

Mr Gordon Clarke
Clerk of the Committee
Environmental Audit Committee
Committee Office
7 Millbank
London
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9th December 2008

Dear Mr Clarke,

NATIONAL HOUSING AND PLANNING ADVICE UNIT RESPONSE TO THE ENVIRONMENTAL AUDIT COMMITTEE'S TWELFTH REPORT OF SESSION 2007-08

1. *Greener homes for the future? An environmental analysis of the Government's house building plans*, was published on 3rd November. The report draws on oral and written evidence provided to the Environmental Audit Committee between April and May. As some of the recommendations relate in part to our remit (as set out below), it is appropriate for the National Housing and Planning Advice Unit (NHPAU) to respond.

We recommend that both the Department for Communities and Local Government, and the National Housing and Planning Advice Unit, review the share of new homes attributable to meeting the aspiration for bigger homes and gardens in their national house-building plans and targets; and seek the advice of the Sustainable Development Commission on the environmental limits of continuous annual house-building targets. (Paragraph 8)

We recommend that the Government urgently reviews the assumptions on which the 3 million homes target was based and whether it is still justified on the basis of the latest economic growth projections, fundamental changes in the mortgage market and house prices which are falling anyway. (Paragraph 12)

We recommend that the Government suspends the implementation of its regional spatial strategies until it has carried out and published an environmental appraisal of its house-building targets. We also invite the Committee on Climate Change to assess the impact of new house-building targets on the UK's 2020 carbon reduction target, and related carbon budgets. (Paragraph 18)

In the light of the dramatic financial events of the last few weeks, we recommend that the Government revisits the extent to which a target of 3 million new homes by 2020 is realistic and viable. (Paragraph 82).

Establishment of the NHPAU and its remit

2. Firstly I should provide the Committee with a little background information about NHPAU. As Members will be aware, the planning regime for housing has undergone considerable change in recent years and much of this is still bedding down. Many of the changes have flowed from Kate Barker's 2004 Review of Housing Supply. Planning Policy Statement 3 on Housing (PPS3), the Housing and Planning Delivery Grant and the merger of Regional Housing and Planning Boards are just three examples of a much broader programme aimed at addressing the well documented and long standing lack of responsiveness of housing supply in England.

3. The Barker review recognised the need for a balanced approach to spatial planning, understanding the need to weigh the environmental, social and economic consequences of decisions. A concern the review team had about the planning system with regard to housing supply was that it failed to take into account market signals and how housing markets operate. This had contributed to a situation where in the last 3 decades of the twentieth century the rate of increase in housing supply had fallen by 50 per cent while the rate of increase in the number of households had risen by 30 per cent.

4. One of Barker's recommendations was that a Unit should be set-up to ensure that better information about housing market signals were incorporated into the planning system. The Government accepted this recommendation and the NHPAU was formally launched in June 2007. Our main role is to provide independent advice to government at all levels about the impact of housing plans on affordability prospects over the medium and long term.

5. There are three main elements to our work:

- To engage with all stages of the Regional Spatial Strategy (RSS) process, from the outset in developing the evidence base through to representing our advice at Examination in Public.
- To conduct a programme of research that improves understanding of specific facets of the housing affordability and supply problem.
- To support regional partners in a practical way, in particular to help them meet obligations under PPS3 to set out the implications of their plans for affordability prospects.

Current turmoil in the housing market and the wider economy

6. As the Committee is aware, we are well into a period of adjustment in the housing market, which reached the top of the price cycle last year. While inevitably there is now a focus on short-term prospects and uncertainty arising from this, it is vital that planners and decision makers keep an eye on the medium and long-term. It is the longer term outlook that planning affects since new construction is only a small component of total housing supply.

7. Last year concerns were of ever rising prices, liberal lending conditions and worsening affordability - which had reached its worst ever position locking out more first time buyers. Now we are worried about falling house prices¹, a building industry which is cutting output² and circumstances in the finance sector that mean already hard pressed first time buyers face a situation in which mortgages are harder to secure and relatively more expensive.

