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Going to Scale:

How a National Housing Fund Can Unlock Britain's House Building Capacity

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About ResPublica

The ResPublica Trust (ResPublica) is an independent non-partisan think tank. Through our research, policy innovation and programmes, we seek to establish a new economic, social and cultural settlement. In order to heal the long-term rifts in our country, we aim to combat the concentration of wealth and power by distributing ownership and agency to all, and by re-instilling culture and virtue across our economy and society.

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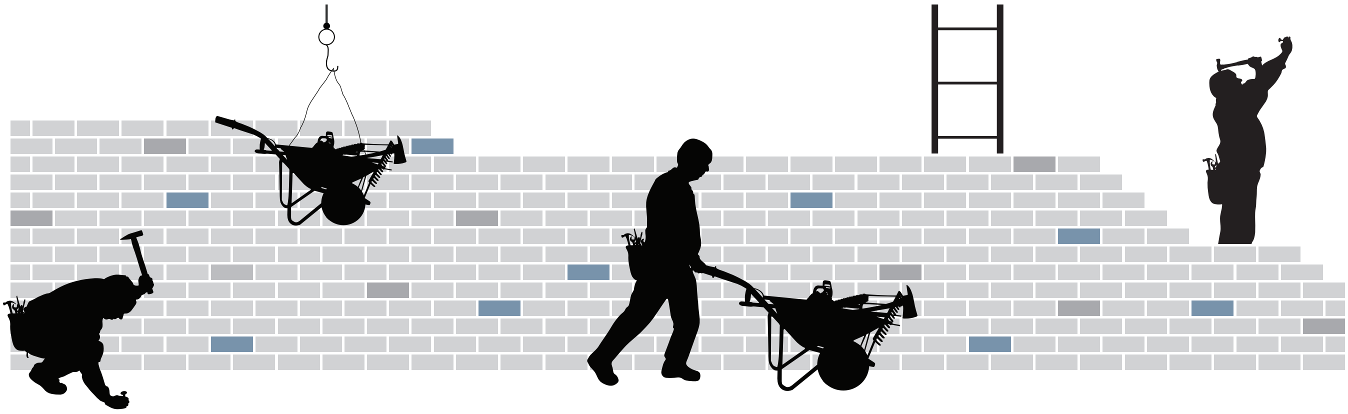


Introduction

"The real problems with the UK house building industry are number, pace and scale. We believe we have the answer – a guaranteed buyer each year for ten years for a minimum of at least 40,000 and up to 75,000 new homes a year."

The Brexit vote in June spoke to the deep divisions - in wealth, education and opportunity - in our country. Factors such as class and geography interacted with age and culture and produced a result that manifests the urgent need to re-orient policy and priority towards those who have lost out over the last 30 years.

Nowhere is this need for a fundamental reorientation of policy and direction more clear than in housing. Home ownership rates have reached a 30-year low.[1] A baby boomer at age 30 was 50 per cent more likely to own their own home than a millennial today of the same age. Over 1.2 million people languish on housing waiting lists in England, while more than 6 million face tenure insecurity and no prospect of asset accumulation in the private rented sector.[2] Prospects for moving from renting to owning are now so low that only a minority of renters under 40 are trying to save for their own home.[3] So extreme is this trend that PwC forecasts that the number of households renting privately will match the number of households buying with mortgages – 7.2 million – by 2025.[4]

The acute instabilities and pressures that the housing crisis has brought to many people are well known. When your landlord can decide whether you have a home or not; when the National Living Wage barely covers rent in houses at the bottom end of the market; when you no longer believe your children will one day own a home of their own; then policy must change.

The challenge we face is twofold. Firstly, and most importantly, we need to change the current structure of the housing market so that we finally build more homes. Secondly, in light of the current barriers to ownership we need to build good quality homes for rent and give those who live in them more long-term tenure security, as well as a pathway to owning the house that they currently rent.

The question of course is: what policy change will deliver housing at the pace and scale we need? What we do know is that private sector house builders alone will not meet the nation's needs. Over the last 35 years, on average, the private sector has built less than 150,000 homes a year – 50,000 short of the Government's current target and up to 150,000 short of some independent assessments of our housing need.[5] What this shows is clear: the current housing market, as presently constructed, cannot build the housing the country so urgently needs.

If a One Nation agenda is to move from political aspiration to practical reality, a good start would be a new way forward on housing and ownership. That means a policy intervention that delivers the types of homes we need, at the scale we need them, whilst offering those on medium and low incomes new prospects for tenure security while renting and ultimately a path into home ownership.

The last few years have seen a range of schemes on both the demand and supply side to address these twin interrelated problems.

On the supply side, the Government has sought to support housebuilding across a range of housing types and tenures – schemes such as the Build to Rent Fund, the New Homes Bonus and the Builders Finance Fund have helped. But they have not delivered at anything like the scale we need. Last year's housing starts reached 143,500 – 56,500 less than the 200,000 needed each year over this Parliament to hit the Government's own targets.[6]

On the demand side, initiatives such as Help to Buy have helped those eligible, buy homes. But they have been too concentrated in one part of the market, raising demand without sufficiently raising supply and thus increasing prices for the millions of people unable to both save to buy and pay increasingly high private rents while they do so.

The question we need to ask is: what policy can deliver new homes at the scale we need? What measure over a sustained period of time can propel a dramatic increase in house building sufficient to bridge the gap between current delivery levels and the Government's one million homes target?

We believe that much of what is asserted to hold up house building, such as land, planning and finance, are not the major problems they are commonly held to be. For example, across England there is currently planning permission for 460,000 homes that are yet to be implemented, an increase of 25% since 2013.[7]

No, the real problems with the UK house building industry are number, pace and scale. We do not have enough builders (be they public or private) of enough capacity who can build fast enough at a great enough scale. Why? Because builders largely rely on sales to determine the pace of build and will only build at the rate they can sell. And though the demand for houses is enormous those able to buy represent but a small proportion of the overall demand. What can change this? We believe we have the answer – a **guaranteed buyer** in the form of a new **National Housing Fund** running each year for ten years for a minimum of at least 40,000 and up to 75,000 new homes a year. What follows outlines our plan for a National Housing Fund that would do just that.

1 Clarke, S. (2016) "Home ownership struggle reaches Coronation Street", 2 August 2016, *Resolution Foundation* [Online]. Available at: http://www.resolutionfoundation.org/media/blog/home-ownership-struggle-reaches-coronation-street/ [Accessed 3 November 2016].

2 DCLG (2016) "Table 600: numbers of households on local authorities' housing waiting lists, by district, England, from 1997" [Online]. Available at: https://www.gov.uk/government/statistical-data-sets/live-tables-on-rents-lettings-and-tenancies [Accessed 8 November 2016].

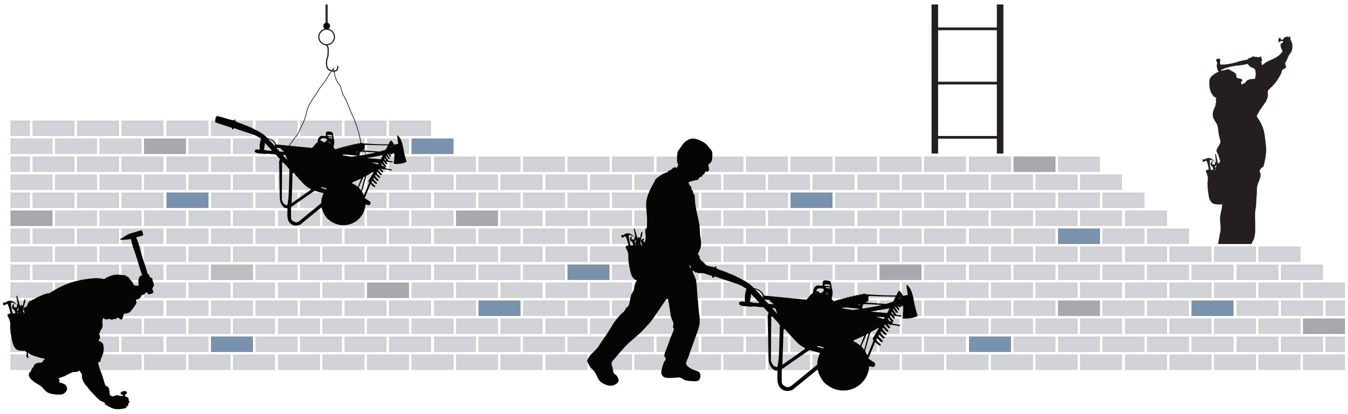
3 PwC (2015) *UK Economic Outlook*, July 2015 [Online]. Available at: http://www.pwc.co.uk/assets/pdf/ukeo-jul2015.pdf [Accessed 3 November 2016].

4 PwC (2015) *UK Economic Outlook*, July 2015 [Online]. Available at: http://www.pwc.co.uk/assets/pdf/ukeo-jul2015.pdf [Accessed 3 November 2016].

5 House of Lords Select Committee on Economic Affairs (2016) *Building more homes* (HL 2016-17, 20)

6 DCLG (2016) "Housing starts and completions hit 7-year high", 26 February 2016 [Online]. Available at: https://www.gov.uk/government/news/housing-starts-and-completions-hit-7-year-high [Accessed 8 November 2016]. Total housing supply, including new builds, conversions and changes of use, increased by 171,000 between 2014 and 2015 – see DCLG (2016) "Live tables on dwelling stock (including vacants)" [Online]. Available at: https://www.gov.uk/government/statistical-data-sets/live-tables-on-dwelling-stock-including-vacants [Accessed 8 November 2016].

7 Local Government Association (2016) "Mapping unimplemented planning permissions by local authority area" [Online]. Available at: http://www.local.gov.uk/mapping-unimplemented-planning-permissions-by-local-authority-area [Accessed 8 November 2016].



1. The need for a fresh approach

"The Government has set a target of building one million homes over this Parliament – equivalent to 200,000 each year - but on average, over the last 35 years or so just under 150,000 new homes have been built each year in England."

