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PRICED OUT?

THE AFFORDABILITY CRISIS IN LONDON

Luke Murphy and Darren Baxter

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SUMMARY

London's housing market is increasingly unaffordable for those on low to middle incomes. While it has always been more expensive to rent or buy in the capital, the scale of the unaffordability of housing has never been greater. As a result, today's Londoners or would-be Londoners face a range of consequences including lower levels of home ownership, increased overcrowding, and rising levels of homelessness and rough sleeping. There are also wider consequences including increasing wealth inequality and higher costs to the public purse, not least through a rising housing benefit bill. It is also affecting London's economic competitiveness, with businesses finding it increasingly difficult to recruit and retain staff in the capital.

Building more homes, particularly affordable homes, will be crucial to tackling the affordability crisis that the capital faces. Yet the evidence shows that housing delivery is falling well short of estimated need – and the provision of affordable housing even more so. Despite a range of products on offer in the capital, the level of intermediate housing to rent and buy to support those on low to middle incomes is extremely modest. Moreover, our analysis reveals that many sub-market home ownership products on offer in the capital are in fact unaffordable and some fail to meet the aim of many households to achieve full home ownership.

The new Mayor of London, Sadiq Khan, has made a promising start, committing to a long-term strategic aim for 50 per cent of new homes to be affordable, introducing lower benchmark rents for the London Affordable Rent product, and introducing a new intermediate product in the form of the new London Living Rent. However, there's more that can be done at all levels. Central government should, in the short term, seek to increase the capital subsidy to the London Mayor in order to increase affordable housing output. This should be followed in the medium to long term by the devolution of additional powers for the Mayor to set and retain property taxes in the capital so that London can determine its own housing future. There needs to be a clear and universal understanding of what 'affordable' means and each and every affordable housing product should be rated against it; those that don't match up should not be eligible to be considered as affordable housing or supported by subsidy.

KEY FINDINGS

- London is failing to deliver the homes it requires to meet housing need – the annual minimum target is 42,000 homes but the average delivery over the past 12 years (2004/5 to 2015/16) has been 31,125.
- The delivery of net additional affordable housing is falling even further short of need than for overall supply – the overall shortfall is 50 per cent under target over a three-year period (2013/14–2015/16). With a new London Plan in development and a new methodology for assessing housing need, it is likely that assessed housing need is only likely to increase, making the shortfall even greater.
- A single person (working full time) on lower quartile or median earnings living in London would find all affordable home ownership products in the capital unaffordable under a 35 per cent net income cap.

- A couple with a child (one working full time and the other working part time) on lower quartile earnings would find all affordable home ownership products unaffordable under a 35 per cent income cap. On median earnings, shared ownership would be affordable in six boroughs, while London Help to Buy would be affordable in one borough.
- For a couple (both working full time), far more products come into reach, with shared ownership becoming affordable to those on lower quartile earnings in over a third of boroughs. For a couple both on median earnings, shared ownership becomes affordable in the majority of boroughs and London Help to Buy in more than half of boroughs.
- Starter homes perform poorly and are inaccessible to all those except on the very highest incomes. They would be affordable only to a typical couple with one child on upper quartile earnings in just five boroughs and the same for a couple working full time on median earnings.
- Some affordable housing products don't meet their specified aims; for instance a household living in a Rent to Buy home wouldn't be able to save for a sufficient deposit to buy a home outright in any London borough when saving the difference between their rent and market levels.

RECOMMENDATIONS

1. Devolved funding and increased investment: the government should increase the capital subsidy to the London Mayor to increase the number of affordable homes that can be built. In the long term, the capital grant should be gradually replaced in exchange for additional devolved powers for the Mayor to set and retain property taxes in the capital.
2. A clear measure of affordability – and mapping the affordability of sub-market housing products: a universally understood affordability measure should be developed, linked to earnings, and applied transparently for every affordable housing product – with the development of an affordability matrix that sets out when each product becomes affordable.
3. Clear targeting of subsidy to meet stated aims: subsidy should be targeted at those products that are clearly affordable, and it should be withdrawn from products that do not meet the need of those for whom they are designed to assist. This should include London Help to Buy, the funding for which should be placed under the control of the London Mayor to direct as they see fit.
4. Support of innovation and encouragement of the development of alternative affordable housing models: the government and the Mayor should consider how new and innovative products and delivery models might contribute to meeting the capital's affordable housing need. This should include the reform of compulsory purchase orders to enable the purchase of land at a lower value and the funding of affordable housing at lower costs.

