Housing in London
Addressing the supply crisis
HEIF 5

Looking ahead: how should the new government address London's housing supply crisis?

Briefing Paper

Since the project launched in September, *Housing in London: Addressing the Supply Crisis* has explored key barriers to increasing housing supply through workshops, site visits and events around four main themes: New Housing and the London Plan, Improving Private Renting, Alternative Housing and the Role of Foreign Money. The objective of the project was to improve the debate around London's housing supply crisis leading up to the national election and to identify not only barriers but recommendations for overcoming barriers to accelerating development. This short briefing paper offers a first look at the key policy recommendations that have emerged from the knowledge exchange over the last nine months.

Overall, the project has revealed various barriers relating to *institutional challenges, procedural challenges* and *fundamentals*. Different strategies and instruments for addressing these barriers have emerged from discussions on the project thus far—related to both policy and practice—which we have summarised here:

Challenges	Main Barriers	Proposed Solutions
Institutional	• Staff and resource shortages in planning departments • Lack of institutional memory within Local Authorities • Limited partnership-working between boroughs	• Increase cross-borough networking, particularly around strategies for alternative housing • Redefine the role of the GLA—providing templates to support partnerships and resources for over-stretched departments
Procedural	• Uncertainty in the planning system • Dysfunctional viability procedures • Difficulties in land assembly and complex land ownership	• Clarify and modify CPO powers and procedures • Introduce more transparent and consistent targets for affordable housing and infrastructure—move towards tariffs and away from negotiation
Fundamentals	• High land values • Density is too low • Land supply constraints • Finance	• Introduce more Housing Zones • Develop the London Land Commission • Establish more revolving infrastructure funds • Expand Builders Finance Fund

Each of the following sections presents the key issues, barriers and recommendations relating to our four project themes. More detailed information about each theme and multi-media outputs from the project (including blogs, videos, podcasts, and an interactive map) can be found on our project website, www.lselondonhousing.org.

Looking ahead, our hope is to build from the lessons learned this year in terms of national government policy as we turn our attention towards the 2016 Mayoral race. We hope you will join us at our next event in September (exact date TBC) at which we will begin looking at the key questions and issues related to housing supply and accelerating development facing London's municipal government.

The Issues – *Constrained land supply; difficulties of assembling sites for development; and costly, extensive negotiation processes*

NEW HOUSING AND THE LONDON PLAN

It is evident both from our project thus far and from other reports about the housing crisis that there is little desire or need for major reform of the planning system. Nevertheless, we have found from discussions with planners, developers and other key stakeholders that there are some concrete changes related to planning that could accelerate the production of new housing supply. In general, it is clear that local authorities should play more of an enabling, driving role in the development of new housing, which should include a) actively making more land available for development, b) improving clarity and transparency, c) providing leadership which incentivises and encourages developers and other actors to work together (particularly by identifying strategic growth areas such as Housing Zones), and d) introducing financial mechanisms at the local authority level which can fund new development. However, due to increasing measures of austerity, it is increasingly difficult for councils to provide these services effectively.

One area these changes must address is the 'artificial scarcity of land' as it is described in the Lyons Review. There are a variety of suggestions related to the fact that land is constrained due to greenbelt and historic conservation regulation. For authors like Cheshire the reasonable thing to do is to strategically release greenbelt land and presumably relax planning regulations in London around sightlines and conservation more generally to produce taller buildings. Reviewing greenbelt regulations within reason and in a carefully managed way appears on balance a very reasonable measure, albeit a politically contentious one.

The second strain to the land arguments centres on the issue of land banking. Here things like Housing Zones show real promise, areas in which local authorities identify and assemble brownfield land, minimise or eliminate planning restrictions within the area and forge partnerships with developers and housing businesses to deliver substantial volumes of units. The key here is helping to facilitate land assembly and then bring development forward. Modification/clarification around CPO is a big part of this. There seems to be some real reticence to use CPO, even when justified, due to questions around its legalities. The compensation rules for CPOs for large scale sites should be reformed to ensure that landowners are offered a generous benefit from the sale of the land while ensuring that the uplift in land value as a result of planning and development can be captured to fund the infrastructure required.

Site Visit - Ailsa Street, Tower Hamlet

Related to this issue of land availability, there is a need for more clarity and transparency concerning public sector land holdings and the status of land in the planning pipeline. We view the London Land Commission, which will help to identify public sector brownfield land, as a potentially positive step in the land supply equation. In addition, we could envisage a system that showed land price data and ownership (including options) as a good mechanism for bringing more SME's into the game, as better information would be available to them. However, given the track record with previous large IT data information projects clearly there could be major obstacles to be overcome.