On average, over the last 35 years or so just under 150,000 new homes have been built each year in England, with just 139,690 homes completed in 2015-16. This total comprises output from all types of builders, but the overwhelming majority were produced by the private sector house builders (some 111,000 homes in 2015-16) and housing associations (26,000 homes in 2015-16).

Projections agree that to cope with both migration and new household formation 250,000 new homes need to be built each year. This is without addressing the 800,000 homes shortfall in new supply that extends back to the year 2000. This lack of supply has a deeply adverse impact on housing costs and job mobility.

As stated above, we believe that contained herein is a clear and credible policy proposal that could, if backed by the Government, create at least an extra 40,000 and up to 75,000 homes per year with a fully repayable £10 billion annually invested by the Government into a National Housing Fund created in partnership with major housing associations. We envisage this scheme running initially for ten years.

The immediate gains from this proposed scheme are potentially enormous: adding, on 2010 figures, 0.4% to GDP and up to £2.4bn of tax receipts each year, as well as supporting as many as 200,000 jobs.[8] The impact would be realised, given the swift impact of housing construction, within 12 months and represent a significant boost to a post-Brexit economy. Repeated investment over the next 10 years would provide the essential stimulus for construction infrastructure investment, the development of long term skill supply, innovation in house building and it would finally unlock major development sites, since there would be a certainty of demand to enable them to be built out at scale.

It would also act as a stimulus to reconfigure both the housing associations sector and the lower capacity private sector builders. In terms of the housing associations this plan would release the embedded capacity of a sector containing, on current figures, around three million homes and a total asset value in excess of £138bn. This investment would substantially enhance the pace at which the larger associations were able to move on from being SME developers to producing 4,000-plus homes each annually as larger-scale homebuilders. The National Housing Fund would accelerate the rate at which they could expand their development by providing them with a guaranteed purchaser for part of their building programme.

These associations would also build further capacity into the mid and lower tier of the private house building market, being the natural partners for those developers producing anything from 300 to 2,000 homes annually. The interaction of those developers with the larger associations in the Fund would in turn enhance the capacity of these SME developers turning them into similar engines of housing production.

Housing Delivery Across England

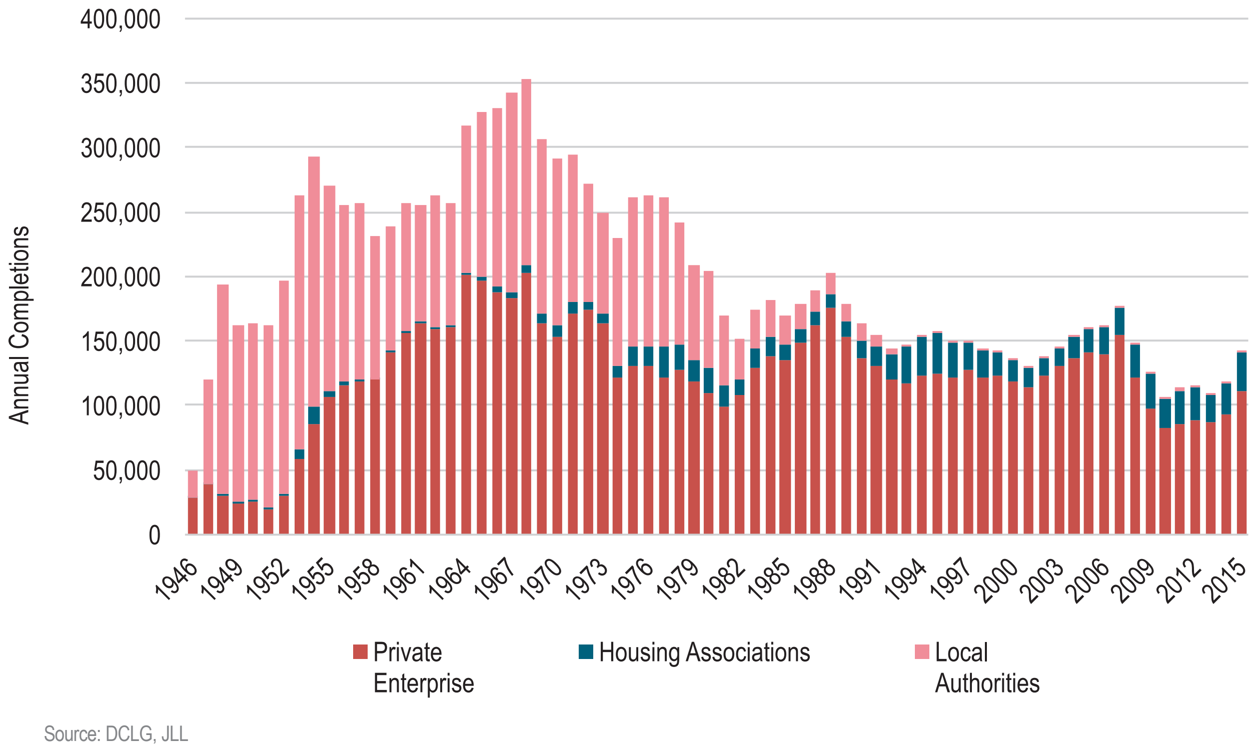


Figure 1 - Breakdown of historical housing delivery, by sector (1946-2015)

The private sector will only build at the pace that it can sell and with the market already slowing, the future pace of production will reduce further to match anticipated sales. Government-funded intervention on the demand side may help to speed sales but there is scant evidence to demonstrate that additional homes would be produced as a result.

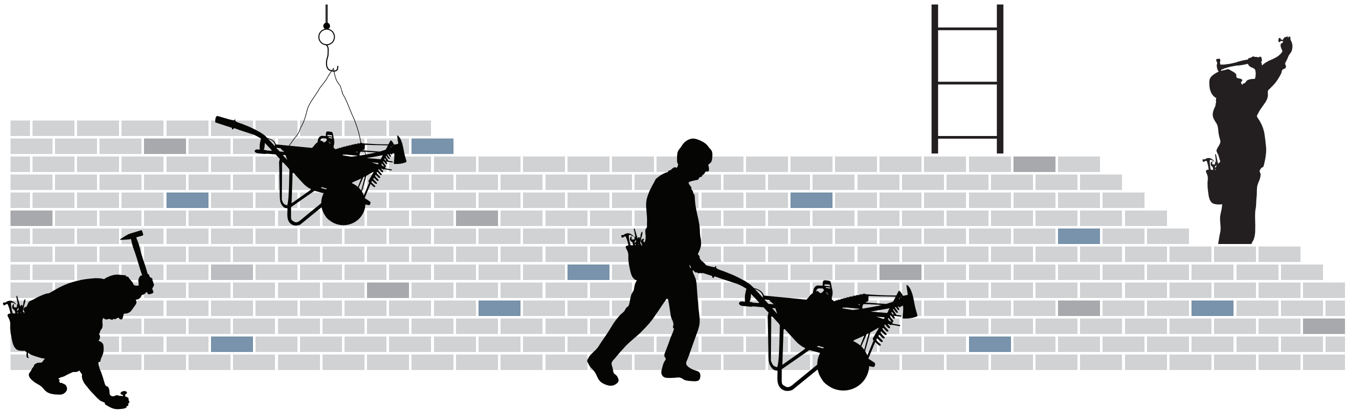
Housing associations, on the other hand, have demonstrated the ability to build more homes and create innovative methods of funding new homes for sale and rent. Associations have the potential to dramatically increase production but the fragmented nature of the sector prevents the effective use of associations' embedded capacity. It is our view, therefore, that any scheme that seeks to build more homes must concentrate on housing associations and SME private sector builders to facilitate the sustained expansion of output.

The previous five years under the Coalition Government focused on support for first-time buyers through schemes such as Help to Buy. Housing then dominated last year's general election campaign and was followed by early action to introduce Starter Homes and extend the Right to Buy. These actions have not addressed the fundamental issue of a lack of supply.

The appetite for policy-makers has now rightly shifted to supply side issues looking at for example, unlocking major housing sites shunned by the private sector because uncertainty of sales prevents the infrastructure investment required, hence the recently announced Government fund to finance such investment is most welcome. Equally estate regeneration to create more economically mixed and sustainable communities is on the policy agenda as are issues around housing conditions, availability and price in the private rented sector.

However, despite such measures the house building market, as currently configured, will not meet the supply deficit and a new solution is required.

8 Savills (2010) *The Case for Housing* [Online]. Available at: http://pdf.euro.savills.co.uk/uk/market-insights/the-case-for-housing---spring-2010.pdf [Accessed 8 November 2016].



2. The Ask of Government: a new fully returnable public investment in housing

"The National Housing Fund would provide a secure and sustainable route to increased production of new homes. It operates in addition to the existing sales or grant-subsidised new homes market. For developers, it provides a guaranteed purchaser of new homes, and would build up the capacity of SME developers and housing associations over the long-term."

The National Housing Fund

This report demonstrates how the Government can use historically low funding costs to create a functioning housing market through measured investment in new supply. Its scale mirrors previous intervention by Government into a series of broken markets and successful past interventions to boost housing supply; especially from 1951- 1971. But it would be structured to support greater diversity in the market and would expand building across all types and tenures. As such, it would equip the market to genuinely meet people's needs at different points in their lives across the country and across income ranges.

This intervention would be delivered through the creation of a yearly National Housing Fund formed with a group of housing associations who would bid to join each year of the Fund.

The Fund would operate with Government providing funding through 50-year gilts and the associations providing the exit route for Government by agreeing to buy out the Government's share at an agreed point. Adopting this financial instrument approach would ensure that the intervention would not add to the deficit. Moreover, the immediate and sustained gains to the economy would more than justify the Government's investment, with £2.4bn in economic growth potentially gained in the first year. The Government could pace in and negotiate any return over and above costs that it would look to recover.

