fund a significant HCA grant programme to allow councils and housing associations to build at scale, and lever in private finance
In addition to the grant funding for the programmes above, we model a significant additional contestable amount of grant funding to be disbursed to councils and housing associations through the Homes and Communities Agency and the Greater London Authority. We model the grant per home needed as £60,000 per unit, the same level as under the National Affordable Housing Programme from 2008-11. This enables an average of 30,000 additional units per year, weighted towards the final years of the Parliament to enable the sector to gear up for this level of building.

Implementing this set of housing policy changes would result in the following capital costs and savings to housing benefit.

Table 2: Capital costs and savings to housing benefit

Direct housing benefit saving (2015-20 Parliament)	£0.3bn
Direct housing benefit saving (30 years from 2015/16)	£19.6bn
Total cost/saving (2015-20 Parliament)	-£13.5bn
Total cost/saving (30 years from 2015/16)	£5.8bn
Payback period for 2015-20 investment	26 years

Source: author's calculations

This is then, a ready-to-go set of housing policies which could feasibly see the building of 100,000 affordable public homes. It could not only pay for itself but deliver a public saving of almost £6bn over a 30 year period. And this is only considering an alternative for the current Parliament alone. If this sort of build programme was sustained the savings would be multiplied.

What's more, this sort of public investment can be a lever for private investment – multiplying its effect. The record of this government has shown the relationship in reverse: alongside the cut in public housing investment over the last four years, there was £1.4bn *less* private housing investment in housing association homes last year than in 2010/11.[17]

If they are to built to a good standard then these homes will be here for decades to come. Much of the Garden Cities, early public housing blocks built by the Greater London Council and the government's early New Towns are still here and with adequate maintenance will be housing people for many years to come. So the rental income above the costs of repair on those public homes can continue to be reinvested.

This illustrative policy programme is of course not the only set of options available.

As well as recognising the need to depend upon ways of directing new building that have been or are currently used by the government, we should also look to learn from other countries where affordable homes are funded in different ways, and which may be applicable here. Like France where the introduction of popular tax-free savings accounts now provides the source for a good deal of the country's social housing finance, or Denmark, where there is a national mechanism for pooling and recycling housing association surpluses.[18]

17 *UK Housing Review 2015*
18 Good recent work on new ways of funding new affordable homes can be found in JRF (2013) *Innovative Financing of Affordable Housing*; CCHPR (2012) *Funding Future Homes*; and Capital Economics (2014) *Increasing Investment in Affordable Housing*

And some of the best ideas for action I hear come from practitioners themselves - council and housing association staff who are at the coalface building new homes and providing services for tenants. It is to them too that campaigners and politicians must now look, as we seek to show how public homes can be built at scale once again.

We must also not lose sight of the vital changes that need to be made in other parts of the housing sector. A growing number of private rented homes could be a positive development, but it doesn't feel like that for many of those who rent at the moment. Parts of the private rented sector are too insecure, in too poor a condition, and too expensive. The number of private renters with children has almost trebled in the last decade to 1.5m households, and we know renting privately can be particularly tough for them.

Home-ownership levels meanwhile are the lowest in a generation because younger people are just getting priced out. Home ownership shouldn't be a luxury, but it's fast becoming so in some of our major towns and cities.[19] So there's a big task for government to help bring down the cost of owning a home too.

19 See Smith Institute report *The end of the affair: the consequences of declining home ownership* (2011)

Conclusion

Conclusion

Any government that wanted to consider building on this scale would face big challenges. Some of the necessary arguments and ammunition have been set out above. But by way of conclusion I want to outline three further challenges which must also be met: cost, public support, and delivery.

1. Cost

The extent to which further austerity measures are needed to reduce government borrowing (predicted to be 3.7% GDP in 2015/16) is subject to political debate. Politics is always about choices and proper fiscal targets can be set and met in different ways. But when framing an alternative to the course that this government has set upon for public housing, we need to consider first the upfront cost of a social house building programme.

As set out above, there are a range of policy changes which will increase the number of social homes built at little or no cost to the public purse. Restoring the private contribution towards public homes by tightening up on developers' obligations to include social housing in their projects could yield big rewards and without harming overall viability, as could ending the giveaway of tax-payer investments through big right-to-buy discounts. The Lyons Review on housing which was published last year set out a number of further ways in which we could increase the supply of new homes within existing fiscal constraints.

Even with these changes, a bigger social house-building programme would require some additional capital spending. The politically and economically crucial distinction between this and other sorts of government spending is that this is borrowing to invest. Just like when prospective home-owners take out a mortgage, a business buys a new capital good, or a student decides to go to university. And the proof of this as I have shown above is that this investment creates a long-term asset and yields a financial return to the public purse in lower housing benefit payments.