Perhaps one of the most important planning concerns centres on viability/affordable housing targets. There is a lot of consternation out there on both sides (planners and developers) about how hard it is to navigate the planning system when the rules (affordability targets, density, etc.) are seen as negotiable elements of planning. This leads to people basing their bid price for land on an assumption that they can get more out of planning than the rules might allow – thus driving up price. A transparent set of numbers (affordable units/density) that were fixed would probably aid considerably here. However, the setting of these numbers would be very hard. One of the Lyons Review's key recommendations was that guidance should be produced to 'ensure a single and robust methodology for viability assessment to reduce the scope for different interpretations of viability and reduce uncertainty' (Lyons, 2014: 76), which seems like a sensible strategy for progress on this issue.

Finally, authorities could play a larger role in financing new construction by establishing revolving infrastructure funds. Because of soon-to-be-implemented changes to the governance of local pension funds, members could soon have the chance to challenge pension funds to invest a modest proportion of their potential investment in residential property. The Elphicke review argues that an investment of 3% could lever in up to £5 billion investment for housing (Elphicke, 2015: 44). Revolving infrastructure funds specifically offer a way of pooling central and local funding to target priorities in a contextually sensitive way and allow for the initial outlay to be recouped over time. Our discussions with local authorities like Croydon have already revealed cases where these funds are being used to unlock developable land.

Site Visit - Millbrook Park, Barnet

Key Recommendations:

- **promote more Housing Zones**—areas where local authorities identify and assemble brownfield land, simplify planning restrictions within the area and forge partnerships with developers and housing businesses to deliver substantial volumes of housing units
- **strategically release greenbelt land** within reason and in a carefully managed way
- **clarify and modify CPO powers and procedures,** particularly the right of local authorities to use them if needed to assemble land for Housing Zone-type development; reform the compensation rules for CPOs for large scale sites to ensure that landowners are offered a generous return from the sale of the land while ensuring that the uplift in land value as a result of planning and development can be captured to fund the infrastructure required
- **examine the possibility of setting transparent and consistent targets** for affordable housing and local infrastructure that are fixed to reduce the costs and time of extensive negotiations between planning departments and developers

The Issues: *No stock of dedicated private rental units; development of purpose-designed long term PRS requires scale, expertise and long-term investment model; PRS-only blocks could accelerate development on large sites but a tenure-neutral planning system and greater profitability in the owner-occupied sector mean developers build for home ownership and buy-to-let instead.*

IMPROVING PRIVATE RENTING

The following concentrates on enhancing the contribution of the PRS to new supply, rather than on affordability or security of tenure in the existing stock.

Potential role of PRS in new supply

Most new residential development in London is carried out by a small number of large house builders. These developers follow a tested model of 'drip feeding' new housing onto the market, rather than releasing large chunks of stock at the same time. This is for three reasons: it helps cash flow (because income from the sale of early units helps finance the construction of later ones); it facilitates the sequencing of construction tasks; and it ensures that the market is not flooded with identical units, which would depress prices. Even on sites that will eventually accommodate thousands of homes, development for sale proceeds at a rate of a few hundred units a year at most.

The targeting of some blocks or sections of big sites for PRS use could help accelerate development, as policy makers have recognised. In effect, this would revive the model of large PRS-only blocks last seen in London in the 1930s. This is because PRS blocks and owner-occupied units are essentially two separate markets. Producing entire blocks for sale to large landlords would allow for much faster build rates, would bring in cash, and would not affect sales to owner-occupiers.

However, this is not straightforward. The English planning system makes no distinction between owner-occupied and rented housing--residential development is a single category, and owners of private dwellings are free to occupy them or rent them to others (although they may be required to register as landlords in a minority of local authorities). This means that there is no permanent stock of private rented housing, as any dwelling may switch from one tenure to another at any time. On the other hand, it also means there is nothing to stop developers from producing tranches of housing specifically for the PRS.

Site Visit - East Village, Stratford

Why aren't they doing so already, if PRS has such evident benefits? There are two main reasons. First, bulk lots of PRS housing sell for less per unit than individual owner-occupied dwellings. This is partly because purchasers expect volume discounts, but more importantly because the amount they will offer is based on projected rental yield, which results in lower prices than owner-occupiers are willing to pay. This means PRS blocks are not as profitable for developers: the price of land (which in London makes up the majority of the cost of a new dwelling) is a function of the most profitable use of that land. If PRS-specific housing is to be an attractive product from the developer's point of view, the cost of land needs to come down.

Second, there is not yet a critical mass of potential buyers for this sort of housing, although pioneers have started to emerge (e.g. QDD at East Village, Genesis and M&G at Stratford Halo). While developers can retain ownership and act as landlords themselves, and a few have indeed done so, most would prefer to sell in order to generate income.

Fizzy Living Development

What could be done?

