Countrywide
integrated solutions local expertise

HAMPTONS INTERNATIONAL

Lambert Smith Hampton

Tonic for tomorrow:
proposals for a healthier UK property market

Foreword

In this document the research teams from Hamptons International, Countrywide and Lambert Smith Hampton have worked together to identify the key trends we believe will be drivers of change in the property market in future years. We've highlighted the areas where we believe a policy response or tax change is required to ensure flexibility, fairness and certainty in the property market.

The document is presented as a Green Paper to share our current thinking on how to improve the working of the property market. Some of our proposals are statements of support of ideas put forward by other organisations and others new proposals. We intend for it to stimulate debate. We will be canvassing opinion from our clients, trade bodies and stakeholders, looking for challenge to our assertions, identifying areas that warrant further attention and refinement from what is presented in this paper.

We hope that the debate will serve to further our understanding of the drivers behind structural changes in the property market and lead to effective recommendations for policy responses. If you wish to share your thoughts on the content of this document, or comment on proposals put forward we would be very grateful if you were to share by emailing **research@hamptons-int.com**.

Shifting bases

P2 Growing population and changing households

Household size has been dropping and number of households increasing for the last fifty years.

Single person households doubled between 1961 and 2014.

2012 saw the largest new babies born for 20 years.

P4 Affordability constraints and barriers to homeownership

Most measures of affordability have deteriorated over the last few decades, particularly for first time buyers.

Rising costs of living have affected the ability of households to buy their home.

P5 Shifting tenures

421,000 more households in the private rented sector between 2014 and 2013.

But eighty per cent of renters still aspire to own their own home.

1 in 4 private tenants are now in receipt of housing benefit.

P6 Growing cities

Not since the 1970s have so many people lived in cities, and numbers are growing – since 2001 their populations have risen 10%.

47% of people aged between 20 and 30 now live in a city.

By 2018 50% of people between 20 and 30 could live in a city.

P7 Technology: How we live, work and shop

Over 80% of firms now allow remote working, up from less than half in 2007.

13% of all UK retail sales were made online in 2014 and by 2020 this could rise to 20%.

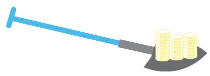
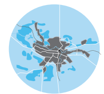
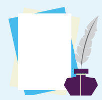
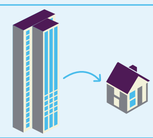
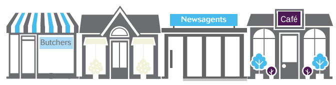
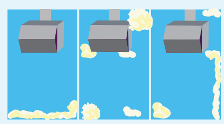
In 1981 there were an equal number of manufacturing and service based jobs. Today service based jobs outnumber manufacturing jobs by five to one.

Tonics for Tomorrow

Proposals for a fairer, more flexible and predictable housing market

The UK economy and its housing and property markets have come through a deep recession and are now recovering. But that recession disguised some underlying changes in the market which are structural rather than cyclical. Understanding these structural shifts is the first step to understanding the policy and industry changes required to move to a more efficient market that helps provide the right solutions to the property needs of the country. This document identifies the key structural drivers of change in the residential and commercial property markets, and then presents proposals for policy responses to adapt to these changes. The document has been written as a Green Paper, to stimulate debate on how the property market will change in future years and what the best policy response should be to this change.

Proposals for a Healthier UK Property Market

	Proposal	Picture
Building homes for our changing population	**P10 Boosting the New Homes Bonus** We support the indefinite extension of the New Homes Bonus and doubling or tripling the grant attached to each new home.	
	P12 Redefining Greenbelt for modern needs We support a review of precisely what we call Greenbelt today, with a view to freeing up more land for development.	
Certainty and flexibility in planning	**P13 Giving planners time to catch up with policy** We believe there should be a period of 3-5 years free from reform of the plan led system during which planning documents are brought up to date.	
	P14 A new more permanent permitted development right (PDR) for office to residential We are in favour of developing a new PDR right for office to residential conversions, which is effective for at least 10 years.	
	P14 Helping the high street by widening the retail use classes We support establishing a wider retail use and additional PDR to convert from retail to leisure.	
Fairer taxes	**P15 Reforming business rates** We suggest increasing the frequency of revaluations from five to two years and scrapping annual RPI uplifts. Small businesses should be exempt from business rates and targeted assistance given to the high street.	
	P16 Reforming council tax We propose the addition of a new Band I at the top of the scale, bringing 1991 values up-to-date and merging some of the lower bands.	
Preparing for a growing private rental sector	**P18 Stability and transparency for landlords and tenants** We propose the creation of standard tenancy contracts of six months, one year and three years and a transparent rent uplift mechanism to be built into the longer term contracts.	
	P19 Making build to rent viable We propose that local authorities should be allowed to interpret the best value obligation in land sales in a more flexible way to be able to release land for PRS rather than just owner occupied development.	
	P20 Sharing out shared ownership The shared ownership re-sales market needs to be simplified, opened up and funding made available to build more shared ownership homes.	

Population and households

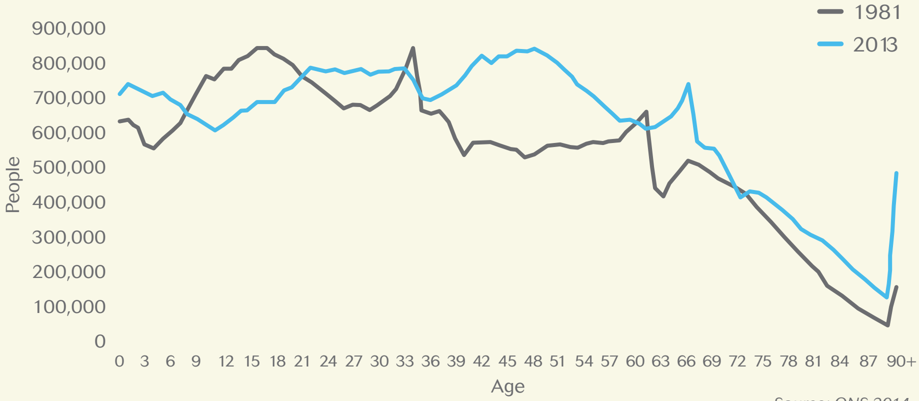
It is well-documented that the population of the UK is aging. The baby boomer generation is now entering retirement and living longer than ever before. In the 32 years between 1981 and 2013, there was a fourfold increase in the number of people aged ninety or older.

At the other end of the age spectrum, the UK has found itself in the midst of a new baby boom since the early 2000s. While there was a small drop in the number of babies born in the immediate aftermath of the 2008 recession, in recent years the number of births has continued to rise. In 2012, the largest number of new babies for twenty years were born.

Despite our ageing population, the UK has a significantly younger population profile than almost every other European country, a product of higher birth rates and inward migration from both Eastern and Western Europe. The interplay between these two factors over the coming decades will serve to shape the future of the UK's housing market.

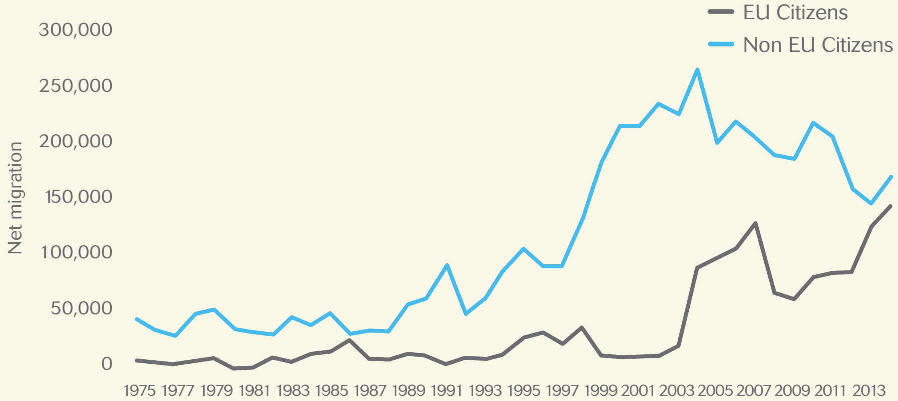
In the short to medium term the strength of the UK's economy will continue to attract migrants from both within and outside the Europe. Between 2010 and 2014 more net new jobs were created in the UK than in the rest of the EU combined. In the medium to long term however, many of the Eastern European countries look set to catch-up. The continued economic development and rapidly rising living standards in some of the EU's newest member states may serve to erode some of the UK's current allure.