1.
INTRODUCTION

London's distinct housing market has been exhibiting the strains of a crisis for some time. The scale of the demand for property, the tenure and household mix, the affordability gap for both renting and buying, and the scale of serious housing need all set London apart from the rest of England (Harrison et al 2013). In short, the housing crisis in the capital is more acute than elsewhere, driven by significant undersupply and affordability challenges (LHC 2016).

It has always been more expensive to rent or buy a home in London when compared with the rest of the country – in nearly two-thirds of London's boroughs, the ratio of lower quartile house prices to local earnings was higher in 2002 than the England average in 2016 (ONS 2017a). Yet the demand for homes, the housing supply gap and the crisis of affordability have never been greater. Home ownership in the capital has dropped significantly, with fewer than 50 per cent of Londoners now owning their own home. Moreover, because of the high housing costs in the capital, the number of Londoners living in poverty almost doubles to just over two million once housing costs are taken into account (JRF 2013).

This has not gone unnoticed by the public. Until recently, polling showed that the housing crisis was the number-one concern facing the capital. Crucially, seven in 10 people reject the notion that the government can't do much to tackle the housing crisis but fewer than two in 10 people believe the government has the right policies to solve it (Ipsos MORI 2017).

In London there is a division of labour between local authorities, the Mayor and central government in terms of who has the power and responsibility to build more homes, plan new communities and improve existing housing stock. In campaigning for the mayoralty, the Mayor of London Sadiq Khan said that the election was a 'referendum on the housing crisis' (Khan 2016). Having won, he has set a high bar for achievement and progress will be expected. Yet the Mayor has fewer powers to drive up the overall supply of new homes than he does to increase the number of affordable homes.

Perhaps that explains the Mayor's focus thus far on driving up the proportion of affordable housing in the capital: securing a deal with government to devolve £3.15 billion for affordable housing; introducing a threshold of 35 per cent affordable housing on developments without the need for viability assessments; introducing lower benchmark rent levels for London Affordable Rent, and introducing a new intermediate rent product in the form of London Living Rent.

Crucial to tackling the housing shortage will be building more homes in the capital and addressing the long-standing drivers of the housing crisis: the undersupply of land; the complexity of the planning process; lack of sufficient investment, and capacity challenges in construction. Only a sustainable increase in house-building over the long term will contain rising housing prices, but it is crucial that a significant component of the new homes, if not a majority, be provided at sub-market levels.

This briefing provides an overview of London's housing market with a particular focus on the way in which the housing crisis has reached up the income scale to increasingly affect those on low to middle incomes. We assess the new-build products available to assist this struggling demographic in the capital, their affordability and whether they meet their stated aims. We argue that a significant proportion, if not a majority, of new homes delivered in the capital should be affordable – and it will be essential that a range of products to rent and buy are provided to meet the diverse needs and incomes of Londoners.