The Fund would access funds via low-cost long-term Government borrowing such as bonds, a route the Prime Minister has already rightly suggested the Treasury should examine (for example, 50-year gilts at c.1.5%).

The Fund would be a joint venture between Government and the housing association sector and be created through a traditional private company structure with shares. These would be held equally by the Government and the participating associations.

The Government would secure the long-term funding and on-lend to the Fund. The associations would begin to buy out the Government's shares (in, say, year 11). The share purchase would be at a nominal value with the associations then taking sole responsibility for the future repayment of the initial loan of £10 billion. The Fund would, however, commit to continuing to provide properties of particular tenures for specified groups. The Government would retain the option of retaining some of the shares – perhaps as 'Golden Shares' – to ensure the continuing mission and social purpose of the fund, such that current funds and any surplus is available to finance on a national basis an ongoing social mission.

The associations, as controlling shareholders in the Fund, would be free to trade shares or invite additional similarly minded and suitable investors to join, such as local government pension schemes. Crucially, though, the embedded value of the Fund would be captured within the Fund and its inherent social mission. The charitable status of housing associations would prevent any leakage from housing provision as only those upholding the mission and purpose of the fund could retain and reinvest the ongoing returns of this investment. Hence, this approach is significantly more attractive than those based on other sources of investment that generally leak public surplus into private return. In short the surplus generated by the fund over its 50 year cycle would remain dedicated to the public good and constantly replenished by rents and sales which would be reinvested in new homes and/or social projects aimed at improving the education, health and well-being of those who rent or buy these homes. Such an approach would speed up the realisation of larger sites and boost regeneration, representing a massive ongoing public endowment.

Structured and sustained investment

This proposal envisages Government investing £10 billion annually over the next 10 years to deliver at least 40,000 and up to 75,000 additional homes per annum into a National Housing Fund. The Fund would serve as guaranteed buyer for these homes, delivered by housing associations and/or SME builders and offered as market and submarket rented homes. With a Fund in place to act as a guaranteed buyer of new homes over the long-term, this would provide counter-cyclical support to deliver more homes and build capacity amongst housing associations and smaller builders. By raising capacity of housing associations and medium and small developers, it would improve the long-term health and capacity of the housing market.

Our analysis shows that this could enable national output to climb to 200,000 homes per year over the next decade and then be sustained at that level. It would be a transformative long-term intervention with the Government investing and acting to challenge and change a dysfunctional market.

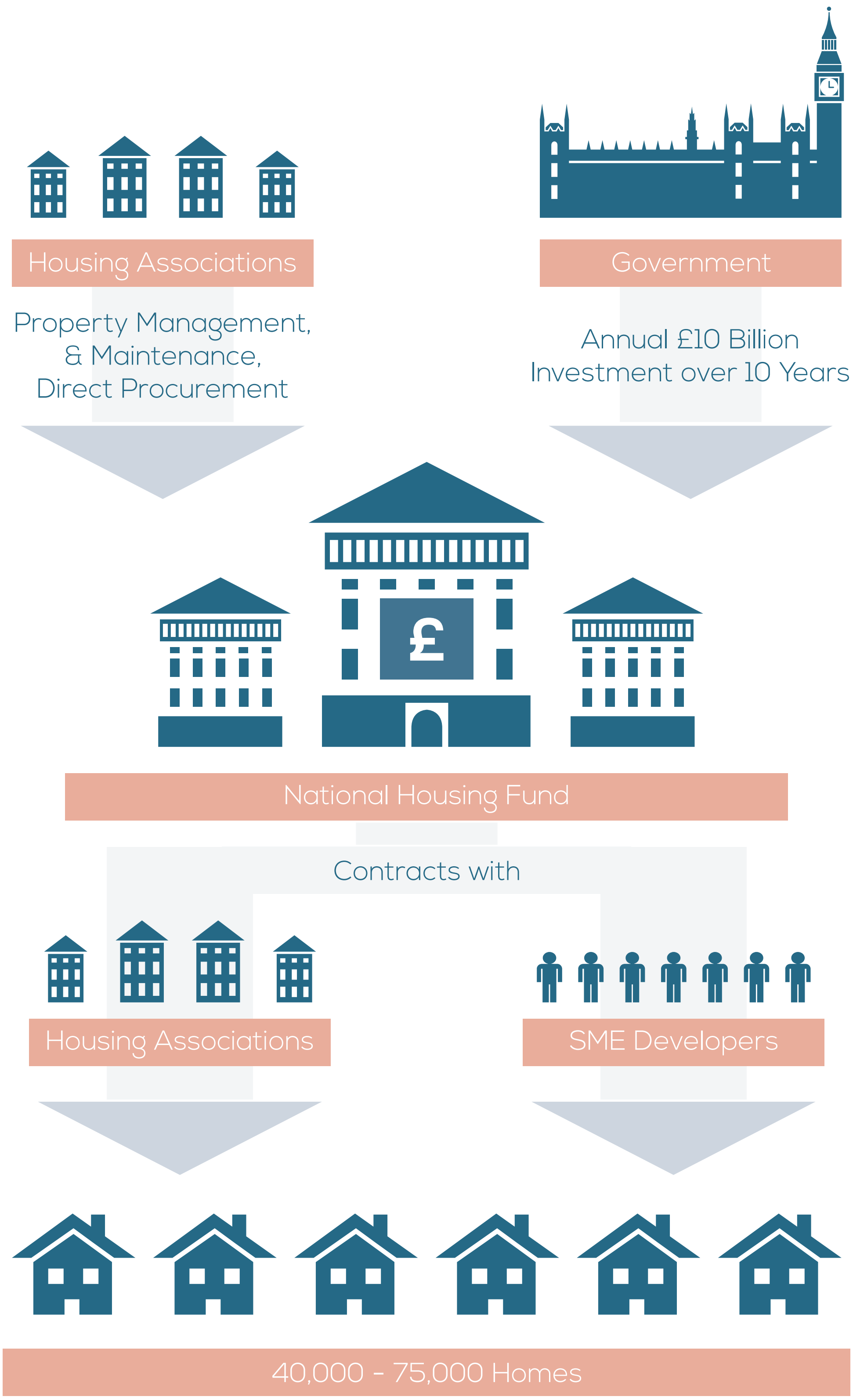
An intervention at this scale would give the Government an immediate return on its investment via the direct gains that flow from the construction of these additional homes. In addition this proposal considers the subsidiary benefits of a restructured housing market, where the additional output positively impacts on the type and cost of rented housing. It highlights the potential gain to the public sector of utilising part of the output for specific groups of employees, such as nurses, the police force, teachers, and other key workers.

Notwithstanding questions surrounding the classification of housing associations as public sector bodies, (legislation to change this definition is currently planned), the debt in the Fund, however it was classified at the outset, would progressively move off the Government's balance sheet from year 11.

It would not impact on the Government's current efforts to introduce new regulations to reclassify housing associations as private sector bodies because the Fund would operate as a private limited liability company with an initial issue of 1,000 shares. These shares will be owned by government and the founding housing association members. In the unlikely event that housing associations remain classified as public sector bodies in 2028, government should have the ability to offer its shares to mission driven private sector organisations or social enterprises, (providing they abide by the founding social ethos of the fund) ensuring that the National Housing Fund is not classified as public sector vehicle at that point.[9]

9 The Housing and Planning Act 2016 includes a number of deregulatory measures that will tackle the issues flagged by the ONS. These focused largely on the relationship between the regulator (the HCA) and the sector. These deregulatory measures must have commenced before the ONS can reconsider the status of housing associations. The National Housing Fund would not affect the role of the HCA nor efforts to deregulate the sector; nor would it change ownership or control of housing associations.

How would the Fund work?



Case Study: The National Housing Fund model

The National Housing Fund provides a secure and sustainable route to increased production of new homes. It operates in addition to the existing sales or grant-subsidised new homes market. For developers, it provides a guaranteed purchaser of new homes:

1. The Housing Fund does not compete for sales with developers as all homes are rented for at least 5 years. This is a crucial positive distinguishing factor compared to the Starter Homes initiative. And they are sold to organisations who specialise and excel in successfully managing large portfolios of rented homes – housing associations.

2. Homes are let to economically active tenants who aspire to buy at a future date. This adds value to the rest of the development as the homes are owned by one well managed landlord rather than an eclectic group of investor landlords.

3. Where homes are subsidised, they are targeted at specific client groups, such as nurses, the police force, and teachers. Again, it adds value rather than detracting from the value of the stock as social rent is often viewed negatively in the eyes of some external purchasers.

4. Therefore, the sales to the Housing Fund do not diminish the value or pace of the sales of the developers' own sales product.

5. Certainty of sales to the Housing Fund will enable developers, especially smaller developers, to secure funding for their sites at a lower interest rate and lower equity hurdle (e.g. the banks may lend them 60-70% of development finance at 3 over base rather than 40-50% at 4-6 over base).

6. The certainty of sales will enable developers to produce at an accelerated rate. For example, rather than a production that allows for say 2-3 sales per month with 25 homes being produced over a year the developer could produce twice or three times as many homes knowing the Housing Fund will take up these extra properties.

7. This pre-sale will accelerate development as developers can pre-sell the first and second phases of developments establishing the essential presence on the site and giving it initial depth to the market for that development – thereby allowing the natural sales market to develop.

8. The national Housing Fund will provide an economic close out for the end of site development taking on the remaining properties at the end of a development.

9. These factors will enhance the pace of development and the efficiency of the capital employed. It will provide the smaller developers with a significant benefit enabling them to grow their business. It is worth noting that most of today's major developers grew up as contractors for government in the 1950/1960s, under a similar guaranteed buyer scheme.