The changing age profile of the UK



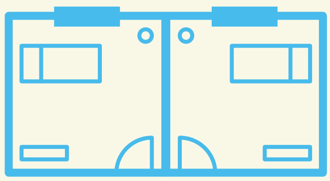
Source: ONS 2014

Components of net migration to the UK



Source: ONS 2015

103%
Growth
in 1 person households
(1961-2014)



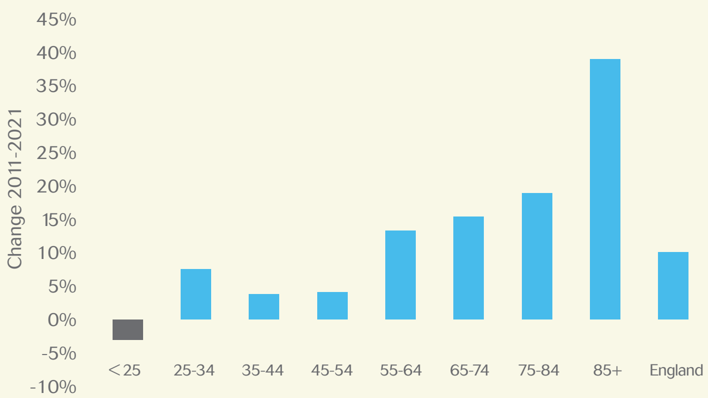
17%
Growth
in 2 person households
(1961-2014)

Growth in population inevitably means more households, which is an important number for planning the supply of housing. Household growth has outstripped expectations – and new housing supply – for decades. But there's more going on than that. Not only are the numbers of households changing, but so too is their composition.

Household size has been dropping and number of households increasing for the last fifty years, due to an increase in the number of one and two person households. This change in size is driven by the ageing population, increasing wealth and higher levels of divorce and separation.

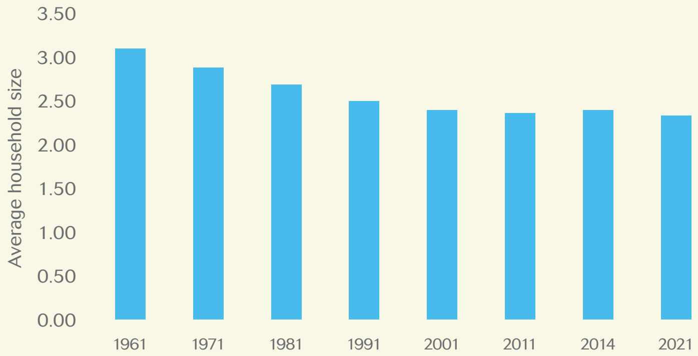
The age breakdown shows the number of households under the age of 25 are falling while older households are projected to grow further. As well as the age structure this is also a likely signal of longer education and older offspring remaining in or returning to the family home for longer. This trend is not expected to change significantly regardless of tenure, since income growth has been so low since the downturn. This also has implications for the turnover of property and moving up and down the property ladder. If children are remaining in the family home for longer, delaying the age of 'empty nesters', then the larger family home will be retained while the grown up children are still resident. The growth in the number of households has been stronger, and is predicted to be more concentrated in London and South East. As with population, higher growth is predicted in urban compared with rural areas as the maps show.

How we're ageing



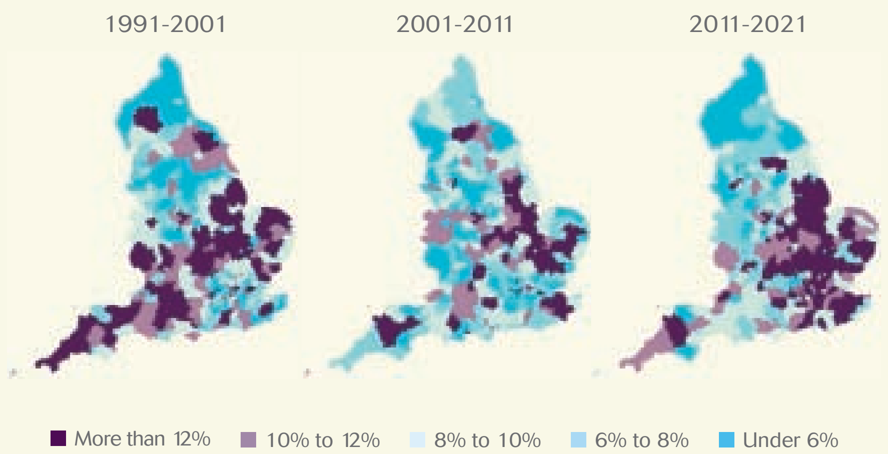
Source: ONS 2014

How our households are shrinking



Source: ONS 2014

Where our population's growing



Affordability

Where and how people live is inevitably driven by what they can afford. Most conventional measures of affordability have deteriorated over the last few decades, particularly so for first time buyers. House price to income ratios across the UK are now close to their historic 2007 peak, while in London new heights have been scaled. Lower interest rates since 2009 have helped to improve affordability – but even comparing mortgage payments to household income shows affordability is stretched. Between 1997 and 2002 house prices grew at an average annual rate of about 8%, but interest rates fell from 7% to 4.6%, keeping affordability broadly stable. This is one reason why house prices were able to continue to rise, despite historically high house price to income ratios.

In addition to high house prices, rising costs of living have affected the ability of households to buy their home. Spending on essentials takes up a significant proportion of income and this means that conditions for buyers haven't improved as much as the mortgage payment to income measure suggests.

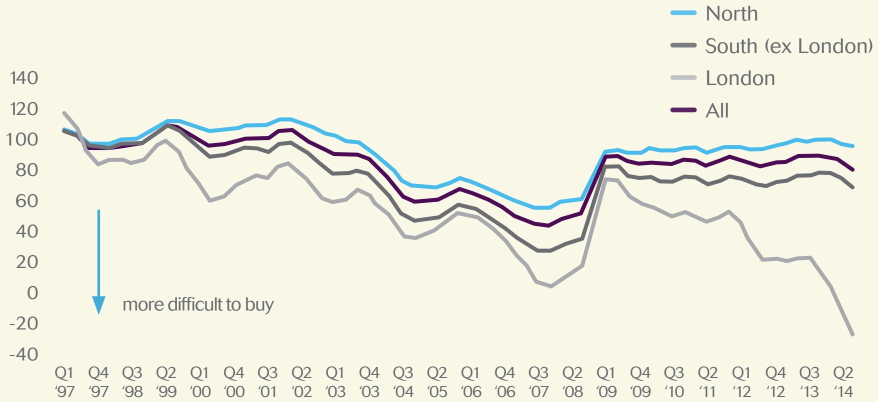
Lower interest rates have come at a price – lower wage growth. The growth in home ownership up to 2007 has only been achieved by higher levels of debt, which, because wage growth is lower, will remain a significant burden for longer.

Higher debt levels make regulators twitchy and the series of measures under the mortgage market review – supplemented by new controls given by the Financial Policy Committee further limit the availability of credit. The collapse in lending after 2008 was in part due to the more risk averse attitude of banks in the financial crisis. Since the introduction of new regulations in the Mortgage Market Review and subsequent additions to the power of the Financial Policy Committee to change rules around acceptable affordability in lending, credit is still limited compared to before the crash.

Overall the story is one that suggests that ownership will become increasingly less affordable unless price growth falls behind wage growth and inflation of essential goods and services. Without a change to housing supply, improvements in affordability look unlikely in the short to medium term.

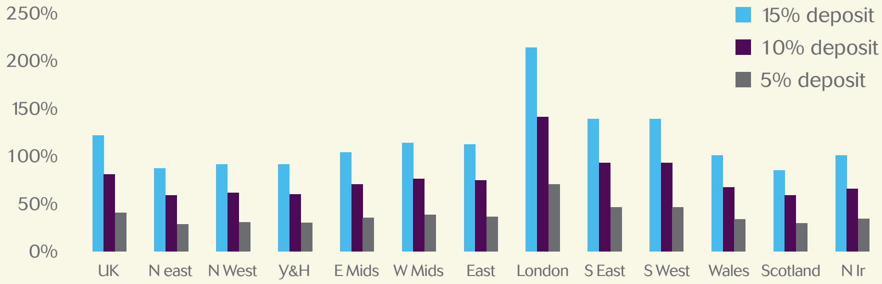
Affordability has deteriorated most in London and South East where ability to buy has fallen to the lowest ever level and, consequently, lenders affordability tests are most difficult to pass. In the rest of the country low interest rates have maintained affordability at about 2003 levels. But even though income may more comfortably cover mortgage payments, this does not take into account the required deposit. Even outside of London and the South East, a 10 per cent deposit takes up more than half of a year's post tax income – and that's before essential spending is taken into account.

The ability of a household to buy (1997 = 100)



Source: Hamptons International Research

The deposit as a proportion of annual post tax income



Source: Hamptons International Research

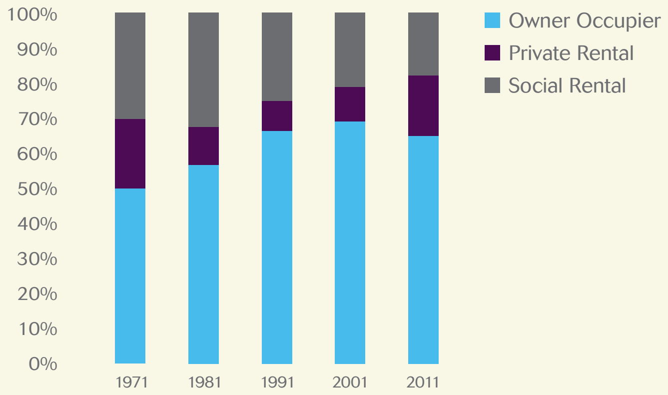
Tenure

We may have become accustomed to the UK being a nation of homeowners, but that is a relatively recent trend. Before the introduction of Right to Buy policy in the 1980s, owner occupation was only around 50% of the stock. The opportunity to buy a home at a significant discount to market value, allowed many households to move from social housing into ownership. The relaxation of lending controls on banks at a similar time meant mortgage finance was more easily available too, allowing movement from the private rented sector (PRS) into ownership. So we shouldn't be so shocked that there is a return to the use of the PRS as an acceptable tenure, even if it is not the first choice of households. 80% still aspire to own their own home, but in reality this is becoming more difficult to achieve.