2.
A CRISIS OF SUPPLY?

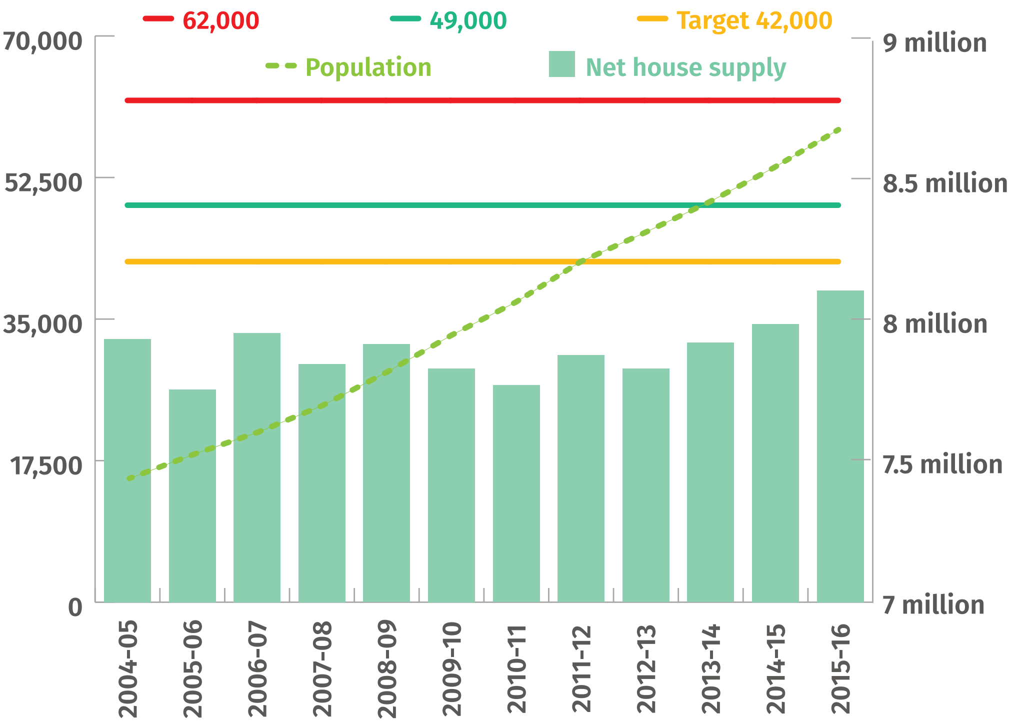
LONDON'S SUPPLY CRISIS: HIGH DEMAND AND UNDERSUPPLY

Annual estimates of the need for new homes in the capital currently vary from 50,000 to 80,000 a year (Wilson 2015). The 2013 Strategic Housing Market Assessment (SHMA), which provides evidence on London's requirement for new housing to 2035, identified a need for 48,800 homes a year between 2014/15 and 2034/35 (GLA 2014a).[1]

However, the Strategic Housing Land Availability Assessment (GLA 2014b) found evidence for capacity for only 42,000 new homes a year (which is the London target) between 2015 and 2025 within London Plan policies and constraints, with the potential for delivering up to 49,000 if the density of new schemes in certain areas could be increased.

FIGURE 2.1

Net housing supply and population estimates in London, 2001–02 to 2015–16
Net housing supply continues to fall well short of the capital's housing targets and estimated need



Source: GLA 2017a

1 Although the SHMA also considers another annual requirement of 62,000 new homes a year, which is based on clearing the historic backlog of undersupply of housing in London in 10 years, rather than 20 years as in the 48,800 estimate.

Despite a lower target set well below need but at assessed capacity, the supply of new homes in the capital continues to fall significantly short (as Figure 2.1 shows). Over the past 12 years an average of 31,125 homes have been delivered each year, more than 10,000 homes short of the current annual annual minimum target of 42,000 homes (GLA 2017a).

London isn't alone in its supply challenges, but the London Housing Commission (2015, 2016) identified the key barriers the capital faces to building more homes: land, planning, investment and construction. These challenges must be confronted if we are to build more homes over the long term in the capital.

3.
UNAFFORDABLE CAPITAL?

The increasing unaffordability of housing in London is a key issue for Londoners. For decades it has been more expensive to buy or rent in the capital relative to the rest of England (LHC 2016). In 19 of London's 33 boroughs, the ratio of lower quartile house prices to earnings was higher in 2002 than the 2016 average across England (see Figure 3.1) – for example, the ratio was 10.4 in Camden, 11.5 in Westminster and 7.6 in Richmond upon Thames, compared with 7.2 across England as a whole (ONS 2017a).