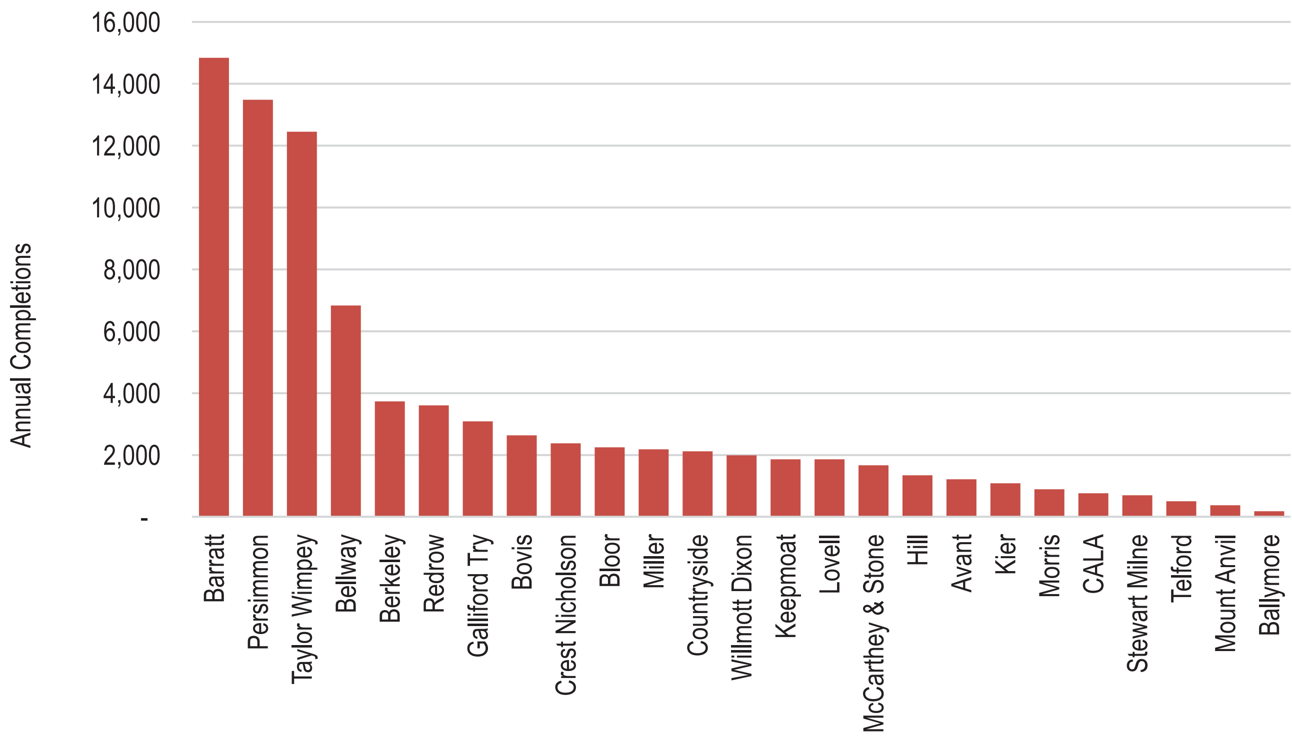
The Housing Fund, repeated over 10 years, will foster new supply chain capacity stepping outside of the 10-12 larger developers who exert profitable influence on the market. This has functioned to constrain the market by limiting to the business models of its dominant providers and squeezing out the market needs and hence the capacity of small builders.

The certainty of purchase will draw in new providers and enable developers in the 11-40 range of development output to grow over the next 3-5 years' upscaling their output. Moreover, it will provide the 3,000 or so small developers who produce 1-100 homes per annum with the opportunity to increase their output. If each produced an extra 15 or so properties this would provide the additional 40,000 homes envisaged.

In addition, housing associations have helped to produce around 20,000 -30,000 homes per annum. With the significant curtailment of grant the larger associations have sought to become developers themselves, producing housing for sale to provide the subsidy required to sustain submarket rents. The associations market has started to consolidate as the larger associations are seeking to establish themselves as scale developers. We believe housing associations with the aid of the National Housing Fund could comfortably add another 20,000 homes to their current level of construction.

In short we believe that the proposal we advocate herein can rapidly grow house building capacity in two previously dormant sectors and utterly transform the British housing market to everyone's benefit.

Top Housebuilders by Annual Completions



Source: Housebuilder, JLL, Completions 2014

Figure 2 - Top housebuilders by annual completions

Building capacity, increasing production, creating new homes

Crucially we envisage The National Housing Fund only buying homes that are initially for rent. We want to avoid any economic displacement of sales activity since our intention is to increase housing production – not simply buy houses that would have otherwise been bought by others. Initially, the Fund would support existing schemes, accelerating the pace of development and bringing forward planned phases of construction. This would have the positive impact of encouraging production to be maintained at current levels rather than decline as the wider sales market slows.

However, the bulk of the Fund's activity would give housing associations the means to build more; and create joint ventures with private developers outside of the top ten house builders, using the skills, capacity and enthusiasm of this group of developers to rapidly expand production. This co-ordinated investment would help provide what the market has singularly failed to do – tens of thousands of new homes on an annual basis.

In terms of expanding capacity to build amongst the private developers, the house building market has historically been populated by many SME businesses focused on their local markets; constructing homes that are in tune with their local area. Over the last 25 years, a series of recessions has been matched by a withdrawal of access to funding that has decimated this industry and seen the number of small builders (building less than 100 homes each year) fall from over 12,000 to less than 3,000.

At the same time, consolidation amongst the larger producers has created a market dominated by 10 or so companies producing around 67,000 homes in 2015. These companies exert considerable influence over the market, too often determining the pace and the scale of output.

This group has been highly successful in lobbying successive governments to provide incentives to weather their downturns in the housing market; Help to Buy is the latest in a line of such incentives. However, there is little or no evidence that these incentives increase overall output.

We argue that any attempt to boost output should look outside this group to supplement existing levels of delivery. Our proposal demonstrates how sustained investment in joint ventures with the wider developer market will significantly increase capacity and drive up production of new homes. Initially the Fund when looking

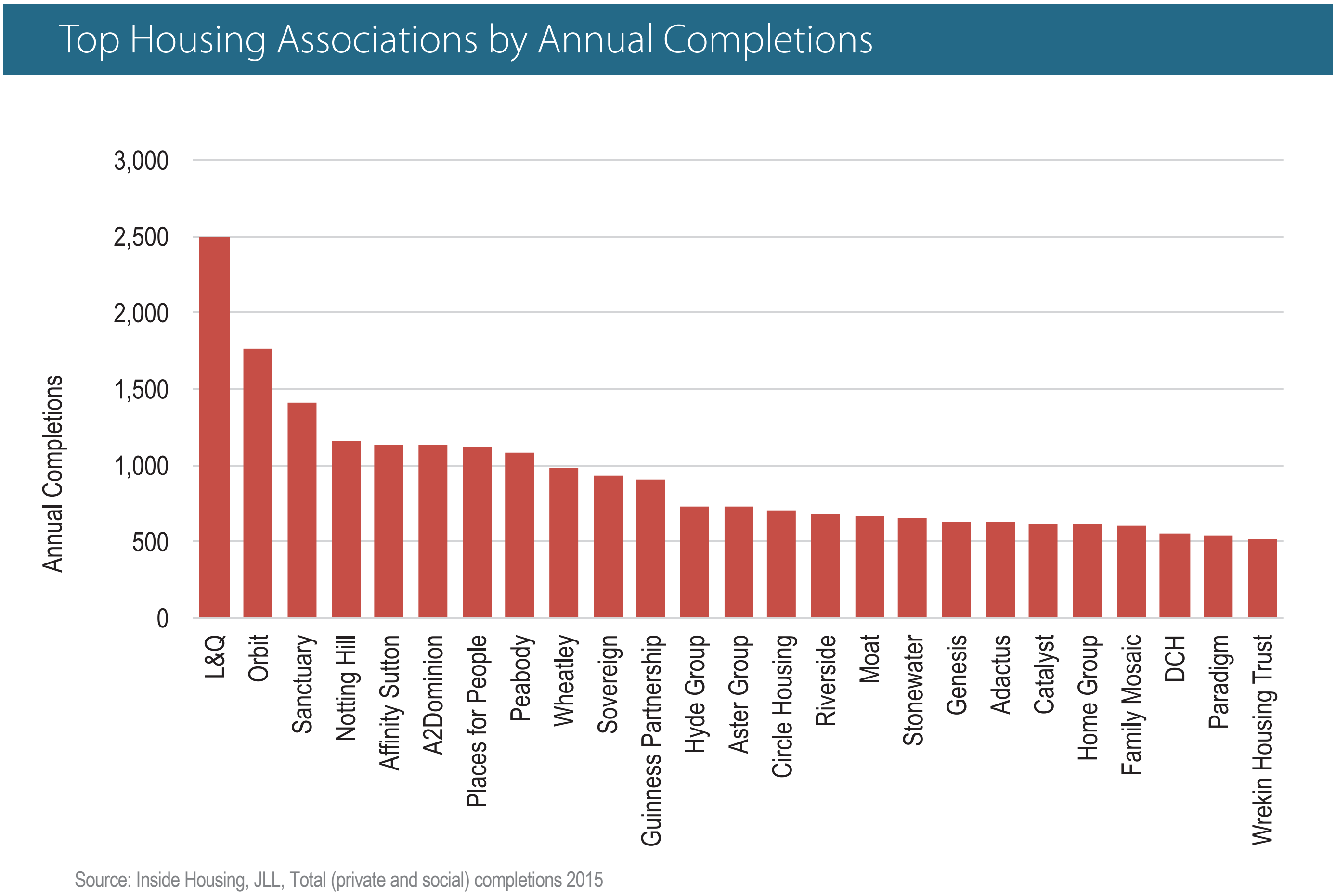


Figure 3 - Top housing associations by annual completions

at the private sector will focus on the developers ranked 11-40 in terms of output. This group produced 25,000 homes last year. The variation in output demonstrates the rapid tapering of the market, with Countryside, the 12th largest developer, producing 2,134 homes last year and Springfield Properties, the 40th, producing just 455 homes.