The PRS is also doing much of the heavy lifting for the social rented sector – albeit supported by housing benefit. One in four private tenants are now in receipt of housing benefit with the number of claimants in the private rented sector rising 50% in the last six years. But as pressure on the total supply of housing grows, there will be increasing affordability issues with rent. That makes finding an intelligent approach to solving the supply problem more urgent from a macroeconomic point of view.

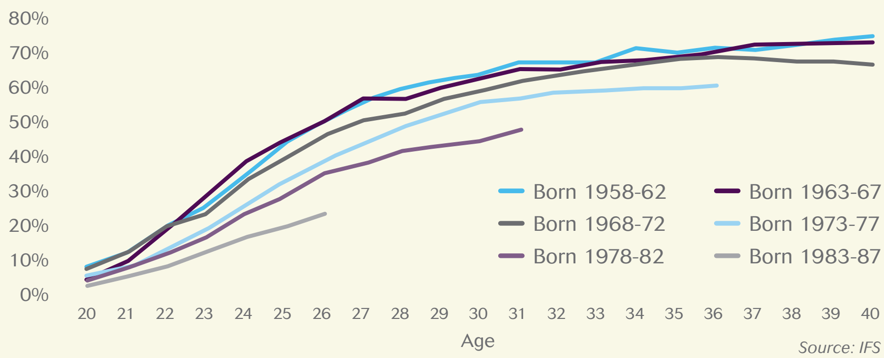
A healthy rented sector is a feature of other wealthy countries. It is a common misconception that the UK has one of the highest owner occupation rates in Europe. In fact it's comparable to the US and relatively low in comparison to the southern European countries such as Spain and Italy.

A high water mark for owner occupation?



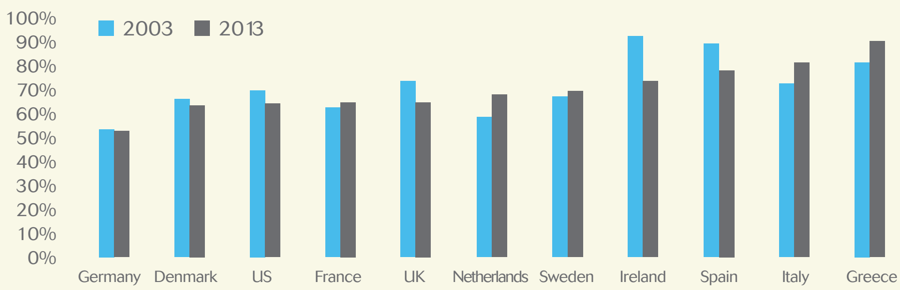
Source: 1971-2011 Census

Homeowners are being created more slowly



Source: IFS

UK Homeownership rates are now inline with the European average



Source: Various

Growing cities

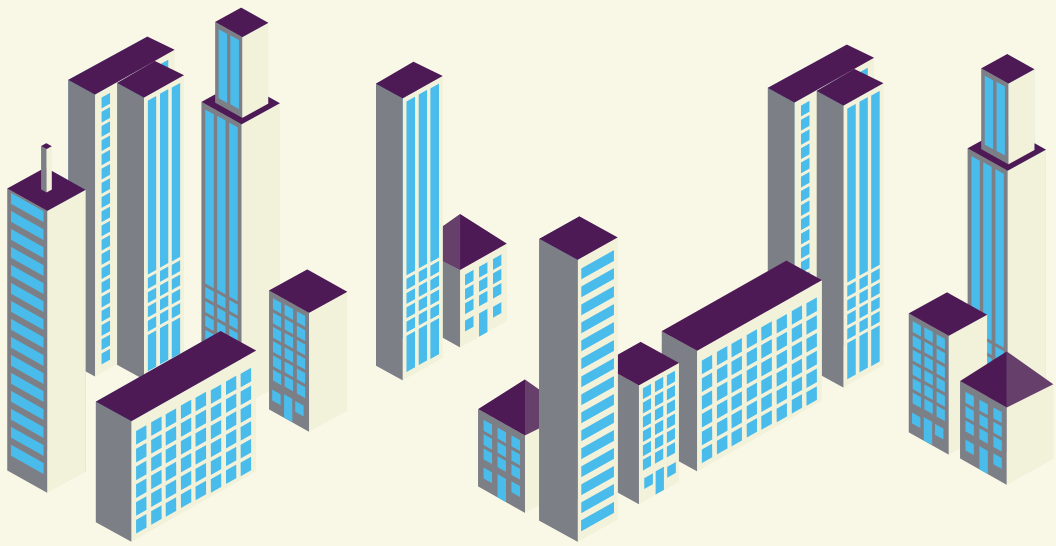
When Labour came to power in 1997, one of its key manifesto pledges was to reverse the fortunes of Britain's ailing cities. The 2001 Census had marked the low water mark in terms of population for most of UK cities. Between 1971 and 2001, Greater Manchester lost over 300,000 people from its population. But this trend has reversed, as it has in much of the Western Hemisphere. A combination of economic growth, tax incentives, local authority planning directions, larger numbers of students, 'city centre first' policies and emphasis on brownfield land has made cities in the UK more attractive. Between 1990 and the peak of the boom in 2007, the proportion of housebuilding which took place in the 10 largest cities grew from 20% to 30%.

Over the course of the last 15 years, the look and feel of British cities has changed dramatically. This has been as much a physical change as it has been a cultural one. For an increasing number of younger (and older) people since 2001, living in a city is now a lifestyle choice. A new generation is growing up who are more likely than their peers to have attended university, call the private rented sector home and marry later in life. Generation Y (those born between early 1980s and early 2000s) is more likely to have grown up in the city and is more likely to stay. While many in the early 1990s predicted that advances in technology and communications would reduce the importance of location, striking the death knell for cities, today the importance of physical proximity should still not be underestimated.

Change in density

Change in people per km^2 2001-2013

"Student numbers have risen 25% since 1997 and they now comprise 20%-30% of the private rented sector in most cities outside London."

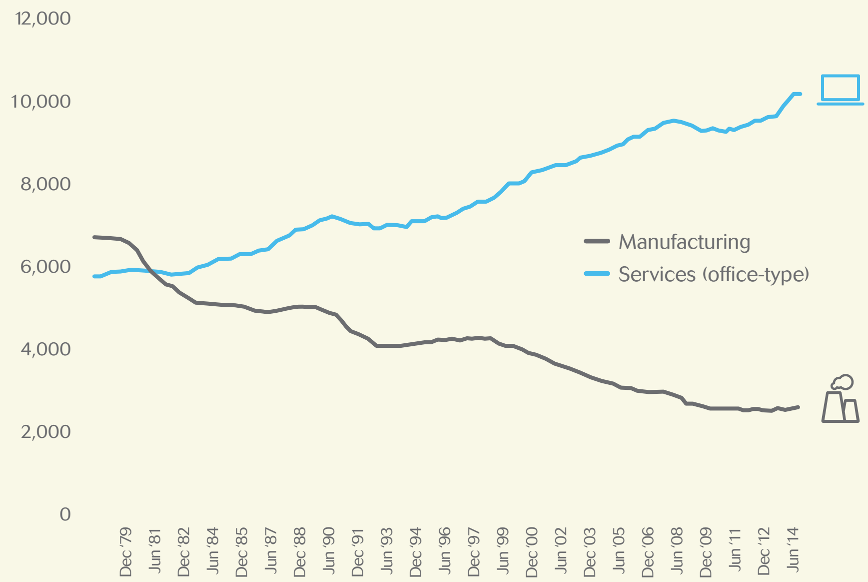


Technology and structural change

Alongside changes in population and household structure, a key driver of change within property markets over the long term has been the invention and adoption of new technologies. In the 21st Century, rapid advances in computing and telecommunications are influencing where, and how, people choose to live and work, and this is having knock-on consequences in the nature of property demand.

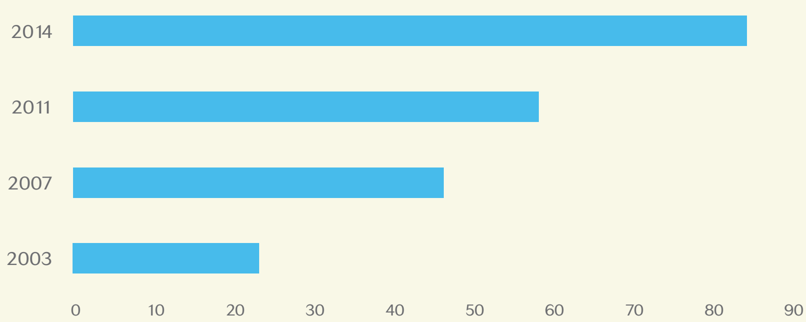
The deindustrialisation of the UK since the 1960s has driven significant change in both the economy and property market. As new technologies afforded greater access to cheaper, global labour markets, the UK's manufacturing industry suffered. This change in manufacturing left the UK with swathes of obsolete property. In tandem, however, the UK's transition towards a knowledge economy saw the level of services employment expand rapidly, reflected by the threefold rise in the amount of office floor space created since the mid-1970s.