8. This change has been driven by financial markets and not other fundamentals. The number of new potential households is still rising more rapidly than the number of new dwellings³, real disposable incomes are still expected to rise in future, albeit at rather a low rate in the short run, and the economy is expected to return to growth within 2 years⁴.

¹ Nationwide project a fall in average house prices of 25 per cent from 2007 peak to trough in 2009.

² The Construction Products Association forecast UK home completions will fall to 170,000 in 2008 and 140,000 in 2009 and 2010. The Home-Builders Federation is more pessimistic.

³ New and higher projections of the future population in England: a first look at their implications for households and housing – TCPA Tomorrow Series paper September 2008 and Homes for the Future- a new analysis of housing need and demand in England – Shelter November 2008.

⁴ Inflation Report – Bank of England November 2008.

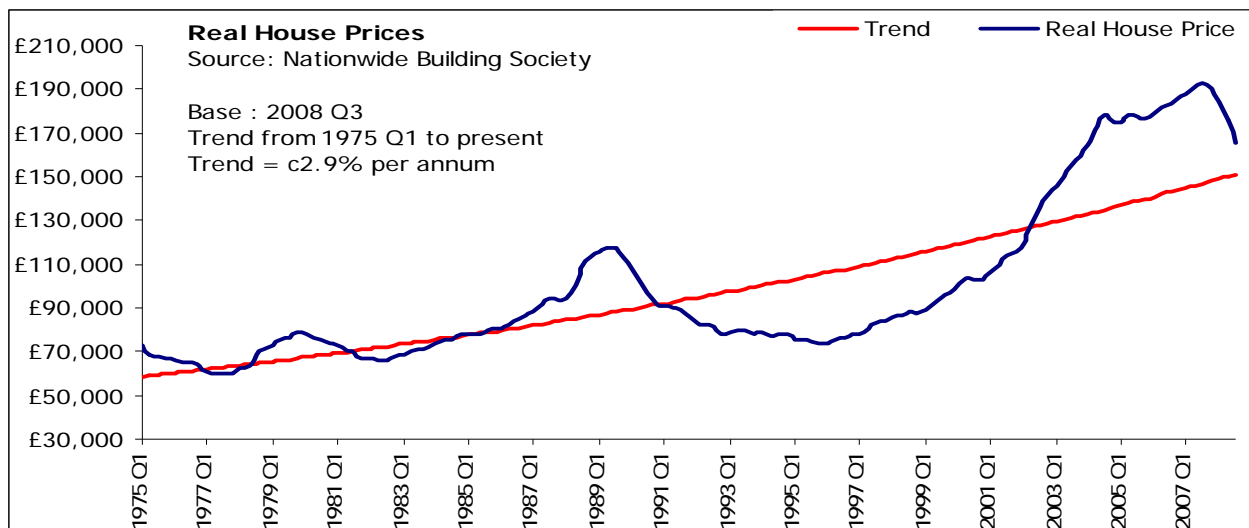
9. To generalise, due to a lack of trust, lenders find it much harder to access money markets because mortgages are no longer seen as trustworthy collateral, and mortgage backed securities are less readily traded. As a consequence there has been a big reduction in the supply of mortgages and first-time-buyers are now severely rationed. Furthermore, lending to prospective landlords in the private rented sector is also very restricted.⁵

10. First-time-buyers and purchases by prospective landlords are key to the operation of the housing market, since they soak up much of the new-build properties as well as, indirectly, properties released on the market by last-time sellers. The severe mortgage rationing that they face is undermining the market as a whole as well as the fortunes of house builders. This is why house prices are falling and will continue to fall until the mortgage market gets back to some measure of normality.

11. However, for most people the current fall in house prices is not making homes 'more affordable' in any real sense, because cheaper housing does not make it any easier for first-time-buyers if they are unable to get a mortgage. Furthermore, when credit markets recover house prices will simply go back up again if nothing else changes.

12. In *Affordability Still Matters*⁶ we set out why in a cooling housing market, and facing wider economic difficulties, it is important that planners and decision makers keep an eye on the long term. This is especially the case as planning authorities begin to consider reviewing their RSSs and the number of homes they permit to be delivered from 2011 onwards.