We believe that these SME developers have the capacity to sustain significant growth in output but are restrained by the structure of their current capital and project finance.

The Fund would address this by providing these developers with a secured exit route for their developments. It would enter into joint ventures, shaping developments and guaranteeing to buy completed homes at an agreed price. These contracts would be structured to enable these companies to secure project finance for their developments and build out their sites at a much more rapid pace.

As the capacity of these developers increased, the National Housing Fund could look to expand the number of developers it contracted with, thereby growing future capacity to sustain the scale of increased output.

For the last 30 years housing production has been inescapably linked to the sales market with its cyclical performance following the wider economy, as Figure 4 illustrates. The cyclical nature of the market works against sustained investment in the essential infrastructure to support house building. Each downturn of the market reduces capacity as the workforce is shed, skills are lost and component producers downscale. This in turn creates inflationary pressures as the market improves, with labour and material costs rising as short term demand outstrips the much reduced supply. This is best illustrated by the requirement to import bricks over the last few years.

The Fund would provide certainty of demand that would stimulate infrastructure investment in building components and the construction workforce. Producers would know that there was a steady market seeking components to produce an at least an additional 40,000 homes each year. The 11-40 developers would have the confidence to invest in jobs and capacity, safe in the knowledge that they have willing and able purchasers for their output.

These additional homes would initially as previously stated, be for rent, with any future purchase by tenants delayed to year six or, depending on conditions, to year 10 (therefore not competing directly with planned sales by house builders or associations). The rents could range from heavily subsidised rents for key workers through to market rent.

Cyclical Nature of Housing Construction in England

Source: DCLG, JLL

Figure 4 - Cyclical nature of housebuilding in England

Although producing the extra homes each year would have a measurable impact on the wider market, it is contended that the Fund could tackle asset inequality and social instability by using its scale to reset the market rented sector. It could offer five-year or ten-year tenancies that provide for security of occupation. Some of these homes could be deployed to provide steps to ownership; with options including the ability to fix the future purchase price at the point of rental or save some of the rent into a deposit scheme.

In the first year the Fund would focus on expanding delivery and maintaining it at an additional 40,000 homes per annum as a minimum. However, it would seek to work with Government and public service agencies to identify where additional housing would assist the delivery of wider policy goals, such as addressing the performance of failing schools by being able to match a job offer to the best new teachers with attractive and affordable housing.

The Fund could provide a route to unlocking major housing sites that often stall as they rely on sales to fund the essential infrastructure. As such, it could support the Government’s provision of infrastructure finance through the new Home Building Fund and lock this together with sites and an accelerated scale of purchases. There are numerous regeneration sites throughout the country where many additional homes could be delivered. Many of these sites will deliver substantial benefits to the local economy and act as a further boost to housing and associated development. Without intervention these sites will lie fallow for years; examples include Holt Town and the wider surrounding district in Manchester where up to 4,000 houses could be built, providing the essential next phase of the regeneration of Manchester and retaining its economically active population as they move from apartments to houses.

The ability of the Fund to guarantee purchase of future phases would provide developers with the certainty of income to push ahead with the infrastructure investment, safe in the knowledge that it would be repaid as each phase of the development was delivered.

Similarly, the Fund would also accelerate the pace of current building by the housing associations themselves. The ability of those associations to pre-sell sales products to the National Housing Fund will accelerate the rate at which these associations become established as significant developers of all forms of housing. Already several associations have aspirations for development programmes that would place them in the top 15 developers. In practice this part of the market will grow slowly without the stimulus provide by our proposed Fund, not least if there is a housing market downturn and a larger association encounters difficulty. The potential exists for around 10 larger associations to fully enter the developer market producing, say, 2,000 to 5,000 homes each and therefore adding approximately 20,000 additional homes over current output, if our proposal is implemented.

Although associations can access funding at a much lower rate than the SME developers they have an understandably cautious approach to risk and funding capacity limits, both of which constrain the overall size of their development programme and the pace at which they develop out sites – especially larger scale regeneration sites. The Housing Fund would enable them to better expand their risk appetite by providing a guaranteed purchaser for part of an expanded development programme. Moreover, the National Housing Fund would be outside their existing programmes and would not consume their funding or capacity, thereby ensuring that the Fund genuinely aided the production of additional homes. Along with the SME developers the Housing Fund would act as a catalyst to transform these larger associations from smaller scale participants in the development market to mainstream developers.

Taken together, these factors will enable development at a higher level and pace. The Housing Fund would sit alongside associations' development programmes and Government could look to set a scale 'hurdle' when selecting the founder association members of the Housing Fund.

The associations would bring all of their patient investor skills to the fore in assessing proposed developments and the ability of these new homes to sustain demand for rent or ownership over 25 years and beyond. The associations would ensure that the developments created economically sustainable communities.

Case Study: Operation of the National Housing Fund Model

Structure and ownership

The National Housing Fund (NHF) will operate as a private limited liability company with an initial issue of 1,000 shares. These shares will be owned by government and the founding housing association members.

Shares will be split between the government (50%) and the associations (50%). It is envisaged that there will be 5 founding association members who will in total hold a 50% share in the NHF.

This model will be replicated annually, with government holding 50% of the shares in each year's NHF and the joining associations holding the remaining 50%. It is envisaged that new association members will join each year, supplementing or replacing the founding association members.

Therefore, each annual HIF will be established on a separate basis and identified as NHF 2017, NHF 2018, etc.

Sale of shares

Government will have the option of requiring the associations to acquire all or the majority of the government's shares in year 11 of each NHF. This put option will enable government to dispose of its interest in the NHF at a given point. For illustration, the first NHF will be established in 2017 and government would then depose of its interest in 2028 requiring the association in the 2017 NHF to acquire its shares.

The associations will have the right to acquire the shares at nominal value in year 11 of each NHF. It is acknowledged that the NHF should have greater value than the initial £10bn invested at the outset, however, the association shareholders will, by acquiring the government's shares would be taking on the responsibility for the eventual repayment of the £10bn loan in 40 years' time. They would then have the option to sell down some of these shares to third parties.

In the unlikely event that housing associations remain classified as public sector bodies in 2028, government will have the ability to offer its shares to appropriate mission driven private sector organisations, ensuring that the NHF is not classified as public sector vehicle at that point.

Funding and life of the NHF

The annual NHF will secure funding via government gilts with the expectation that government will seek 50 year funding at circa 1.5%. Each NHF would have a target life of 50 years until the repayment of the gilt. It is assumed that the gilts will attract interest with full repayment in year 50 through the sale of assets at that point, or refinancing.

Government would then on lend to the NHF, with an undertaking from the associations to acquire the government's shares in year 11 (or enable a third party private sector body to acquire the government's shares). This arrangement will provide the NHF with access to low cost funding and maximise the number of homes that could be acquired by that NHF. It will also enable the funding to be classified as a financial instrument ensuring that the debt did not count towards the government's deficit calculation.

Drawdown rate

The initial NHF will require a period of mobilisation and time to create relationships with developers. Government would raise £10bn of funding and allow the NHF to draw this down over an 18 month period as it acquired homes. Subsequent NHF will draw down funds over 12 months.

Operation of the NHF

The NHF would operate with a focused management team and board nominated by government and association shareholders. The management team would be responsible for drawing up the investment criteria and tenure mix for the portfolio, with both being agreed by the government and association shareholders.

The management team would engage with a variety of developers, agree a product specification and purchase price on completion. They would regularly review developments during the construction phase and pay over funds on completion. They would engage the associations to provide a comprehensive asset management service, providing for the management and maintenance of the homes within the NHF. The NHF would be accountable to government for the delivery of the 40,000 homes and would negotiate with government on the proposed portfolio mix on an annual basis.

Case Study: *Continued*

Mobilisation

Assuming for the sake of example that the Autumn Statement initiates the creation of the NHF then a 6 month mobilisation period is envisaged.

Months 1-3 would focus on the creation of the NHF, the establishment of the investment criteria and the initial portfolio mix. A small team of skilled executives and non executives have been identified offering substantial experience of establishing new enterprises, funding, institutional investment, property development and management and operating with government agencies.

This team will form the mobilisation team and will start to recruit the board and senior executive team that will run the NHF. Months 4-6 will progress discussions with developers to a formal status and identify homes that could be acquired by the NHF within the coming 12 months.

The aim will be to have a substantial programme of delivery agreed by the end of the mobilisation period.

How does this differ from the Government's Home Building Fund?

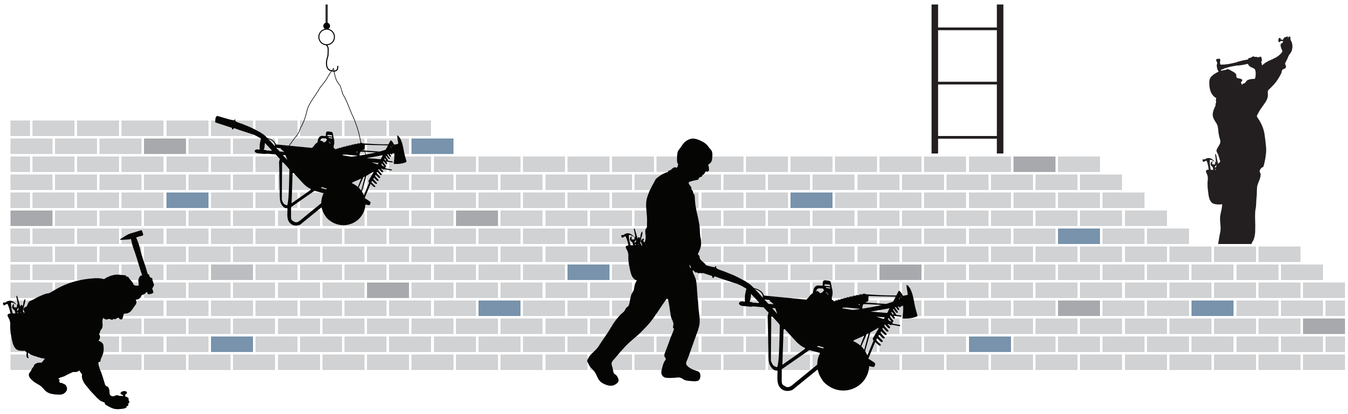
The Government recently announced plans for a new Home Building Fund. This will be worth £3 billion, consisting of £1 billion of development finance to provide loans to SME builders, principally aimed at increasing diversity in the market and supporting innovation in construction; and £2 billion of infrastructure finance to allow housing progress and prepare land for development.