The changing face of UK employment (000s jobs)



Source: ONS, LSH

Proportion of firms allowing remote working



Source: CBI employment trends survey

Changing working practices

More recently, continuing technological advances are raising questions over the quantum, form and type of office space that companies require. The rise of 'remote working' has been substantial over the past decade, driven by leaps in telecommunications technology and, increasingly, a drive amongst occupiers to use space more efficiently. With face-to-face contact, however, remaining as important as ever, traditional theories that technology spells the 'death of the office' seem to be misplaced.

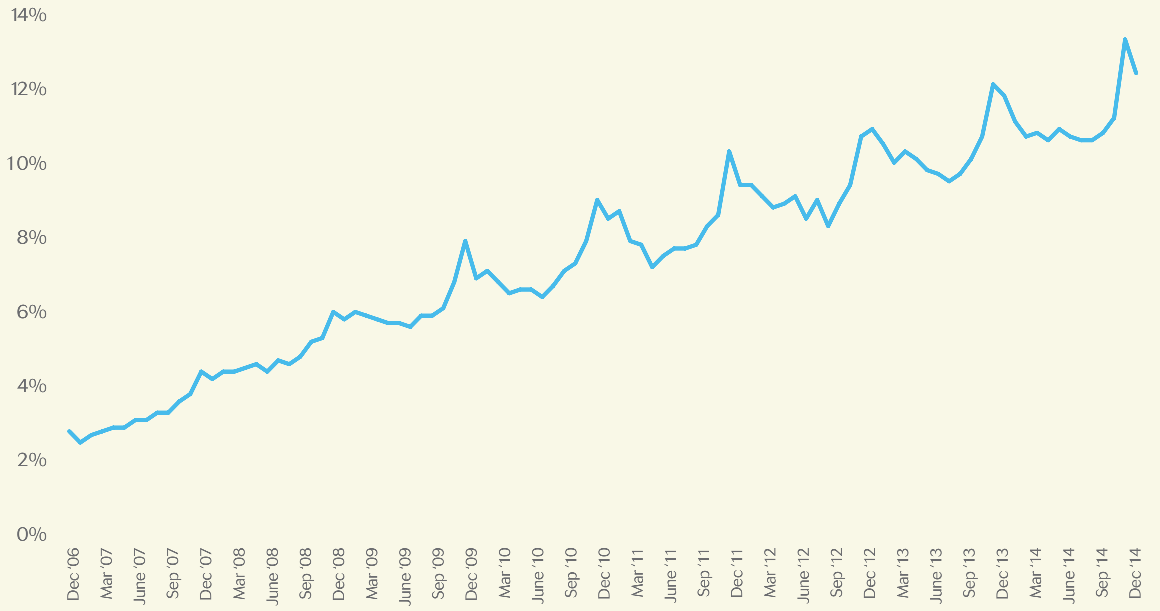
Changing patterns of consumption

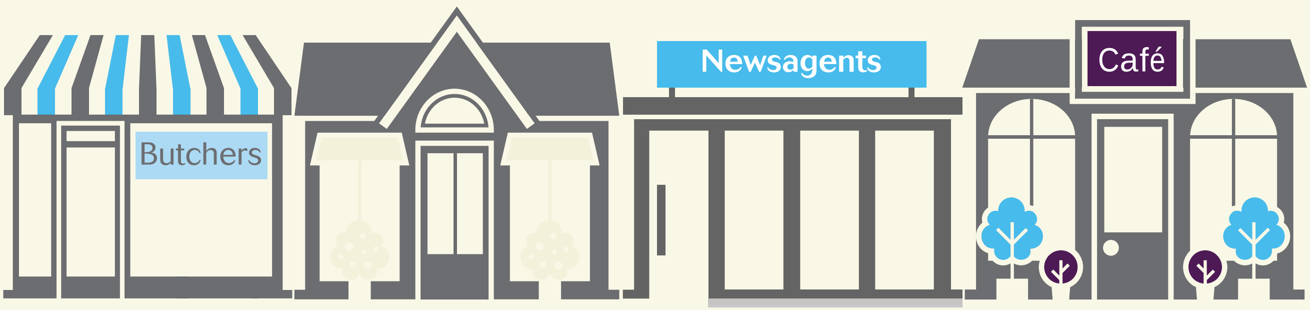
The near universal adoption of the internet seen over the last two decades in the UK is driving a fundamental change to patterns of consumption. Shoppers are increasingly choosing to buy online, with latest official figures showing that 13% of all UK retail sales were made online. Moreover, even conservative estimates suggest that this will rise to 20% by the early 2020s.

While ecommerce presents opportunity for the UK high streets, reflected in the exponential rise of 'click and collect' offerings, it does increasingly bring into question the overall amount of conventional bricks and mortar retail space that is really needed. Weaker stores in less affluent locations are in most danger, with a report by Centre for Retail Research predicting that 22% of UK stores will close before 2020.

Conversely, the rise of ecommerce has been a boon for the UK distribution market, with demand among 'multi-channel' retailers and parcel carrier occupiers responding to the growing need for so-called e-fulfilment. In order to meet increasing demand, companies are busy streamlining their e-fulfilment processes to maximise efficiency and service levels.

Proportion of sales made online





Where now?

Boosting the New Homes Bonus

The latest government data shows that the number of homes built in England in 2014 rose 8% (to 119,000) compared with 2013. While any increase in new supply is welcome, the number of homes being built remains over a quarter below 2007 levels and well short of the 200,000 homes a number of measures suggest should be built just to keep pace with demand.

While central government is responsible for national policy which is used by planning authorities to draw up local plans, over 90% of the homes built in the UK last year were given permission by local authorities. If the UK is to increase the number of homes built, it will have to come through planning decisions made at a local level. While central government has rarely shied away from making changes to planning policy, the number of homes delivered over the last decade has continually fallen well below the levels required.

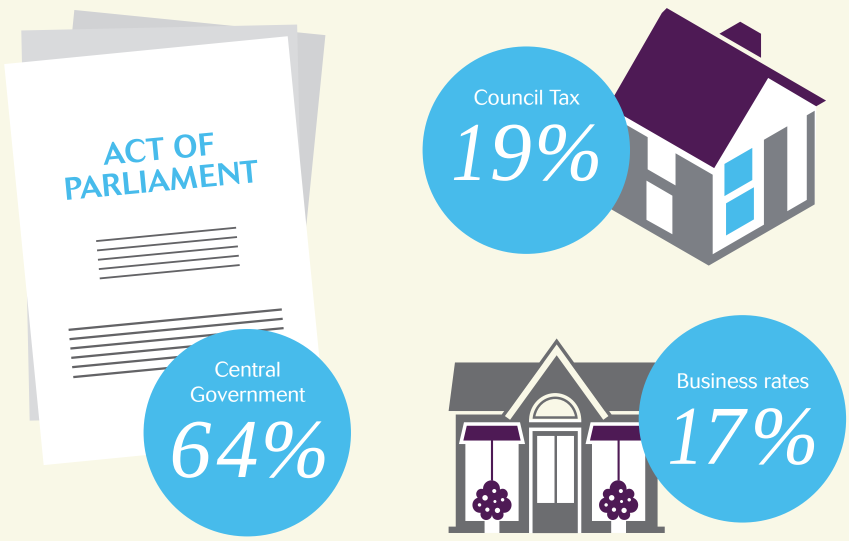
Local authorities are heavily reliant on central government for their revenues. Last year just 19% of local authority income came from council tax, a proportion which has fallen steadily given most local authorities have frozen, or at the very least capped, council tax over the last five years. The majority of local authorities' budgets come from central government, which is allocated via a complex formulae grant taking into account local tax base, population projections and local need as well as other factors.

The New Homes Bonus, introduced in 2011, was designed to provide a financial incentive for local councils to build more homes. The scheme increases the proportion of the income local authorities have direct control over by matching council tax receipts on a pound-for-pound basis for new homes delivered over a six year period. The funds received through the New Homes Bonus are broadly available for local authorities to spend as they see fit.

With the New Homes Bonus paid on all new completions (and empty homes brought back into use), it is not possible to quantify the number of homes which would have been built without the scheme. However there is now a direct link between the building of new homes and the income of a local authority.

The government originally set aside £1bn for the New Homes Bonus scheme between 2011 and 2015, to date just over £3.3bn has been paid out. Allocations made over and above the initial £1bn of funding during the current spending review period (2011-15) will come out of the formula grant received by local authorities and therefore does not represent new money for local authorities.