13. There have always been ups and downs in the housing market, but the trend in prices is relentlessly upwards - real house price growth has averaged 2.9 per cent a year over the past 30 years. This has serious consequences for individuals and the economy, many of which we feel more keenly today.



14. House price volatility has created risk and speculation, it is now impacting on consumer spending decisions, young people are shut out of owner occupation and there is increasing pressure on the private rented sector and subsidised housing. If we want to moderate this cycle then delivering the right number of new homes, of the right type, in the right place and at the right time will be an important part of the solution.

⁵ Net mortgage lending dropped by nearly 70% in October to just £459 million, a reduction of over £1 billion from the previous month and down more than 90% since last October - Bank of England November 2008

⁶ *Affordability Still Matters* – NHPAU July 2008

15. As Yolande Barnes, Head of Research with Savills said last month “House prices may be falling, but they will rise again. If we pretend that we won’t see another boom starting in the next decade, we will not be able to nip it in the bud when it comes.” The case to plan for a positive step change in housing supply is stronger now than it was before the current downturn.

Planning for the right number of new homes

16. The Committee recommends that the Government should suspend implementation of the first round of RSSs until an environmental appraisal has been conducted – we would have concerns about this. It is already a requirement for each RSS to provide a full Sustainability Assessment. In addition, if RSS plans were suspended this would inhibit the production of local authority plans, and the uncertainty generated would have further negative consequences for housing delivery. The RSS process is in any case one of ongoing review, monitoring and management.

17. Last year’s Green Paper on housing - *Homes for the Future: More affordable, more sustainable* – commissioned the NHPAU to provide the Government with independent advice about the supply ranges to be tested by regional planning authorities in future RSS reviews. Our advice was published in June⁷ and on 16th July the Housing Minister wrote to the Chairs of the Regional Assemblies to ensure that our analysis was properly tested. Testing must include a full sustainability assessment, for example setting out the effect on hard and soft infrastructure, land supply requirements and proposals on broad distribution.

Region	BOTTOM OF THE PROPOSED HOUSING SUPPLY RANGE			UPPER END OF THE PROPOSED HOUSING SUPPLY RANGE				
	Average annual net additions to 2026	Minimum delivery point by 2016	Total net additions by 2016	Total net additions by 2020	Average annual net additions to 2026	Projected delivery point by 2016	Total net additions by 2016	Total net additions by 2020
North East	6,700	6,600	61,500	87,800	7,500	7,600	66,800	97,300
North West	26,600	27,600	228,900	339,300	29,500	31,300	247,700	373,000
Y&H	23,800	25,100	202,100	302,500	26,400	28,300	218,300	331,700
East Midlands	23,400	23,700	207,000	301,900	24,600	25,300	214,500	315,500
West Midlands	19,100	19,800	164,100	243,200	22,600	24,300	186,600	283,700
East	30,100	32,100	259,600	388,000	39,200	43,000	314,300	486,300
London	33,800	35,500	286,600	428,500	42,600	46,700	342,400	529,100
South East	37,800	38,700	331,500	486,200	49,700	53,800	407,200	622,500
South West	29,800	31,000	255,600	379,600	34,800	37,400	287,400	436,800
England	231,100	240,100	1,996,900	2,957,000	276,900	297,700	2,285,200	3,475,900

18. In constructing our advice we adhered to the Government’s strategic and policy objectives for housing. We considered three separate methodologies to triangulate evidence about what was required. The first utilised the CLG Affordability Model, developed by Reading Business School, which integrates information about the labour and housing markets, and demographic trends. The Model enables us to understand the effect of supply on affordability prospects. The second was a traditional demographic method which draws on household projections and makes an allowance for constrained need and demand, vacancies and the demand for second homes. The third was a macro-economic forecasting model developed by Experian.