Whilst this is a very welcome step in the right direction, but it is a short-term intervention at a much smaller scale than our proposal. Access to finance is a clear issue for many smaller builders and new entrants – and for builders using new modes of constructions, lenders remain risk averse in their approach to lending. But £1 billion is a comparatively small pot of money if we are serious about sustainably building up capacity in the market. It is likely to largely provide help to SME builders looking to realise existing development plans.

Moreover, this initiative as currently outlined does not address the issue of the purchaser. We believe that a separate, large-scale intervention in the form of our Housing Fund should sit alongside the Home Building Fund. The National Housing Fund would give certainty of demand to SME builders as there would be a guaranteed customer (i.e. the Government via housing associations) over a period of 10 years. This would attract new entrants and allow existing SME builders to increase their capacity sustainably, as funding would be repeated on an annual basis that would give SMEs certainty of sale.

With a Housing Fund in place, small developers could take an option on a site and then approach the fund with a plan for development of that land. The developer would then work up an agreement with the fund on price, size, layout and timing. An agreement to purchase from the fund would provide the security for SMEs to obtain development finance at a competitive rate with low equity investment. This would free up their capacity to do more schemes and gives them a better rate of return – which in turn would result in lower costs to the Fund per scheme.

Moreover, our proposed National Housing Fund would catalyse the growth of housing association delivery. It would encourage the consolidation of the association market by boosting the capacity of large associations to rapidly expand their development delivery for homes. This will unleash their future potential to sustain future development. As such, it would be a more holistic approach to addressing our supply needs as it would raise market capacity through both SME builders and housing associations.



3. What could The National Housing Fund deliver?

"The National Housing Fund could deliver between 40,000 and 75,000 additional homes a year - finally bridging the gap between current levels of delivery and the Government's housebuilding target."

In this section, we look at the potential buying power of the Fund, across four main scenarios: an even geographical spread; a regional focus; and focus on London and the South East; and a two phase approach. The full methodology on which this analysis is based is outlined in JLL's report, released alongside this publication. We find that the Fund could deliver between 40,000 and 75,000 additional homes a year.

Assumptions

Rents

Monthly median rents were sourced from the Valuation Office Agency for studios, one bed, two bed and three bed homes for each of England's nine regions. The VOA sample group includes a blend of flats and houses. Rental growth as forecast by JLL has been built into our analysis.

Unit mix

We have used the below indicative unit mix, which is typical of current Built to Rent schemes. In reality any variation on this could be purchased by the Fund, but a weighting towards higher value two bed and three bed units would of course reduce the overall buying power of the Fund.

	Unit Mix
Studio	10%
One Bed	40%
Two Bed	40%
Three Bed	10%

We have included studios because many private rental housing development schemes will include studios to comply with local authority development plans. We have also looked at one scenario in which studios are removed to assess delivery potential in line with the Fund's attempt to support the 'squeezed middle' and young families through the delivery of slightly larger mid-market rental and rent-to-buy tenures.

Yield assumptions

The model is priced on a gross yield basis, exclusive of management and maintenance costs. In reality, the Fund will buy on a net yield basis, and this would result in a reduction in gross rent as well as the yield. This gross-to-net leakage, which JLL has typically found to be 25% in the current Build to Rent sector, will ultimately result in the same buying power for the Fund as has been modelled for this report.

Transaction costs

Agent fees, legal fees and Stamp Duty have been factored into the model.

Scenarios

We have started by look at the buying power of the Fund across a number of geographical scenarios. The issue of additionality is addressed in the following section.

Scenario 1: An even regional spending allocation – 80,475 homes per annum

JLL modelled the potential buying power of the Fund assuming an even allocation of the £10bn pa in each of the nine English regions. By adopting this strategy a theoretical total of **804,750 units** or an average of **80,475 units pa** could be purchased.

Scenario 2: A regional focus – 94,400 homes per annum

JLL modelled the potential buying power of the Fund assuming the £10bn pa Fund was weighted significantly towards the North and Midlands. By adopting this strategy a theoretical total of **944,000 units** or an average of **94,400 units pa** could be purchased.

Scenario 3: A London and the South East focus – 59,380 homes per annum

JLL modelled the potential buying power of the Fund assuming a weighted allocation towards London, the South East and the East. By adopting this strategy a theoretical total of **593,800 units** or an average of **59,380 units pa** could be purchased.

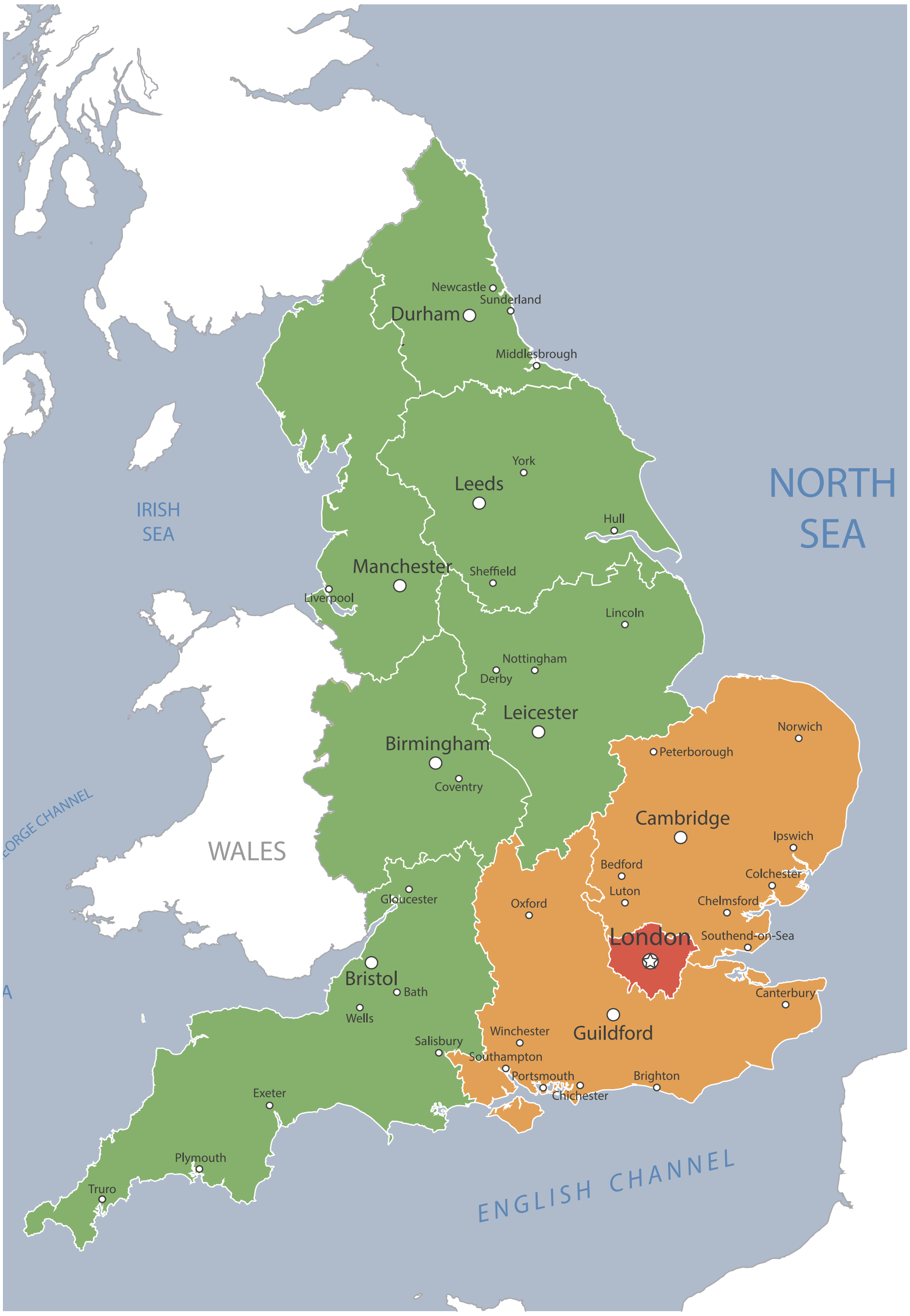
Scenario 4: Initial London and South East focus followed by regional focus – 73,850 homes per annum

JLL modelled the potential buying power of the Fund combining an initial focus to London and the South East in the first five years, followed by a regional weighting in years 6-10. This is considered the most sophisticated of the strategies modelled allowing for greater power. By adopting this strategy a theoretical total of **738,500 units** or an average of **73,850 units pa** could be purchased. See Maps 1 and 2 on the following pages for a visualisation of this spread.