Where local authorities get their money

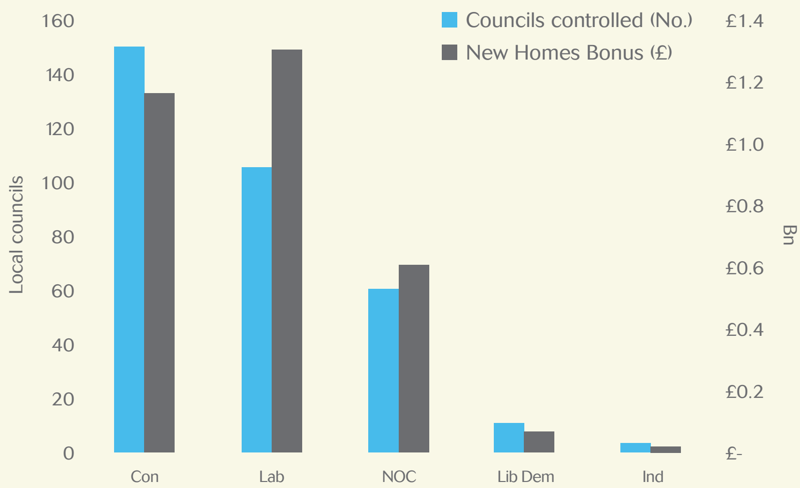


Largest recipients of NHB payments

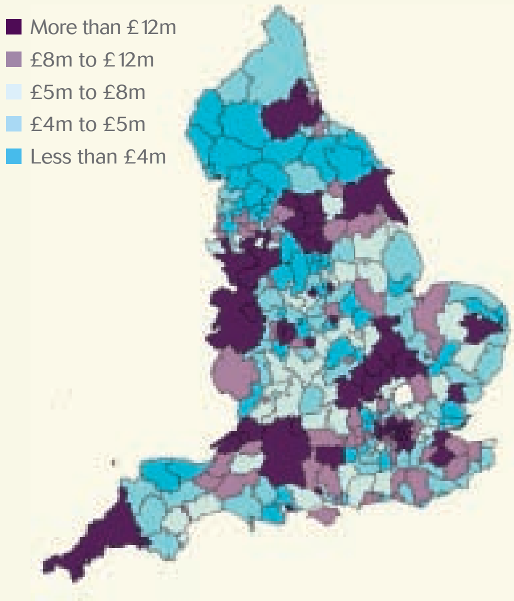
Council	Control	NHB payments to date
Tower Hamlets	NOC	£75m
Birmingham	Lab	£54m
Cornwall	NOC	£45m
Islington	Lab	£44m
Hackney	Lab	£44m
Leeds	Lab	£41m
Southwark	Lab	£40m
Wiltshire	Con	£39m
Bristol	NOC	£35m
Milton Keynes	NOC	£33m

*NOC = no overall control

Where New Homes Bonus money has gone



Source: Countrywide & DCLG 2015



Proposal 1: Rewarding delivery

The introduction of the New Homes Bonus fostered an important link between new development and local authority income. Under the existing system, the majority of funding for local services comes from central government. Across Europe local authorities, or their equivalents, raise a much larger proportion of their taxes locally. The impact of decisions made locally are directly felt by local people. Extending the role of the New Homes Bonus to encompass a greater proportion of local authority incomes at the expense of central government grant would serve to heighten the incentive for local authorities to permit new housebuilding.

We support the indefinite extension of the New Homes Bonus, which would provide more certainty for local authorities when planning and budgeting for services while continuing to provide a strong incentive for planning departments to facilitate the delivery of new homes. While the current six year period does allow local authorities to bank on receipts for future income, the requirement to provide services for these new homes will of course continue beyond these six years.

The New Homes Bonus now represents a significant proportion of local authority incomes. Against a £20.8bn central government settlement to local authorities in 2015/16 (which comes on top of locally raised council tax), the New Homes Bonus represents total payments of £1.17bn or around 5.7% of the total. This is not an insubstantial sum at a time when the central government payment to local authorities will fall from £24.1bn to £20.8bn between 2014/15 and 2015/16.

Doubling or tripling the grant attached to each new home would further increase the incentive to build locally. **We support increasing the premium attached to the delivery of each new home.** It would also serve to help establish a greater link between locally raised revenue and local services. If local communities are more tangibly able to see the benefits of housing built in their area, it seems likely it will reduce their opposition to it. Indeed if local communities feel the benefits that come from new housebuilding are large enough, they may reverse from being opponents of new development to its proponents.

Redefining Greenbelt for modern needs

The rapid growth of London during the 1930s was, for many, a cause of concern. Between 1930 and the 1939 the capital grew by almost 100,000 people per year, a similar rate to today. By 1939 8.6 million people were squeezed into an area around 35% smaller than the footprint of London today. The vast majority of these were living in what is known as inner London today. Overcrowding, particularly in the inner city meant that living conditions were often extremely poor. As concerns about living conditions grew, the Greater London Planning Committee were the first to propose the creation of a Greenbelt, preserving areas surrounding London from future development.

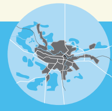
Perhaps ironically the Greenbelt, which is broadly unchanged since it was drawn up in the years immediately after the Second World War, represented a barrier to growth at a high water mark for many British cities. The Second World War saw many flee the cities and not return, while the decades after the war saw deindustrialisation take a bite out of the number of jobs. Between 1939 and the late 1980s, the population of London fell in virtually every year to 6.6 million. Similar falls were recorded by most British cities. As such, managing decline rather than growth was the priority for most councils.

Fast forward to 2015 and London saw its population once again pass 8.6 million, 76 years after it previously first reached this figure. While the population of many cities, particularly those where heavy industry provided large numbers of jobs, are still below where they were on the eve of the Second World War, since the turn of the millennium they have again begun to grow. As urban populations approach the levels they reached when the Greenbelt was drawn up, we need to ensure it doesn't become an ever tightening collar on urban growth.

Potential plots within a mile of railway stations in the greenbelt

Greenbelt	Plots
Birmingham Greenbelt	64,000
Bournemouth Greenbelt	33,000
Bristol and Bath Greenbelt	25,000
Liverpool, Manchester and West Yorkshire Greenbelt	162,000
London Greenbelt	213,000
North East Greenbelt	12,000
Total potential new homes	**509,000**

Source: Countrywide Research



Proposal 2: Take another look at what we call Greenbelt

Greenbelt comes in all shapes and sizes. It encompasses both Areas of Outstanding Natural Beauty and low density industrial land. Given it was drawn up in the 1940s and 1950s, **we support a review of precisely what we call Greenbelt today**. Building homes close to where people work is one of the most sustainable places to build. While new garden cities have been suggested as a potential solution to the question of supply, allowing growth on the city fringe would also serve to organically add significant numbers of homes close to existing centres of employment.

There are almost 80 railway stations in the Greenbelt on the fringes of cities across England which by virtue of their location offer excellent transport links. Given much of the railway network was built by the Victorians, the areas surrounding stations, even those in the Greenbelt, have in many cases already been developed to some degree. These are places which sit in 'Greenwash', areas of developed land which in local plans fall completely into the Greenbelt. **Promoting development in areas within walking distance of those train stations in the Greenbelt which have already been developed, has the potential to accommodate around half a million new homes.** Over half of these homes could be built on sites in London and the South East, within easy reach of employment markets, the places where demand for homes is greatest.

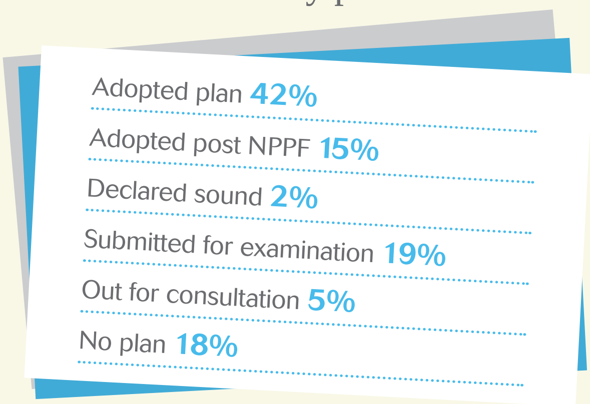
Giving planners time to catch up with policy

The last 10 years in particular have seen successive governments make substantial changes to the plan led system. In 2004 Regional Spatial Strategies were introduced for the first time creating a new tier of planning. These sat between national and local planning policy and were produced by newly created Regional Planning Bodies. Despite being in existence for six years, a number of regions did not manage to fully adopt plans before they were eventually scrapped, taking an average of five years for each plan to be adopted.

The same 2004 act introduced a system of Local Development Frameworks (LDF), creating a portfolio of documents local planning authorities had to produce by 2007. They replaced a previous system which contained a mixture of county and local plans. By 2010, six years after the act and three years after each local authority was required to have adopted their LDF, government data shows that just 20% (72 out of 354 local authorities) had a Core Strategy in place – the most important development plan document. The rates of adoption for other (statutory) development plan documents such as waste, minerals and site specific allocations were lower. Even today, only around 60% of local authorities have the required statutory documents in place.

The introduction of the National Planning Policy Framework (NPPF) in 2012 reduced the amount of national planning policy. Thirteen Planning Policy Statements which ran to some 1,300 pages were replaced with 65 pages of guidance. Upon its introduction local authorities were given a period of 12 months to ensure their portfolio of LDF documents complied with new legislation. To date less than 20% of core strategies have been formally adopted post NPPF. There is growing divide between what local authorities are required to produce and their ability to reflect changes in reality.