There are already several initiatives designed to stimulate new dedicated PRS construction. These include the government's Build to Rent fund and the Mayor's Housing Zones, where the planning system may be used to support PRS in return for a commitment that the housing will remain in tenure for a defined period. These are positive steps and we would support in particular the extension of the covenanted PRS model, as long as this does not involve reductions in the amount of affordable housing achieved.

Key Recommendations:

- **Encourage greater involvement of large landowners, especially from the public sector.** Given current relative returns and funding constraints, making private renting stack up often requires a land owner who is prepared to take an equity stake and/or is willing to defer receipt of payment until after the development is complete. This might be a public-sector owner such as a local authority or NHS trust; equally it might be a major private-sector employer. An equity stake, which could include deferred payment for land, is one way of addressing the requirement that local authority assets be sold into the 'highest and best use', and could in principle be combined with a covenant. Even if the 'highest and best use' requirement is met, a public owner will only allow land to be used for new private rented housing if it accepts that private renting is a necessary and desirable element in local housing provision, which should be reflected in clear identification in local needs assessments.
- **Looking ahead to the Mayoral race, encourage new GLA leadership to immediately make clear its approach to regulation of the private rented sector, and produce any specific proposals, and legislation, as quickly as possible.** There is increasing debate about the desirability of introducing some kind of regulation of rent increases and/or security of tenancy (in particular the Labour party proposals in the run-up to the general election). Many of the institutions that have invested in large-scale PRS are international, with long experience of valuing and managing rental property at scale elsewhere. They often operate in countries where such rent regulation is much more stringent than in the UK, so they are familiar with these systems and accustomed to operating under them. But their investment decisions will be affected by uncertainty about the degree and nature of regulation. Uncertainty means investors cannot accurately forecast returns, so will require much higher yields. Higher yields mean lower prices—reducing or removing any incentive for developers to build this sort of housing. Prolonged uncertainty about the regulatory approach to the PRS will stifle construction of and investment in new PRS housing and reduce its contribution to London's housing supply.

The Issues – *High cost and lack of available land for alternative housing; limited finance available for non-traditional developers; lack of local authority knowledge about the viability, opportunity and support needs of alternative models*

There is a growing tendency to develop alternative housing models in London. Despite the variety of existing schemes across the capital, their 'niche' status means they face similar issues that need to be addressed if they are to move more firmly into the traditional housing market.

Barriers identified

Site Visit - Walter's Way, Forest Hill

Land: The high cost of land in London makes the scaling up of any kind of alternative housing-- whether experimental lifestyle choices motivated by a collaborative ethos, or material and technological innovations that can improve the form, its quality or future sustainability-- extremely difficult. The following is a list of the potential ways to address this key impasse: (a) engage landowners interested in social as well as financial returns (e.g., churches, LAs and HAs); (b) incorporate the communal, neighbourhood and other values of alternative schemes into traditional financial valuations of public land, and think of ways to involve lay people and future residents; (c) support existing ideas like the identification and setting aside of land in central and outer London, garden cities and Homes Zones for community self-build initiatives; as well as releasing of land through Community Land Auctions.

Finance: London's land constraints make the financing of alternative housing schemes difficult and costly, particularly for non-traditional developers. The decline of small and medium size builders exacerbates this situation. Suggested ways to deal with this are to: (a) use local authority revolving funds; (b) encourage LAs to set up mechanisms that channels private funds into infrastructure and development, enabling them to free up land faster; (c) intensify density to reduce per-unit development costs; (d) make serviced self-build plots on council-owned land available; (e) modify rules to make mortgages for alternative developments of different kinds easier to access; and (f) change mono-functional planning and land-use classification system, which requires (for taxation purposes) a distinction between live *and* work.

Y:Cube Prototype

Knowledge: To get politicians on board as well as to shift people's views of what is possible, knowledge about the process of designing and producing innovative housing has to be spread within and across LAs and to a wider consumer and local enabler/regulator base. This may involve: (a) building mechanisms for institutional memory, including local publicly available databases of relevant information; (b) setting up a cross-London forum of exchange that allows for networks to develop and information to be exchanged, increasing future opportunities and speed; (c) encourage LAs to play a more active role in promoting alternative developments and (d) provide supporting tools for groups to be more commercially-minded and competitive; (e) draw and build on individuals, groups and communities with experience of successful development of alternative housing forms (including the importance of including long-term affordability and robust social infrastructure into design) and find ways to pass on their knowledge.