Scenario 5 – impact of removal of studios from scenario 4

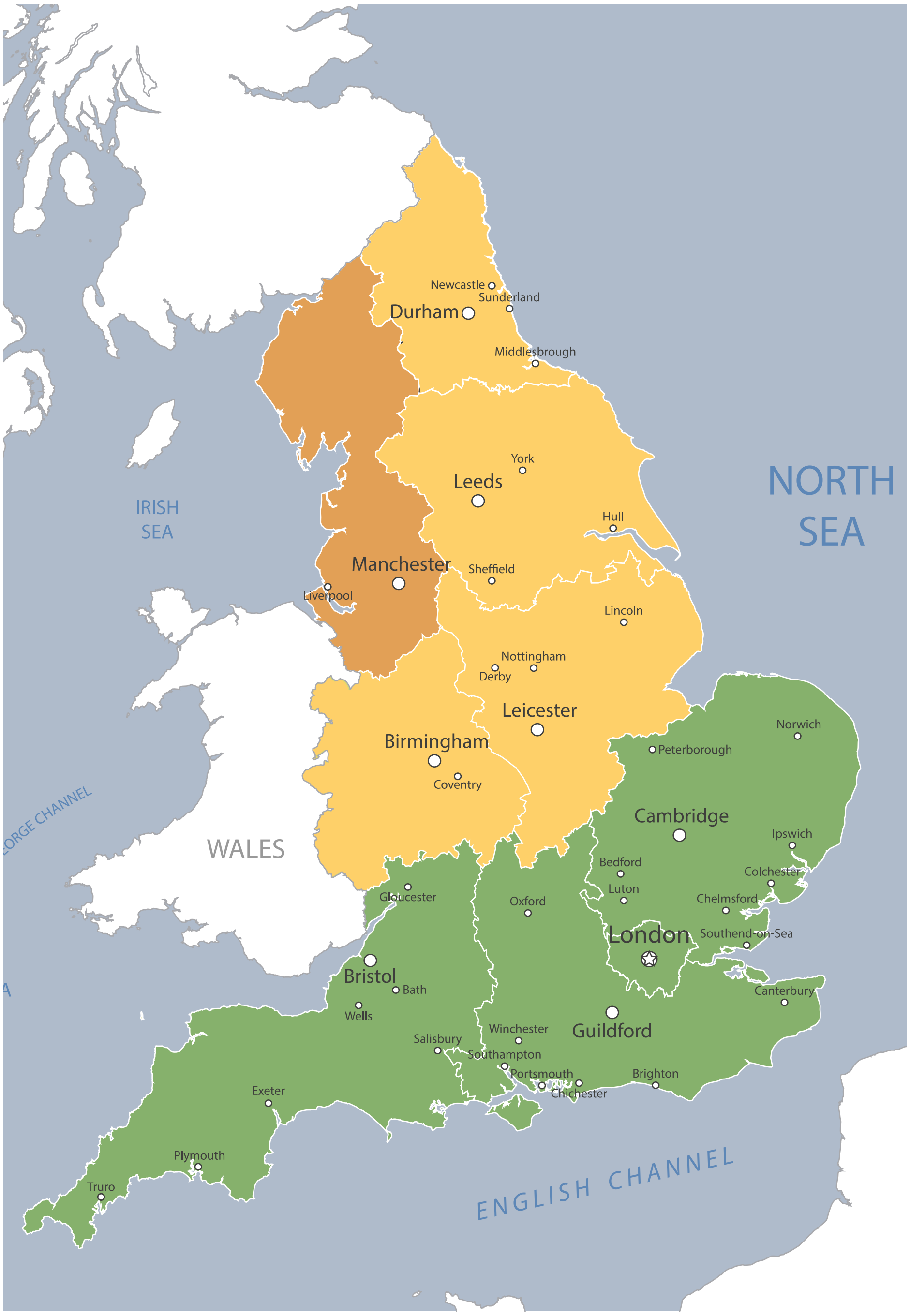
JLL modelled the same as Scenario 4, but removed studios from the mix and re-adjusted to 45% one beds, 45% two beds and 10% three beds. By adopting this strategy a total of **721,800 units** or an average of **72,180 units pa** could be purchased.

Map 1: Distribution of Fund Allocations Years 1-5 (Scenario 4)



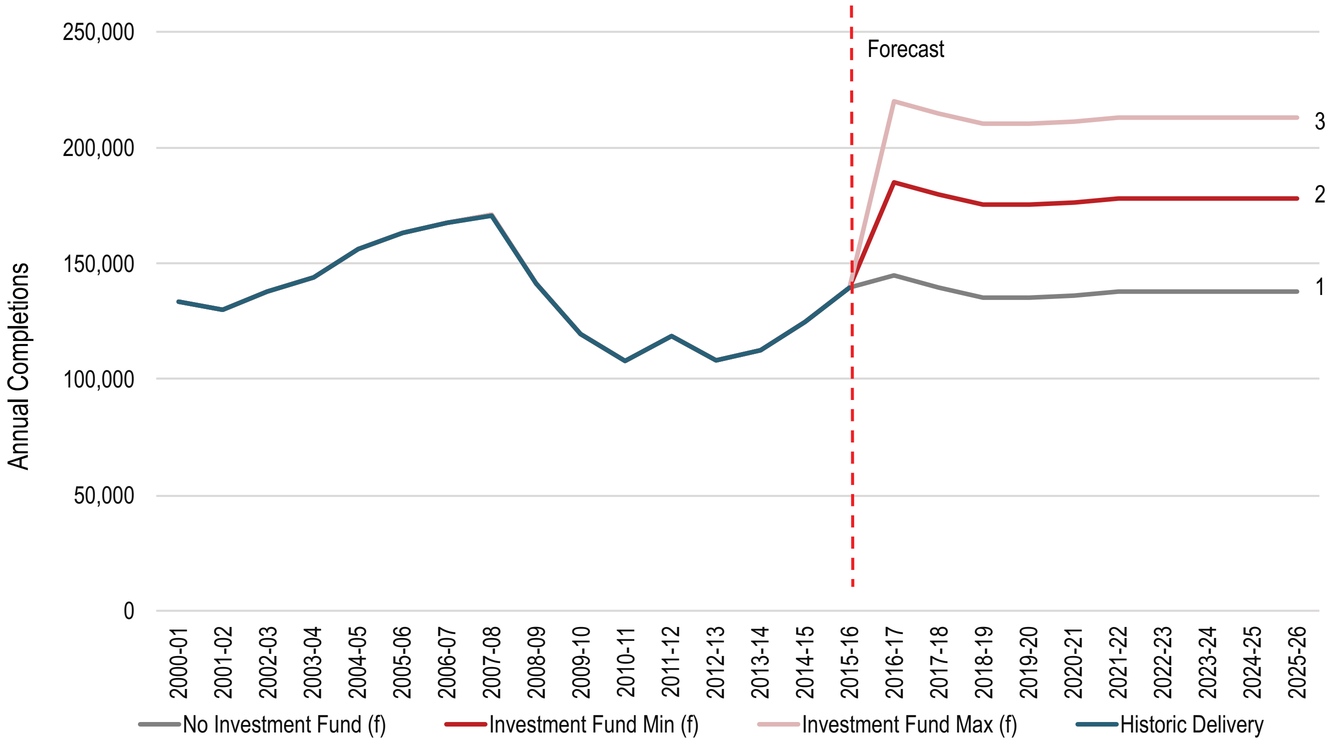
Key – Green 0-5% | Yellow 5-15% | Orange 15-20% | Red 20%+

Map 2: Distribution of Fund Allocations Years 6-10 (Scenario 4)



Key – Green 0-5% | Yellow 5-15% | Orange 15-20% | Red 20%+

Impact of the Fund on Housing Delivery



Source: DCLG, JLL

Figure 5 - Impact of the Fund on housing delivery

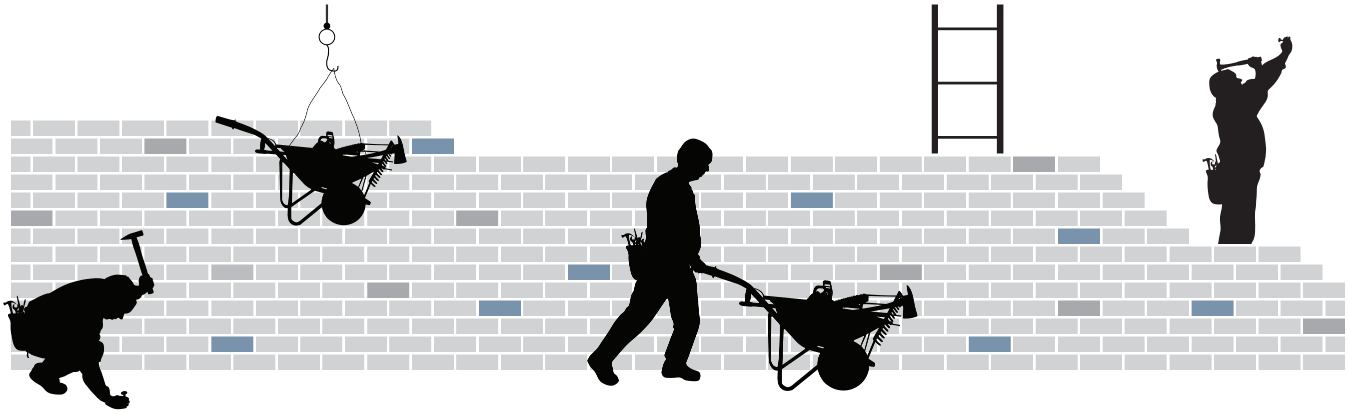
How many additional homes would be delivered?

As we have seen, the proposed Housing Fund has significant potential to deliver new homes. We now consider how many of these would be truly additional units.[10]

In order to understand the potential housing delivery increase as a result of the Fund, the above graph has been created. Line 1 shows a baseline housing delivery forecast for the next 10 years without the introduction of the Housing Fund. This is based upon JLL's annual housing completion forecasts.

Based on JLL's modelling, the realistic maximum additional housing delivery that could be created through the Fund is 75,000 homes per annum, which is illustrated by line 3. The minimum likely additional housing delivery as a result of the Fund is 40,000 homes per annum (line 2).

10 We have taken into account current constraints on capacity, including the planning environment; labour force and delivery rates; housing association ambition and land availability. This are outlined in full in JLL (2016) *National Housing Fund: An assessment of the proposed fund's potential to increase housing supply in England* [November 2016].



4. Why other approaches are not sufficient

"There is widespread support for a major intervention of this kind in the housing market. We believe that the National Housing Fund is the only proposal that addresses the problem of pace and scale of delivery over the long-term."