Status of local authority plans



Source: Countrywide Research

Proposal 3: Time to catch-up

At its best the planning system provides certainty for local communities, developers and local authorities. Over the last ten years the fundamentals of the planning system have been in constant state of flux following reform by successive governments. Local authorities are still playing catch-up with reforms made a decade ago. While planning policy needs to be kept up to date, it is a process which takes considerable time. Infrastructure and large development schemes frequently take a decade to bring to fruition. The existing Crossrail route was safeguarded from development in 1991, 19 years before construction began.

For the planning system to work effectively, its users need a degree of certainty. Development plans recognise this and typically have a lifespan of 20-25 years and in theory should be updated every 5-10 years. Given that many local authorities' statutory planning documents are yet to reflect the changes required by the last two reforms, **we believe there should be a period of 3-5 years free from reform of the plan led system during which planning documents are brought up to date**. A failure to update plans, bringing them into line with recent reforms within this period would result in a strong presumption in favour of development until a plan is adopted.

Permitting change of use

The current coalition government's wide-ranging extension to permitted developments rights (PDR) is a fundamental step towards a more responsive, flexible UK planning system. While far from a magic bullet, PDR can play a key role in attracting housing development and restoring vitality to our town centres.

Office to residential

Among a host of extensions to PDR, both in force and proposed, potentially the most far reaching is the right to change use from offices to residential, in effect since May 2013. Allowing underutilised office space to be converted to housing without the need for full planning consent – or affordable housing contributions – provides a welcome boost for residential developers, while removing obsolete office space.

Evidence of the impact of PDRs, however, is mixed. Research by Planning Magazine in late 2014 identified 17,426 units with prior approval. This is far more than was ever expected, but equates to less than 10% of the annual housing requirement of the UK. London has also been the overwhelming focus, with Croydon providing the main hotspot, along with a number of locations in the South East, such as Brighton and Slough. Anecdotal evidence suggests, however, that few schemes with prior approval have moved beyond the drawing board.

The DCLG consultation sets out further permitted development rights allowing conversion of industrial and warehousing space to residential. We agree with the principle of further liberalising PDR, but remain sceptical that this particular proposal has genuine potential to deliver a high quantum of high quality housing.

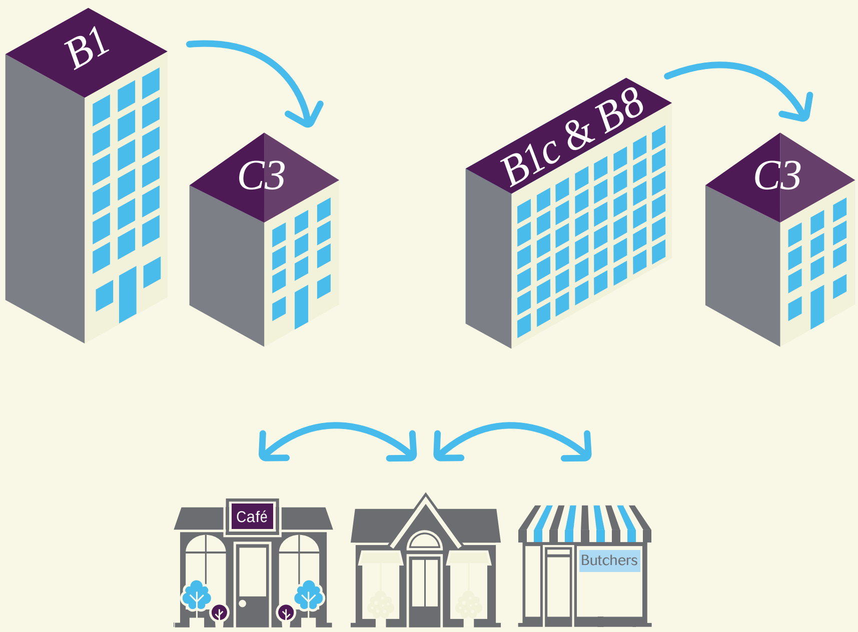
Proposal 4: Make PDR rights permanent

We are in favour of putting the PDR onto a much more permanent footing, as proposed by the Department of Communities and Local Government (DCLG) in its Technical Consultation Paper on Planning (July 2014). If a new, amended PDR does come into force, it is vital that it does not represent a watered-down version of its predecessor and is in place for at least a decade to allow it to be fully utilised.

Proposal 5: A wider retail use

We support DCLG proposals to assist the UK high street, namely **the establishment of a wider retail use and additional PDR to convert from retail to leisure**. While taken alone this is unlikely to reverse the decline of many UK high streets, it does allow localities to respond more quickly to demand, as well as recognising the increased importance of leisure in attracting footfall to town centres.

Key additional proposals to PDR in DCLG's Technical Consultation on Planning (July 2014)



Reforming business rates

The current system of business rates does not seem fit for purpose. We believe a fundamental reform of this tax is required in order to promote small business growth and investment in the localities that need it most.

Business rates explained

- An annual tax on the right to occupy non-domestic property, based on a property's Rateable Value (i.e. annual rental cost) at valuation.
- The current Uniform Business Rate (a single multiplier set centrally) dates back to 1990, but taxing the right to occupy property dates back to the Poor Law of 1572.
- Rates are payable by both private and public organisations, such as schools, hospitals and local authorities.
- The tax is payable annually and rises with RPI inflation between revaluations

Properties are revalued every five years. However, the 2015 revaluation has been postponed until 2017 meaning occupiers will be paying rates which reflect rental values which are up to nine years old. They raise £27bn in revenue annually for the exchequer, accounting for circa 4.5% of UK total tax income and three times the Stamp Duty Land Tax.

Proposal 6a: Increase the frequency of revaluations from five to two years

The five-year frequency of revaluations means that business rates are unresponsive to prevailing market conditions. Many parts of the UK have seen significant falls in rents since the last 2010 revaluation, yet occupiers are paying rates reflecting rateable values from the previous valuation date of April 2008, the peak of the last cycle. **A more frequent revaluation would address this distortion.**

Proposal 6b: Scrap the annual inflation uplifts

Increasing the frequency or revaluations should also be accompanied by a removal of RPI uplifts in the Universal Business Rate (UBR). Business rates is the only tax of its kind to be subject to inflationary increases, yet rental growth has generally failed to keep pace with RPI over past 30 years, and particularly since the 2010 revaluation.

Proposal 6c: Exempt small businesses entirely from business rates

The government should extend help to small businesses by raising the rates exemption level to a rateable value of £12,000, up from its current level of £6,000. Analysis by the British Property Federation reveals that small properties (with RV <£12,000) account for nearly two-thirds of the UK total yet provide just 6% total revenue. In our view, the loss in revenue would be largely recovered through substantial cost savings via simpler administration and a reduced number of appeals.

Proposal 6d: Targeted assistance aimed at high street

Given the headwinds faced by retailers and high levels of vacancy in less affluent towns and cities, further assistance should be made available to encourage occupation of UK high streets. Firstly, at the discretion of the local authority, **we advocate the introduction of 'rates relief zones' (RRZs) where designated streets or areas are allowed complete rates relief regardless of ratable value. Secondly, rates relief on occupiers taking properties that have been vacant for a minimum of 12 months should be increased from 50% to 100%, and granted for a minimum of two years**.

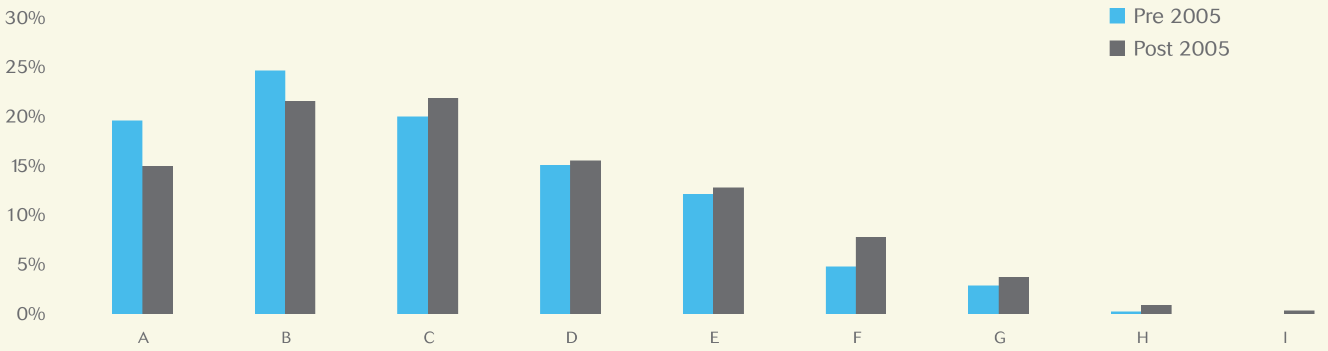
Reforming council tax

The current UK council tax system was introduced in 1992 and was based on the value of each property in April 1991. While in England the system continues to operate in the same way, in Wales, council tax bands were updated in 2005 in an attempt to reflect both rising prices and the distribution between the two ends of the market. The addition of a new top band, Band I, meant that all properties valued at over £424,000 would pay 3.3 times what a Band A pays, up from three previously.