Key Recommendations

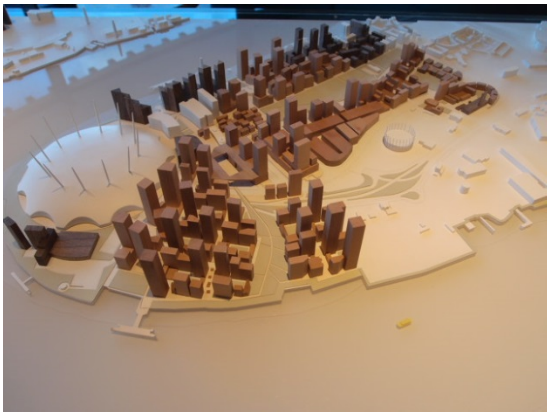
- **encourage more land to be made available for alternative housing development by:** engaging landowners interested in social as well as financial returns (e.g. churches, Local Authorities and Housing Associations);
- **set aside land for alternative housing forms within Housing Zones and large-scale masterplans** and encourage Local Authorities to establish funding mechanisms (like Revolving Infrastructure Funds) which channel private funds into infrastructure and investment, enabling more land to be brought forward more quickly.
- **foster avenues of London-wide knowledge exchange: (**a) within and between local authorities on how best to support alternative housing development, and (b) between community groups and other relevant specialist stakeholders to improve skills and find capital.
- **lobby government to incorporate other values of alternative schemes into traditional financial valuations of public land** to make these projects more viable everywhere, including London.

The Issues – *Although international money directly finances many of the large-scale developments in London and through presales helping to get others underway, it is seen as increasing house prices, excluding local purchasers and building only for the rich.*

THE ROLE OF FOREIGN MONEY

International money is politically toxic - yet it is helping to accelerate large new developments in London which include a variety of market and affordable housing. It kept the central London market moving in the post crisis era and is prepared to put in equity which is looking for longer term returns - a very different model from the traditional debt financing pro-cyclical UK approach to development observed in the past. All of this is good.

The results of the election mean that the environment for development has generally become more stable. Overall there are a range of good examples of the use of international money, and skills, in partnership with UK providers and intermediaries. The main concerns are not with respect to supply but with the (often overstated) impact of foreign demand on the types of units being built and on the possibility of units being purchased being left vacant. Many of these concerns are closely related to issues around mortgage availability for off plan sales.



Greenwich Peninsula Model

Much of the demand from international buyers is for new apartment buildings of the sort which are now being developed so the match between building and demand is very close - making as it feel like a separate market place from which locals are being excluded. Yet the main demands are as permanent residences or for buy to let properties which are then rented out in the general market. The problem that it is filling a gap in London world city but not obviously impacting directly on the overall shortage issue (especially given continued in-migration)?

The most important positive aspects are: it brings in new equity from people prepared to take a longer view (not just QDD style where the money comes in purchase after development but also equity funding for development. This can bring with it new management skills which help build the new style large developments where delivery is speeded up. Can these benefits be transferred to other more mainstream types of development especially outside central London?

Ideally London also wants to attract more traditional types of international finance like pension funds which are looking for private renting - but again this will normally be at the upper end of the scale and could, if we are not careful, directly reduce the amount of affordable housing that will be provided.

International money is also looking for certainty - about regulation, about the tax regime and about how local authorities treat them - in other words they would probably not mind a longer lease term with rents indexed within that term (as long as it is clear how bad tenants are removed) - as long as it was absolutely clear what the terms and conditions were. They clearly do not want incremental changes in tax apparently directed at them because of political pressure. They would like tariffs rather than negotiation with respect to affordable housing and local infrastructure. Many of these 'requests' would also be made by domestic institutional funders as well as developers.

International money is only a part of the answer - and the outcomes need clearly to be seen to be additional and not wasted through vacancy. So we need evidence on vacancies; evidence on additional funding for development itself; evidence on speeding up development on particular sites; evidence on different patterns of returns required; and evidence on how it can help bring in and interrelate with more traditional forms of funding to accelerate the whole range of development opportunities.

International money is currently a requirement for developing large sites – and can play a core role in making the step change to sustaining much higher output levels. But into the longer term, domestic demand and domestic money are also absolutely necessary to ensure high and stable levels of housing investment.

Even though international money is not directly aimed at addressing the affordability problem, if it can provide significant **additional** finance, **additional** skills and most importantly **additional** housing -and it appears that it can – it has an important and continuing role in providing more homes for Londoners.

East Village, Stratford

Key Recommendations:

- **international money is to be welcomed *if* it adds to the stock and encourages more efficient production methods and management -** so need to improve the evidence base on the impact of international money on speeding up development
- **encourage stability in the planning and regulatory regimes -** not political fiddling for the sake of it
- **clarify the position on rent/security regulation as soon as possible after the election**
- **support the GLA and local authorities** in local master planning and partnership approaches)
- **support interaction with Housing Associations** to develop mixed tenure schemes

For more information, please visit www.lselondonhousing.org
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