There have been a number of suggestions on how to intervene in the housing market to increase supply. Below, we examine several recent and older ideas, including proposals to invest in housebuilding at the scale we are recommending. What we find is that there is widespread support for a major intervention in the housing market. Many of these overlap with our proposals – for example, Shelter's suggestion for a Growing Britain Fund that would support housing association development alongside large-scale projects such as garden cities.

What our analysis reveals is that these ideas have merit but would not address the problem of pace and scale of delivery over the long-term. In addition, some would require legislation that would delay implementation, lack in detail, or have failed to articulate how they would spread ownership directly. Our proposal does, and crucially we have mapped the wider economic impact and benefit to the public purse of it.

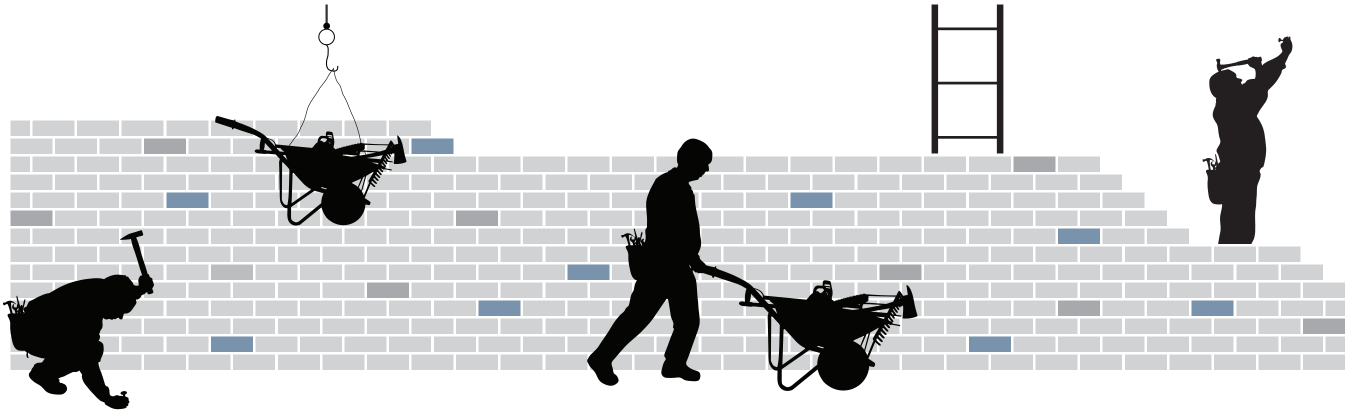
Our analysis shows that the most comprehensive alternative proposal would see housing association building rates boosted at a lower cost to the public purse. Instead, housing associations would be supported through large-scale deregulation. However, this would risk damaging the important social aspect of housing associations as it would risk removing the wider role that registered providers play in their communities and in their tenants' lives. Our proposal avoids this dilemma, whilst setting out a path for a returnable investment that would bolster public finances over the long term.

In the table below, we look at a range of other proposals for boosting housing supply. This details how these proposals compare to our own, with green indicating where they at least match up to our proposal and red indicating where they fall short.

Table 1 - Comparative analysis of other proposals

Name	Funded by	Funding to	Funding amount	Requires legislation?	Returnable?	Timescale
National Housing Fund	50 year gilts	Housing associations	£100 billion	No	Yes	10 years
Home Building Fund (Government)	Not specified	Private sector business, focus on small builders	£3 billion	No	Yes	One-off fund running until 2021
Growing Britain Fund (Shelter)	10 year gilts	Not modelled, but would include housing associations, large scale projects such as new towns, cities, direct commissioning	Not specified	No	Yes	2020
Homes for All (Renewal)	Not specified, but government grant and institutional investors suggested	Not modelled, but would include housing associations, investors, city regions	Not modelled	No	Not modelled	Not specified
Better Financing, More Homes (Policy Exchange)	Government through Help to Buy extension; deregulation to allow HAs to raise own funds	Housing associations	Not specified	Yes	Not applicable	Not specified
Housing People, Financing Housing (Natalie Elphicke & Policy Exchange)	Housing associations raise funding through equitisation to raise funding from e.g. pension funds	Housing associations	£30 billion	Yes	Not applicable	5 years
Stephen Crabb and Sajid Javid (Pledge during Conservative leadership campaign)	Government bonds	Not modelled	£100 billion	No	Yes	5 years

Builds capacity of SME developers?	Build to rent	Security of tenure	Ownership model	Economic benefit	Gain to public finances	Number of houses annually	Number of additional homes to 2027
Yes	Yes	Yes - 5 years	Yes	0.4% GDP	£2.4 billion	60,000-90,000	At least 400,000
Yes but only in the short-term	Not specified	Not specified	Not specified	Not modelled	Not modelled	Annual figure not set	Up to 25,000
Direct impact not specified	Yes	Not specified	No specific model	Yes but not modelled	Yes but not modelled	No specific estimate	No specific estimate
Direct impact not specified	Yes	Yes - 5-10 years	Yes	Not modelled	Not modelled	Annual figure not set	Not specified, but 75,000 set as the aim
Direct impact not specified	Yes	Not specified	No	Not modelled	£275 million per annum	Potentially 100,000 per year	Not modelled – requires legislation
Direct impact not specified	Yes	Not specified	No	Yes but not modelled	Yes but not modelled	Potentially 100,000 per year	Not modelled – requires legislation
Direct impact not specified	Not specified	Not specified	Not specified	Not specified	Not specified	Not specified	Not specified



Conclusion

"Our National Housing Fund offers the British Government a way to finally build the homes it acknowledges it needs. Through the notion of a guaranteed buyer, we reinvent the only formula that has ever enabled the state to build at scale. Crucially, we will open up the market for the millions who need it to work for them."

We are building less than half the number of houses needed to meet both population growth and tackle the backlog caused by decades of undersupply; 1.4 million families sit on social housing waiting lists; private rents have hit a record high and the average home costs 10 times the average salary.

This failure to meet demand is pricing people out of the housing market, increasing intergenerational inequality and for those for whom renting is the only option, a record proportion of their income is spent on housing.

Our National Housing Fund offers the British Government a way to finally build the homes it acknowledges it needs. The Fund we propose will offer full cost recovery for the public purse, or indeed if the Government prefers it could even offer a direct return over and above any interest or management costs. Through the notion of a guaranteed buyer, we reinvent the only formula that has ever enabled the state to build at scale. Crucially, we will dramatically expand the capacity of two relatively dormant sectors, the SME building market and housing associations, such that they too can build at scale and open up the market for the millions who need it to work for them. Finally, we believe that over 50 years each round of the fund will create a massive endowment that can be used to help address not just the housing challenge in the country but potentially the myriad range of other disadvantages that can hold our fellow citizens back.

A One Nation Government that is radical and ambitious has no choice but to transform the housing market and finally get it to provide the homes so urgently needed. Our National Housing Fund represents a serious and credible way to achieve this goal by establishing a new guaranteed buyer in the housing market – to deliver at least 40,000 and up to 75,000 new homes a year to finally meet our housing needs.

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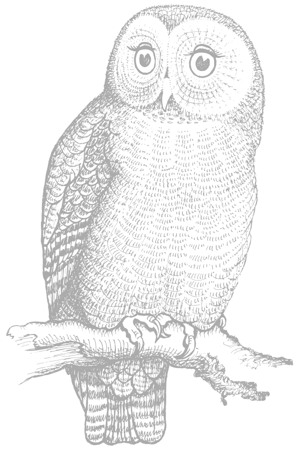

Prosperity

The UK has some of the highest levels of wealth concentration in the developed world. It has an economy where most mature markets are dominated by a small number of players and the barriers to entry are far too high. It is not an exaggeration to suggest that in many areas, from energy to banking to groceries, the UK has a monopolistic rentier rather than a market economy – a system in which certain individuals or small groups gain market dominance and excessive returns through anti-competitive practices. This conspires against innovation and is detrimental to the small and emergent businesses that generate growth and spread prosperity. Added to this, our education system, by specialising too early and often in the wrong areas, fails to produce students with fully rounded skill-sets. We are simply not equipping our future workforce with the means to safeguard our, and their, economic future. This is one reason why the real value of wages in proportion to growth in GDP continues to stagnate or fall. Our long-term productivity dilemma is a function of market capture and the effective de-skilling of the population.

We believe that shared prosperity cannot be achieved by simply tweaking the market. Britain needs significant demand and supply-side transformation, with new visionary institutions re-ordering our economy. We need long-term solutions that give power over wealth and assets, not simply handouts, to ordinary people. Central to this process of economic empowerment is an ethical, practical and adaptable education that gives people the skills to build their own businesses, or develop their own talents, rather than a conveyor belt to a service industry of low wage and less return.

New financial institutions to promote small business lending are required, and this involves smaller, more specialised and decentralised banks that can deliver advice as well as capital. We wish to explore ways in which all financial transactions can be linked to a wider social purpose and profit, which itself needs a transformation of the legal framework within which economic transactions take place. We believe that the future lies in the shaping of a genuinely social market which would be in consequence a genuinely free and open market. Internalising externalities and creating a level economic playing field in terms of tax paid and monopolies recognised and challenged, remains beyond the scope of contemporary governments to deliver. Such a vision requires new concepts. The viable transformative solutions lie beyond the purview of the current visions of both left and right in the UK.

Prosperity *Prosperity* *Prosperity*

The Government has set itself a target to build one million homes over this Parliament to meet our severe housing needs. But over the last 35 years or so just under 150,000 new homes have been built on average each year in England.

What can change this?

In this report, we set out what we believe is the answer – a National Housing Fund that could make the housing market work for the many and deliver at scale over the long-term. Based on analysis by JLL, we show how this approach could deliver a minimum of 40,000 and up to 75,000 new homes a year to finally meet our housing needs.

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