⁷ Meeting the housing requirements of an aspiring and growing nation: taking the medium and long-term view – NHPAU June 2008

19. Given the difficult immediate outlook for the economy and the housing market in June, we were cautious about the assumptions which underpinned our analysis; for example we used modest projections of earnings growth, interest rate prospects and levels of future household formation. We drew on the best available evidence and tools and synthesised results from the different methodologies.

20. The bottom end of our supply range essentially replicates Government targets for new homes. The top end of the range represents our assessment of what it would take to stabilise affordability over the long-term and to tackle pent up need and demand. There is no explicit allowance for bigger homes and gardens in our advice. However, we do attempt some tentative analysis about the impact of delivering more family homes and fewer flats which modelling suggests would have a more significant effect on improving overall affordability. We have recently commissioned further research about the impact of factors such as quality, density and mix on affordability outcomes.

21. Our supply advice is not a target. It is a supply range to be tested. The focus is on homes to be delivered from 2011 onwards. Our supply range should provide sufficient flexibility for regional planning authorities to consider a range of outcomes in a transparent manner, reflecting regional priorities and circumstances. For example, how far and how fast should the backlog of housing need and demand be addressed? What are the likely prospects for newly arising need and demand? What would be required to stabilise affordability? What contingencies should be provided for? And how are housing markets related between linked regions?

The consequences of not building more homes

22. In the same way that there will be environmental, social and economic consequences of building more homes, there will be environmental, social and economic consequences of continuing to under supply. All these matters must be fully tested in each RSS process. It is not the role of NHPAU to direct what the outcome of this debate should be. It is our role to try to ensure a full and transparent analysis of the trade off's being made with regard to affordability outcomes.

23. In July we published new research⁸ that we had conducted with the Cambridge Centre for Housing and Planning Research and using the CLG Affordability Model. We considered what the impact of current regional plans might be, all things being equal, compared to delivery of homes at the 'top end' of the NHPAU supply range.

24. We found that for those households still able to enter the housing market current plans would lead to deterioration in the lower quartile house price to earnings ratio. There would be further pressure on the rationed intermediate and social housing sectors⁹. Perhaps even more significant, our research suggests that household formation will be significantly inhibited by affordability pressures. By 2026 over 1 million of the households in official projections will not have been able to form. This will result in increases in overcrowding, as more people have to be squeezed into the existing housing stock, and this will produce its own social problems.

⁸ The impact of worsening affordability on demand for social and affordable housing: tenure choice and household formation – NHPAU June 2008

⁹ Projections suggest that the housing register will increase by 1 million people by 2010 - Local Government Association November 2008

The delivery challenge

25. It is clear that the house building sector is under very considerable pressure and that in the short-run the number of annual net additions to the stock of homes will fall. But we have seen this pattern in previous house price cycles and failed to plan for the upturn then. We must consider the prospects for delivery when the market recovers. Builders and developers will deliver more homes when the economic conditions are right, perhaps including utilising new business models.

26. It is interesting to note that recent reports such as the Calcutt Review (November 2007) and Homebuilding in the UK by the Office of Fair Trading (September 2008) paint a picture of a reasonably competitive industry that should be able to respond with capacity to meet supply requirements. Historically the nation has delivered many more homes - between 1950 and 1980 an average of 320,000 homes were completed in the UK each year with a peak of 425,000 being delivered in 1968.

27. The Government's housing supply targets will remain stretching, but that does not mean they are unachievable. It is still early days with 12 years to go until the target's end. We should certainly have an eye on what the social and economic consequences might be if there was a shortfall. There would be worsening affordability prospects, further pressure on the private and social rented sectors, more people locked out of home ownership, increased overcrowding and households unable to form.

Refreshing the NHPAU supply range

28. Few had foreseen the scale of turmoil in the finance sector in recent months, a situation which has also impacted on other sectors of the economy, in particular house builders. NHPAU will therefore refresh its advice in the light of these major developments and we will make our analysis public in the spring. However I want to make it clear that we do not expect this work to alter our fundamental position – that as a nation we need to build many more homes than we are currently planning for.

I hope that this note is helpful to the Committee.

Yours sincerely,

Stephen Nickell
Chairman
National Housing and Planning Advice Unit