The impact of this reclassification was substantial – just over 40% of properties changed council tax band. Of these, 32% saw higher bills while just 8% paid less. It was properties in the lower bands in particular which found themselves uprated – one in four Band A properties were moved to Band B meaning the occupier faced an increase in their council tax bill – albeit a relatively modest £104 per year. A property which moved from Band H to the new Band I saw bills increase by an average of £312 a year (the gap between the two bands stands at £433 today).

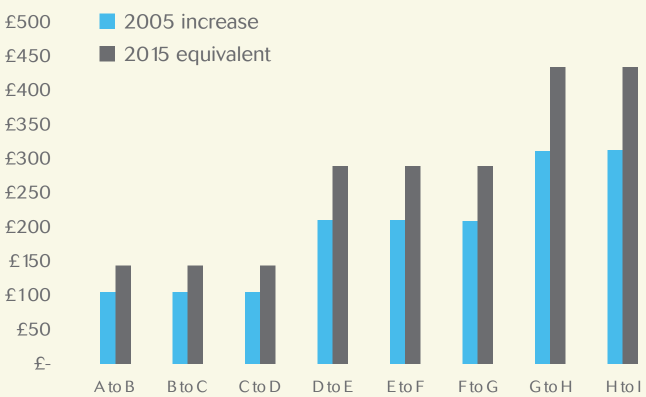
Reform of the Welsh council tax system was achieved relatively quickly, cheaply and was broadly supported within Wales. There are, however, two important lessons which should be learnt from the Welsh experience before wider reform takes place. First, any re-valuation would need to pay particular attention to increases faced by those in the lowest bands. More homes in Wales were moved from Band A to B than from Band D to E. Second, the narrower distribution of house prices in Wales means the difference in price between a three bed semi in Cardiff and Wrexham is much smaller than the difference between the same houses in Newcastle and Ealing. Any reform of the current system would need to strike a careful balance between the growing disparity in values between the South East and the rest of the UK.

The impact of reform on Welsh housing stock



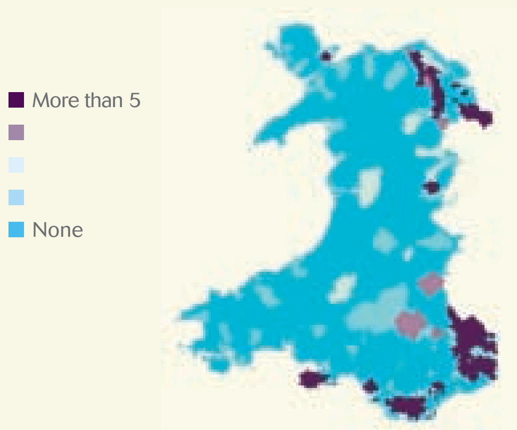
Source: Countrywide, ONS 2015

The cost of moving bands



Source: Countrywide, gov.uk 2015

Properties falling into new Band I in Wales



Proposal 7: Following Wales

The growing divide between the value of homes between the South East and the rest of the country has increasingly made any council tax valuation ever more sensitive. We believe reform of the existing council tax system offers a farer and more practical alternative to a mansion tax.

The existing council tax system remains not only an efficient mechanism for the collection of revenue to fund services, but acts as a tax on the value of the property. **We propose the addition of a new Band I at the top of the scale, in similar fashion to Wales**, which would better reflect the growing disparity in property values.

We also propose bringing 1991 values up-to-date, alongside merging some of the lower bands which would help to account for the regional variations which have emerged. At the bottom of the scale wider bands would help ensure that similar types of properties across the country broadly fall into similar council tax bands. This would protect most Londoners and those living in higher value areas of the country.

Updated bandings and the introduction of a new Band I would raise between £500m and £700m, around half what the Labour party believe a mansion tax could raise. This additional revenue would be raised through a product both of a higher council tax bill for properties worth more than £1.5m, but also the growing disparity in values between the South East and the rest of England. While widening the lower bandings would serve to temper the increase faced by the vast majority of those living in London and the South East, national re-valuing would see more southern properties pushed into higher bands.

1992 Band	1992 values	% of Band D	1992 property distribution	Proposed bands	Proposed 2015 values	% of Band D	Proposed property distribution	Proposed revenue distribution
A	Up to £40,000	67%	24.8%	A&B	Up to £144,000	67%	21.1%	14.9%
B	£40,001-£52,000	78%	19.6%	C&D	£144,000-£245,000	89%	55.1%	51.5%
C	£52,001-£68,000	89%	21.8%	E	£245,000-£443,000	122%	14.1%	18.1%
D	£68,001-£88,000	100%	15.3%	F	£443,000-£886,000	144%	7.6%	11.5%
E	£88,001-£120,000	122%	9.4%	G	£886,000-£1,500,000	167%	1.5%	2.6%
F	£120,001-£160,000	144%	5.0%	H	£1,500,000-£3,000,000	250%	0.5%	1.1%
G	£160,001-£320,000	167%	3.5%	I	£3,000,000 +	350%	0.1%	0.4%
H	£320,001+	200%	0.6%					

For example

£5m Band H Camden Home

- Current council tax: £2,640
- Reformed council tax: £4,620
- Mansion Tax: £10,640

Stability and transparency for landlords and tenants

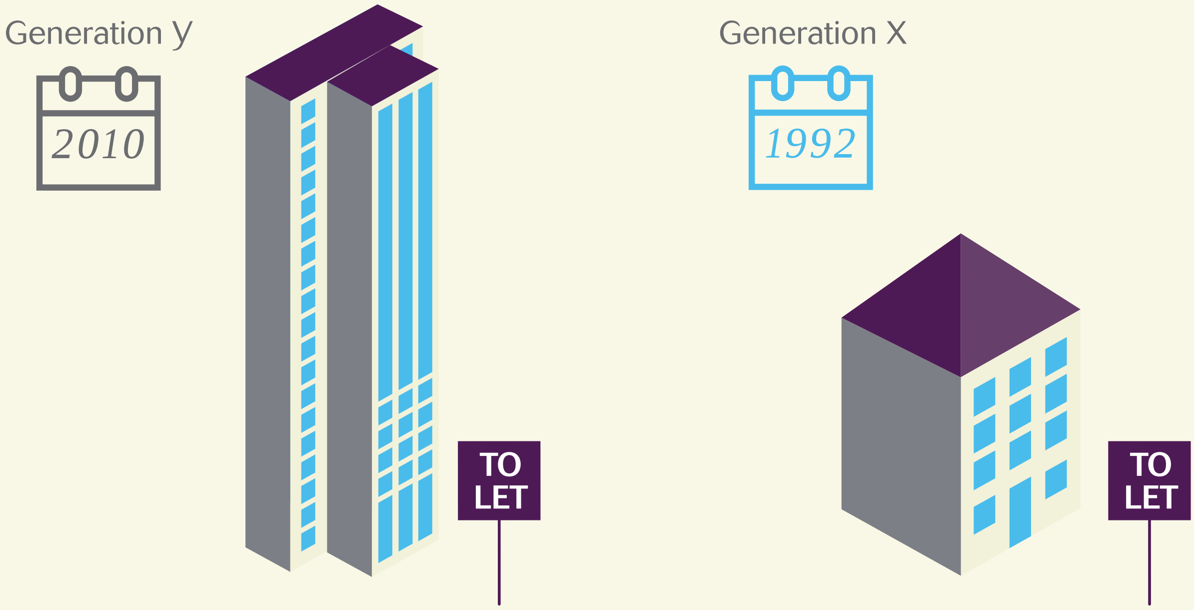
With limited public funds for subsidies, the aspiration for home ownership may not be achievable for all. When housing is in short supply, private rental is actually a more efficient use of stock, due to higher occupancy rates. Our research shows that if all of the 135,000 new homes that were built in the UK during the last 12 months went into the private rented sector, they could be expected to house 281,000 people, but if every new home went to an owner occupier, 40,000 fewer people would be housed.

There are two main reasons for higher occupancy rates in the PRS. First there is a bigger incentive not to pay for empty rooms as there is no gain from capital growth on the extra space. Second, with no stamp duty, legal costs or waiting lists, the flexibility of the private rented sector means those renting can move as their housing needs change. Private tenants account for 60% of households that move each year, but just 19% of the population. If we recognise that renting is a serious tenure for both the short and long term, it needs to be more attractive for tenants and investors. The growth of buy to let lending has helped add stock to the private rental sector and hence some choice to tenants, but without faster additions to the overall housing stock this doesn't solve the problem of a lack of housing supply and its effect on affordability. Indeed, the growth in private renting partly reflects that deteriorating affordability in the owned sector and suggests an increasing acceptance of renting for the longer term and the need in some cases for greater security of tenure.

To make private renting a more acceptable choice for the long term, landlords and tenants need certainty over rents and tenure length. Institutional landlords will find it easier to offer longer tenancies, but much of the sector is currently serviced by small landlords who are likely to be more risk averse, or are looking for flexibility to sell if the opportunity arises. Some would like to offer longer term tenancies but are constrained by lending conditions limiting tenancy length to one year. Nationwide Building Society has notably extended its terms to allow three year tenancies which could see other lenders follow.

Certainty of rent can also be achieved through the mutual benefit and agreement of both parties. While rent control sounds scary, it needn't be so heavily regulated as was the case under assured tenancies. In Germany the majority of rental agreements are unlimited, but rents are pegged to an index, giving landlord and tenant certainty. On top of this there are options for review to reflect improvements or if rent falls behind the prevailing rate in the vicinity.