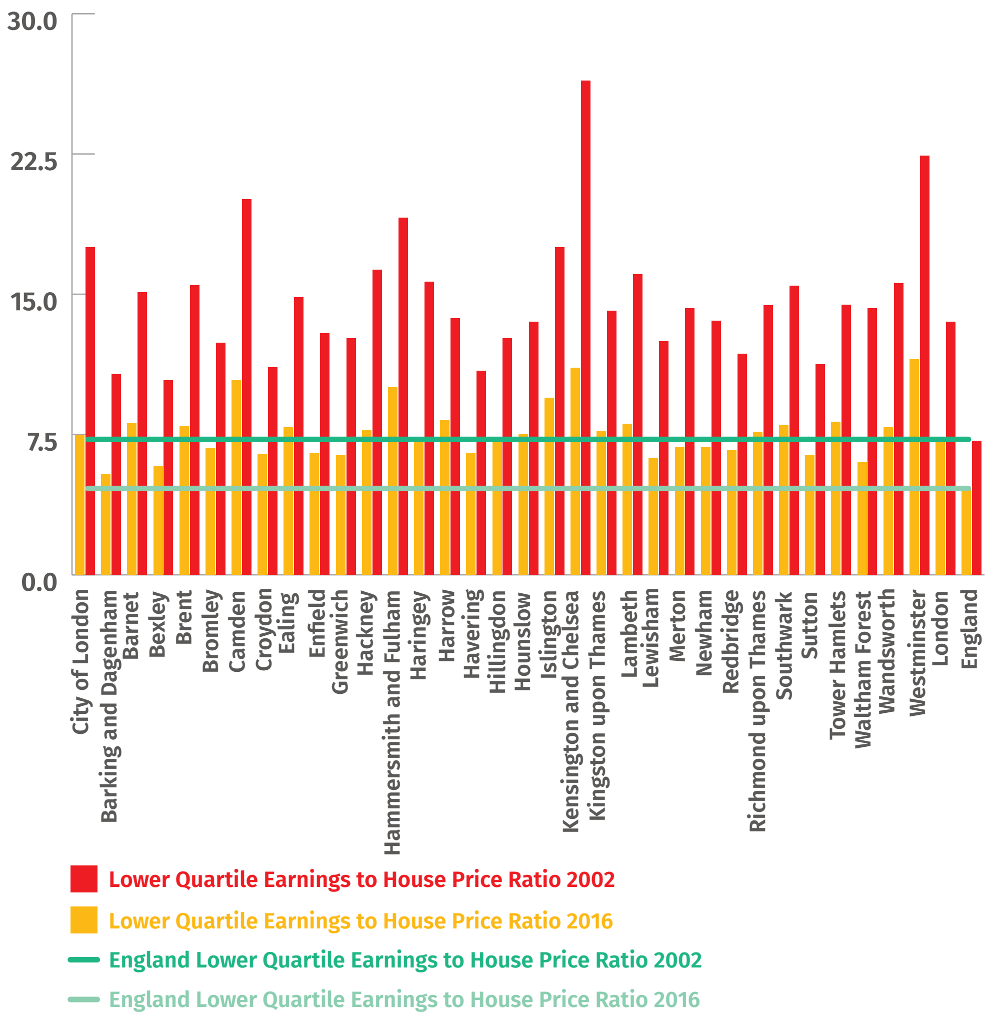
The current demand for homes and the gap in supply is greater in the capital than elsewhere in England, and the crisis of affordability has never been as acute as it is at present. The average house price in London is £483,000 according to Land Registry data (Land Registry 2017), which is 51 per cent higher than England as a whole. Moreover, since the turn of the century, the capital has experienced significantly higher increases in house prices than the national average and in any other region (ibid).

Furthermore, since 2005, rents in London have risen by 41 per cent compared with 24 per cent in the rest of England (excluding London) (ONS 2017a), while median earnings in London have risen by half as much (21 per cent) (ONS 2016a). At £1,495 per month, the median rent in London is 121 per cent higher than in England (£675), while lower quartile rent is 140 per cent higher in London than in England (£1,200 versus £500) (VOA 2017). This is even as rent inflation in the capital slowed in the past year, growing 0.6 per cent below the English average (ONS 2017c).

FIGURE 3.1

Lower quartile ratio of house prices to residence-based earnings in London and England, 2002 and 2016

The ratio of house prices to earnings has increased much faster in London than the rest of England



Source: ONS 2017a

The growing affordability challenge in London has seen the housing crisis spread up the income scale. Households on low to middle incomes are increasingly being squeezed out by the rising price of home ownership and private renting. According to a recent study by the Centre for London, there are now only three boroughs – Tower Hamlets, Newham, and Barking and Dagenham – where home ownership is affordable for two buyers on that borough's median. Moreover, if owner-occupiers on below median earnings were trying to purchase a home at today's prices, almost all of the capital's housing stock would be beyond their reach (Leadbeater et al 2014).