Right now it's a particularly attractive investment for the public purse to make. With yields on 10-year gilts currently below 1.5 per cent, UK government borrowing costs are just about the lowest they've ever been.

But campaigners and politicians alike have more to do to capture the language and arguments to convince a sceptical public that government must behave more like a good business and invest for the future. That challenge may become less pressing as the budget deficit decreases over this Parliament, but it will not go away.

2. Public support

There are good overall levels of public support for the idea of social housing. Polling by YouGov for the Fabian Society last year revealed that a majority of people (57 per cent) back more social housing being built, and more support than oppose social housing being built in their area (44 per cent vs 27 per cent). That's true across social class, gender, age and region. A recent Ipsos-Mori poll for the Chartered Institute of housing found a majority of people would support government borrowing for affordable homes to rent and buy, and with particularly strong support from private renters.[20]

We also know how we can increase support for social housing: good design standards, and allowing local people to stay in their area by giving them greater access to social homes built in their neighbourhood can both help.

But the wider challenge in securing strong public support remains what it has been for at least a generation - to correct the marginalisation of social housing and the perception that public housing is 'not for people like me'. Fewer social homes means only those with higher support needs can often get new social tenancies, which reinforces the perception amongst many people that council or housing association homes are not for them or their family and reduces public support for new social housing.

Part of the answer lies in building to make more homes available but its also vital that developments are mixed so communities are mixed too. This is why requiring social housing to be built alongside open market housing via 'planning gain' is so important, not just to ease pressures on the public purse but because it is essential in creating mixed-tenure developments. Local housing allocation policies also have an important role to play here in ensuring that a broader range of families can access social homes.

We should also explore how we can make a new wave of public homes relevant for a generation who were born long after the heyday of mass council house building finished. Could a set proportion of new public homes be allocated to young people just starting out on a time-limited tenancy or to families with children of school age? These are the questions that those determined to assemble strong support behind a new public house-building programme will have to be serious about answering.

3. Delivery

Building public homes on the scale required is a huge delivery challenge, for central government, local authorities, housing associations and the private sector.

20 https://www.ipsos-mori.com/researchpublications/researcharchive/3558/Majority-of-public-back-borrowtobuild.aspx

To kick-start construction, the government should strike a national 'new deal for housing' – a national target for new social homes and a commitment from all the players in the housing field that they will do their bit. Government needs to provide funding and land, developers must build and be mindful of the social obligation they have to cater for all who need a home and not just a few, and local authorities and housing associations must focus on increasing the number of homes built while staying true to their social mission of providing genuinely affordable accommodation.

None of these challenges are insurmountable. But each must be taken seriously and with urgency at a time when public housing is under serious attack. For those who value it, the arguments are there, and now more than ever must be brought to bear.

Appendix – notes on sources and methodology

Appendix - notes on sources and methodology

As part of a wider project on housing and housing benefit (of which the results presented in this report are one part) we received advice from PricewaterhouseCoopers. The 30-year housing benefit model they helped produced is sensitive to both housing and labour market changes.

Some of the key assumptions and references in the model are:

- Overall housing benefit expenditure is taken from the Office for Budget Responsibility's Fiscal Sustainability Report published in July 2015.
- We use the Department for Work and Pensions out-turn and forecast data until 2019/20, amended for changes announced in the Summer 2015 Budget.
- Award and caseload in the social sector, and award in the private sector are calculated based on previous trends and industry estimates. Private sector caseload is derived from these other results, combined with the OBR top-line forecast.
- All figures are expressed in 2015/16 prices, using the Treasury's GDP deflator, which is derived for future years.
- The published figures above are not discounted. Discount rates are controversial and the subject of wide international variation. Applying the Treasury's current preferred rate to the figures above does not change the case but simply increases the payback period. It is possible to bring that period back within 30 years if we include other benefits of house-building, notably increased tax take or the asset value of the home itself.
- Labour market impact is calculated using Labour Force Survey microdata and a bespoke benefits and tax credits calculator.

For the housing policy simulations we rely mostly on readily available data sources, including:

- LGA/NFA (2012), *Let's Get Building* for the potential of councils to build, if released from housing revenue account borrowing restrictions.
- DCLG data on s106 obligations for the potential to deliver more homes through the planning system.
- Capital Economics (2014), *Increasing Investment in Affordable Housing* for data on the potential impact of borrowing guarantees and a housing investment bank.
- The National Audit Office (2012) *Financial Viability of the Affordable Housing Sector* for grant levels.

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