Younger people are renting for longer. The proportion aged 25-34 has increased from 31% in 2008 to 45% in 2014.



Making build to rent viable

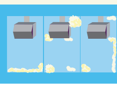
Indexing rents to inflation is familiar in commercial contracts in the UK and should be easy to adopt for institutional investors as a result. Indeed there is precedent for this in the UK already in the Olympic Village development. Longer tenancies, up to three years, are available with agreed rent reviews in line with CPI. Landlords also benefit from fewer void periods and reduced search costs. In addition, tenants who stay longer are likely to take better care of the property. There seems no obvious reason why this approach shouldn't be taken across the whole of private rented sector.

Proposal 8: A new type of tenancy

We propose the creation of standard six, twelve and thirty six month contracts to promote private rental as a viable alternative to owner occupation for tenants and certainty for landlords. This may require agreement from lenders in the buy to let sector, but there is clearly movement in this direction.

We propose that an agreed indexing of rent be built into longer contracts to protect landlords and tenants, but that there remains the opportunity for the landlord or the tenant to be released from the contract with a pre agreed notice period.

Proposal 9: A reinterpretation of best value



We propose that local authorities should be allowed to interpret the best value obligation in land sales in a more flexible way to be able to release lend for PRS rather than owner occupied development.

To make land available at a lower cost for private rental sector development, local authorities should be able to restrict land for private rental sector use, reducing S106 requirement where viability becomes an issue.

Stimulating investment in PRS stock

Institutional investors have a role to play in increasing both the quality and quantum of rented stock. Despite the Build to Rent Scheme allocating £1 billion of government support, the progress of the scheme so far has been disappointing. Although the fund was launched 2012, only £150 million worth of contracts, aiming to produce just over 2,000 units (split fairly evenly inside and outside London) were signed in phase 1. Phase 2 shortlisted a further 36 bids to allocate nearly 10,000 units, with about 60 per cent in London.

The Montague Report shows that there should be a good match for pension fund investment as rents tend to rise in line with real incomes. Residential investment also provides some diversification from commercial property. Unfortunately other barriers to investment remain strong. Many investors are not prepared to take on development risk, and are interested only in income returns, which tend to be lower in the residential than commercial sector. To encourage new building the gap between these two types of returns on investments must be reduced.

The answer would seem to lie in the availability of land and its cost. Section 123 of the Local Government Act 1972 puts the duty on local authorities to achieve best value in the context of land disposals. That tends to bias the sale of land to owner-occupied developments. To encourage more production of housing for rent there is a need for this criteria to be interpreted differently. Kate Barker suggests making land available at slightly lower cost, either by putting a planning restriction on the land, or by reducing the requirements under S106, which could make this more viable. In return for the lower cost of land the developer may be required to ensure that the building is kept as PRS for a certain time thus helping promote secure tenancies.

Shared Ownership and Help to Buy

Shared ownership was introduced in the late 1970s to help people unable to afford a home on the open market get on to the property ladder. Predominantly provided by housing associations, it allows the purchase of a share in a property (typically between 25 and 75%). The housing association owns the remaining share, on which the shared owner pays rent.

Demand for shared ownership vastly outstrips supply, with housing associations approving around 85,000 applications a year, against government funding for the development of just 11,000 shared ownership homes. The tenure has the advantage of giving part owners security of tenure similar to outright ownership, not always available in the private rented sector. As a step towards achieving the aspiration of ownership it is a strong concept. There are several practical barriers, however, preventing the tenure from being universally successful, not least its availability.

Even in London where high prices mean access to home ownership is most limited, shared ownership accounts for just 1.3% of households. To expand shared ownership there has to be a clearer understanding of the product, greater awareness of its availability and increased supply.

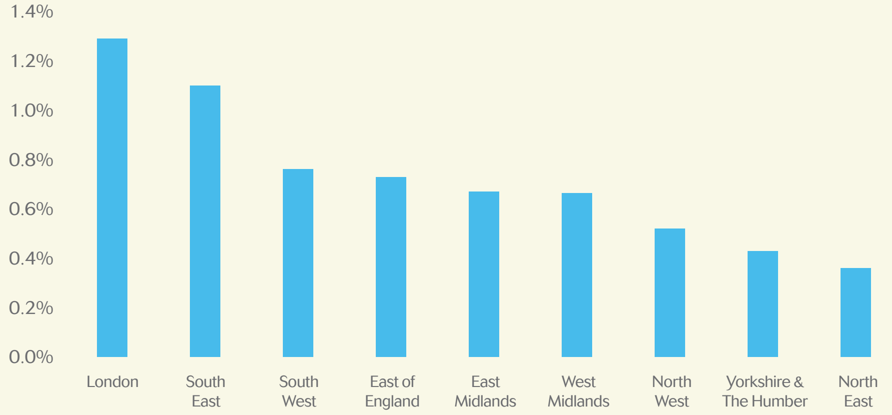
The administration of the purchased share of the property can also be a stumbling block. The current provisions are perceived to have hampered the selling of shared ownership homes because they overcomplicate the process when the householder wants a quick and straightforward transaction. In addition, lenders are concerned that the process affects the value of the home and hence its security. This has meant the market for lending on shared ownership homes is limited.

Part of the issue is illiquidity within the sector. If a tenant/owner wants to move on they must first seek the consent of the housing provider to assign the lease, in writing. The housing provider has eight weeks in which to decide whether to buy the property back or to sell to another buyer before the home can be put on the open market. The opportunity on the part of the housing provider to nominate the next purchaser continues during the period of shared ownership for each owner and even in some instances after the householder has bought the property outright. This seems overly restrictive, particularly if there is a longer term aim to produce more mixed tenure communities.

The argument that opening up the shared ownership resale market would mean housing need isn't considered as well doesn't seem to hold sway either. There are terms and conditions regarding income and location which can still stand as conditions of tenancy, but administration for the housing provider would be reduced.

The Government is clearly attuned to the aspiration for home ownership through its Help to Buy initiatives, so there seems little reason why there shouldn't be greater freedoms to allow stair casing and selling of interests off more efficiently. Indeed the Help to Buy Equity Loan Scheme is itself a form of shared ownership, but in more restrictive terms and for a defined period.

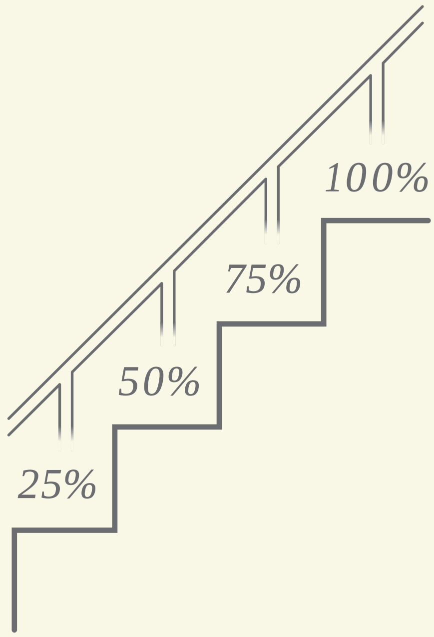
As a tenure shared ownership is largest in the most expensive areas



Source: Census 2011

The government has seen its investment Help to Buy properties rise by £70m

Source: Hamptons International, ONS 2015



The equity loan is free for the first five years, and in the sixth year, a fee of 1.75% of the loan's value is payable. The fee increases every year in order to ensure the loan is repaid. The fee is indexed to RPI plus one per cent.

Loans made under the Help to Buy Equity Loan Scheme across England have increased in value as the housing market has recovered, particularly in London where there is most demand. To date the total increase in the equity share in England amounts to about £70 million. Given that Help to Buy was designed to assist home ownership aspirations, this equity growth is a bonus and should be considered as a source of funds for investment in new shared ownership units to replace stock which moves into the owner occupied sector upon sale.

Proposal 10: Sharing out shared ownership

We propose that the need for the housing provider to retain a hold over the property for those who have purchased properties outright should be removed. These restrictions subdue the price achievable for the property and limit marketability- even among those who may qualify for shared ownership.

We support the current government consultation which suggests reducing the period a Housing Association has to find a buyer from eight to four weeks, but suggest that the measures go further than this. We suggest that the market is more efficient at finding a buyer and the house holder should be allowed to market the property directly, to speed up the process.

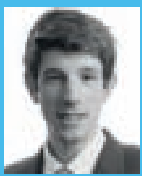
We propose that the owner be allowed to sell shares at different levels when a property comes up. That has the advantage of opening up the market further and achieving a potentially higher value for both the housing provider and householder. That additional sum can be used to provide more affordable or shared ownership units.

We propose that the rise in equity achieved through the Help to Buy Scheme be earmarked to replace and increase the availability of shared ownership.

Johnny Morris
Head of Residential Research
morrisj@hamptons-int.com
+44 (0)2077588438

Fionnuala Earley
Residential Research Director
earleyf@hamptons-int.com
+44 (0)2077588465

Oliver du Sautoy
Head of Commercial Research
odusautoy@lsh.co.uk
+44 (0)2071982193



David Fell
Research Analyst
david.fell@countrywide.co.uk