The long-standing shortfall in housing provision in London and rapidly rising house prices has had a big impact on the tenure mix within the capital. Driven by a sharp fall in mortgaged owners, home ownership has fallen to below 50 per cent of households in recent years – the first time owner-occupiers have been in the minority since the early 1980s (GLA 2017a). These tenure changes have particular intergenerational consequences. As the recent general election demonstrated, an intergenerational divide may be emerging, with housing inequality being one of the most visible drivers. Home ownership grew for households headed by those aged 65 or older; from 49 per cent in 1990 to 69 per cent in 2014. For those households headed by 16–24s and 25–34s, home ownership fell from 25 per cent to three per cent and from 57 per cent to 27 per cent respectively over the same period (ibid).

There has also been a fall in social rented housing, from 35 per cent of London's housing stock in 1981 to 23 per cent today. By contrast, the private rented sector has grown rapidly, nearly doubling in size from 15 per cent in 2000 to 28 per cent in 2016 (ibid). Over the next decade or so this trend is expected to continue, with recent tenure projections suggesting that less than two in five London households will own their own home (39.5 per cent) by 2025, an equal number of households will be renting privately and a fifth of households (21 per cent) will be in social housing (ibid).

What is affordable housing?

There is no statutory definition of affordable housing, although the government's housing white paper (DCLG 2017c) sets out the most recent proposed national definition of affordable housing (which will replace the current definition in the National Planning Policy Framework (NPPF)).

Definition of affordable housing in London

Within London, affordable housing is defined in the London Plan (GLA 2016d) as follows:

'Affordable housing is social rented, affordable rented and intermediate housing (see para 3.61), provided to eligible households whose needs are not met by the market. Eligibility is determined with regard to local incomes and local house prices. Affordable housing should include provisions to remain at an affordable price for future eligible households or for the subsidy to be recycled for alternative affordable housing provision.'

Within this overarching definition:

- '**Social rented housing** should meet the criteria outlined in Policy 3.10 and be owned by local authorities or private registered providers, for which guideline target rents are determined through the national rent regime. It may also be owned by other persons and provided under equivalent rental arrangements to the above, as agreed with the local authority or with the Mayor.'
- '**Affordable rented housing** should meet the criteria outlined in Policy 3.10 and be let by local authorities or private registered providers of social housing to households who are eligible for social rented housing. Affordable Rent is subject to rent controls that require a rent of no more than 80% of the local market rent (including service changes, where applicable)[1]. In practice, the rent required will vary for each scheme with levels set by agreement between developers, providers and the Mayor through his housing investment function. In respect of individual schemes not funded by the Mayor, the London boroughs will take the lead in conjunction with relevant stakeholders, including the Mayor as appropriate, but in all cases particular regard should be had to the availability of resources, the need to maximise provision and the principles set out in policies 3.11 and 3.12.'
- '**Intermediate housing** should meet the criteria outlined in Policy 3.10 and be homes available for sale or rent at a cost above social rent,

but below market levels. These can include shared equity (shared ownership and equity loans), other low cost homes for sale and intermediate rent, but not affordable rent. Households whose annual income is in the range £18,100–£66,000 should be eligible for new intermediate homes. For homes with more than two bedrooms, which are particularly suitable for families, the upper end of this eligibility range will be extended to £80,000. These figures will be updated annually in the London Plan Annual Monitoring Report.'

Within the most recent London Plan Annual Monitoring Report (2017), the Mayor has set out the upper limit of the income thresholds for intermediate housing:

'Therefore from April 2017 the costs, including service charges of intermediate ownership products such as London Shared Ownership and Discounted Market Sale (where they meet the NPPF and London Plan definition of affordable housing), should be affordable to households on incomes of £90,000 or less. From April 2017 the costs, including service charges for all intermediate rented products (including London Living Rent, Discounted Market Rent, Affordable Private Rent and Intermediate Rent) should be affordable to households on incomes of £60,000 or less.'

More broadly, the question of how affordable housing should be defined is contested because there is no official measure of affordability. The commonly accepted way of assessing upfront affordability is as a proportion of net household income (after taxes and benefits). Within this, the most widely accepted measure is a 35 per cent threshold of total household income (Bibby 2015), below which housing is considered to be affordable and above which it is deemed unaffordable – this is the measure we apply in this research, though we accept it is not applied universally.

For instance, the Mayor of London applies a measure of 40 per cent of net income to intermediate housing (GLA 2016c), while the Joseph Rowntree Foundation has devised the Minimum Income Standard (MIS) to determine the necessary income needed to maintain an adequate standard of living.[2] The other measure we apply in this report is a loan-to-income ratio (mortgage to household income) to ensure that where upfront costs are affordable under the 35 per cent net income cap, a household would actually be capable of getting a mortgage.

In truth, no measure is perfect because some households will always be willing to pay more than others and one might argue that those at the upper end of the income spectrum with greater levels of disposable income can more easily afford higher housing costs. In the capital this is particularly the case where Londoners pay a much higher proportion of their income on housing costs. Nevertheless, the measures we apply in this research provide a marker to effectively judge the affordable products against each other.

THE CASE FOR MORE AFFORDABLE HOUSING

As already outlined, the undersupply of housing is pushing up housing costs across the capital (LHC 2016). High housing costs make housing increasingly unaffordable and have a much wider impact on people's lives, including: how much people spend on other purchases such as food, clothing and travel; a

2 The Minimum Income Standard is calculated based on research with groups of members of the public specifying what items need to be included in a minimum household budget. See more here: http://www.lboro.ac.uk/research/crsp/mis/whatismis/

greater reliance on loans, and, for young people in particular, a need to rely on family relationships for housing support (LHC 2016; Pennington et al 2012). It is also driving up overcrowding (Children's Rights Wales 2013), homelessness and rough sleeping, which all increase the cost to the taxpayer, not least through a rising housing benefit bill. London councils are already seeing the cost of temporary accommodation rising across London with two-thirds of boroughs seeing gross costs rise by 33 per cent between 2012/13 and 2014/15, and overall expenditure estimated to be close to £663 million in 2014/15 (Rugg 2016).

Falling home ownership and social renting, housing undersupply and the resulting reliance on the private rented sector have wider implications. Analysis by the Resolution Foundation has shown that a quarter of households in the private rented sector are spending more than half of their income on rent (Resolution Foundation 2016). Moreover, the sector does not provide the same security or stability as other forms of tenure. IPPR analysis has shown that owning a home increases a person's connection and investment in a community (Pennington et al 2012). This has a particular impact on young people, whose sense of aspiration goes unfulfilled – stifling ambition, career goals and family plans as they put off having children in the absence of a secure home (ibid).

Moreover, those younger families which find themselves buying later in life are likely to take mortgage debt into retirement (Resolution Foundation 2017) and a greater number of households not managing to purchase their own home means more people will be subject to rent payments later in life (ibid). This will also have a potentially significant impact on future wealth inequality. From the mid-1990s to the mid-2000s, rising home ownership was the major driver of falling overall wealth inequality, but the recent rapid decline in owner-occupancy raises questions over the extent to which housing will continue its previous inequality-reducing role (ibid).

The housing crisis is also of critical concern to businesses. The Confederation of British Industry (CBI) has pointed to the lack of affordable housing as hindering firms' ability to recruit and retain talented staff (CBI 2016), with over two-thirds of respondents to the CBI/CBRE London Business Survey citing this as an issue (ibid). One survey has shown that nearly three-quarters of employers think London's housing supply and costs are a significant risk to the capital's economic growth (London First 2014). As a result, some employers are taking matters into their own hands, either supporting their employees in the private rented sector or seeking to build homes themselves (Long 2017).

These are all arguments for increasing housing supply overall and not just sub-market housing. However, even if London met or significantly exceeded its housing targets, Londoners would not feel an immediate impact in terms of improved affordability of housing, not least because building more homes in the capital will increase demand for housing by virtue of the fact that doing so will make housing more affordable (Bramley 2016). Moreover, as the Barker Review (HMT 2004) found for housing supply across England, even building more homes than currently required would still only see a modest impact on house price inflation.

Indeed, two of the crucial conclusions of the London Housing Commission were, firstly, that there is a need to build more homes over a sustained period of time to help contain rising house prices and, secondly, that focusing on numbers is not sufficient (LHC 2016). Delivering a variety of subsidised homes will be crucial to ensuring that those on low and middle incomes, including key service staff – such as care workers, nurses and firefighters – can continue to live in London.

The next section looks at London's record of delivering those products to support people on low to middle incomes and how well they support these groups.

4.
SUB-MARKET HOUSING: WHAT'S ON OFFER IN LONDON?

The Mayor has an annual target for the preferred tenure split of affordable homes on new developments, requiring that 30 per cent be provided at low-cost rent (social or affordable rent), 30 per cent intermediate (London Living Rent or London Shared Ownership) and 40 per cent decided locally by the local planning authority (GLA 2016b). However, there is no target for what affordable housing (or any other tenure) should be as a proportion of overall stock in London.

Table 4.1 sets out the range of affordable and subsidised products currently on offer, or proposed, in London. Despite the multitude of products on offer, the intermediate market only makes up a very small proportion of the affordable housing market at less than two per cent (HCA 2016), although social rented housing still provides a significant proportion at 23 per cent (DCLG 2017a). Moreover, as the case studies later in this chapter illustrate, innovation is beginning to take place within the intermediate market as charitable and private providers offer different types of models to their tenants.

TABLE 4.1

A summary of subsidised and sub-market housing options in London

Type	Overview	Allocation	Cost of rent / purchase	Current Stock
Social rent	Social rented housing tends to be owned by local authorities or other non-profit private registered providers (PRPs). Commercial organisations are now able to build and manage social housing. Normally funded through grant subsidy, they will remain affordable in perpetuity, except where properties are sold through the Right to Buy (RTB).	Local authorities set out their own allocations policies but legislation requires that they prioritise certain groups who are given 'reasonable preference'. These groups include those who have been made homeless, are in severely overcrowded conditions or are vulnerable on welfare grounds.	Rents are set locally and determined by several characteristics. These are principally related to local wages and costs of rented accommodation on the open market in the area. Rents are also adjusted by the number of bedrooms in a property.	Current stock is estimated at 764,000 (22.5% of overall stock in London) (DCLG 2017a)
London Affordable Rent (LAR)	LAR is let by local authorities or PRPs. The Affordable Rent product was introduced nationally in response to a reduction in the grant levels available for affordable housing. New homes for Affordable Rent are normally funded through grant subsidy and remain affordable in perpetuity, except where properties are sold through RTB.	Local authorities set out their own allocations policies but legislation requires that they prioritise certain groups who are given 'reasonable preference'. These groups include those who have been made homeless, are in severely overcrowded conditions or are vulnerable on welfare grounds.	Nationally Affordable Rent homes cannot be let at more than 80 per cent of market rents. In London, the Mayor does not consider 80 per cent of market rents to be genuinely affordable and therefore has set benchmarks substantially below this level.	Current stock is estimated at 22,383 units (<1%) (HCA 2016)

Affordable Private Rent (APR)	APR housing is a new product designed to suit Build to Rent Schemes. APR is funded through developer subsidy (Section 106) and it is intended that housing remains affordable in perpetuity or for alternative affordable housing provision to be made if the discount is withdrawn. It is intended that developers will provide APR directly in place of other affordable housing products.	To be eligible, households must have an income of £60,000 or less. Allocation locally determined according to local authorities.	Affordable private rented homes are let at 80% of the median market rent for private accommodation in an area or below.	No current stock
London Living Rent (LLR)	The London Living Rent is an intermediate housing product designed to support those on average incomes into home ownership. New homes for London Living Rent are normally funded through grant subsidy and will remain affordable in perpetuity.	To be eligible, households must have an income of £60,000 or less and intend to and be capable of saving for a deposit and entering home ownership within 10 years.	Rents are set at below market rents by each borough and are based on local wages and house prices. The overall cost of the rent must be 80% of the market rent or lower.	Current stock is in the 100s as LLR is a new product
Dolphin Personalised Rent (DPR)	The DPR scheme applies to the New Era estate in Hackney, inner London. The New Era estate was owned by a family who had kept rents low. When it was sold to a private firm tenants mounted a high-profile campaign to avoid unaffordable rent hikes. The housing charity Dolphin Living acquired the estate and worked with tenants to establish the new rent policy.	Scheme specific.	Rents are set based on tenants' incomes. If it is sufficiently above the Minimum Income Standard (MIS), devised by the Joseph Rowntree Foundation to determine the necessary income needed to maintain an adequate standard of living, the rent will be increased gradually over three years up to the housing benefit limit. If it is equal to or below the MIS then the rent will only be uprated at the level of CPI + 1%.	Circa 96 properties on the New Era estate
Intermediate Rent / Rent to Buy / Rent to Save	Rent to Buy is an intermediate housing model which aims to offer households discounted rent to allow them to save for a deposit towards the purchase of a home.	To be eligible, households must have an income of £60,000 or less. Allocation locally determined. To be eligible households must be able to realistically save for a home and not able to purchase a home on the open market. Tenants may purchase the home they reside within and must be offered first refusal on its sale.	Homes are rented at 80% of market value for up to 10 years at the end of which it is intended that the tenant will be able to purchase a home.	Circa 1,000 (CFL 2015)
Cheyne rent to buy	The Cheyne model is a private rent-to-buy product. New homes will be provided through developer subsidy (Section 106) but the subsidy will not remain in perpetuity or be recycled.	Will be locally determined but to be eligible households must be able to reasonably move into home ownership in five years.	Occupants rent a home at market rent for five years. The cost of purchasing the home is frozen at 90% of the property price at the beginning of the five years. At the end of the five-year period tenants are able to purchase the house at that fixed price, using the difference between that and the open market price as their deposit. If they cannot afford to buy at that point they will be reoffered the home every year and prices will increase by CPI.	No current stock

Shared ownership	Shared ownership is a model in which a household purchases a share of a property and rent the remaining amount from a housing provider. New homes for shared ownership are normally funded through grant subsidy and will remain affordable in perpetuity or the subsidy will be recycled.	To be eligible, households must have an income of £90,000 or less. Allocation is locally determined according to local authorities.	Shared owners may take out an initial stake of varying amounts, commonly 25%, 50% or 75%. They can also 'staircase' up or down, buying or selling stakes back to the housing provider. Shared owners tend to buy their equity with a 90% LTV mortgage. The rent for the remaining portion is set at a maximum of 3% of the unsold equity, although it is encouraged to be set at 2.75%.	Circa 46,000 (1.2%) (HCA 2016)
London Help to Buy	London Help to Buy is an equity loan scheme to aid first-time buyers in purchasing a home. Buyers must purchase newly built homes which are being marketed as within the Help to Buy scheme.	To access the scheme, individuals can be first-time buyers or homeowners looking to move and the property values are capped at £600,000.	Government provides a 40% equity loan. Buyers provide a minimum deposit of 5% and the remaining 55% of the property value is mortgaged. The equity loan is interest free for the first five years of the scheme and must be repaid on sale of the property.	7,476 sales (<1%) (DCLG 2017b)
Starter homes	A home ownership scheme funded through a mix of government and developer subsidy (Section 106). This subsidy will not be in perpetuity – although there will be a 15-year repayment period for a starter home so when the property is sold on to a new owner within this period, some or all of the discount is repaid.	To be eligible to purchase a starter home, a household's income must be below £80,000 (£90,000 in London).	Starter homes are priced at 80% of the local house price or less and are subject to an overall price cap of £450,000 in Greater London and £250,000 elsewhere in England.	No current stock
Pocket Living homes	Pocket Living homes are sold outright to eligible buyers at a discount. Pocket homes are more compact and are defined as 'intermediate affordable' housing. Pocket homes are designed to remain affordable in perpetuity.	To be eligible, applicants must earn less than £90,000 per year, currently live or work in the borough and be a first-time buyer.	Properties are sold at 80% of market value and created to be compact and well designed.	4,000 delivered over next 10 years (<1%)
Discounted market sale	Discounted market sale homes are those which are made available to households who would otherwise be unable to afford to purchase a home on the open market.	To be eligible, households must have an income of £90,000 or less. Discounted market sale housing is subject to income thresholds to determine eligibility. These thresholds are determined locally dependent on median incomes in the area.	Homes are discounted so as to be 80% or less than the market price in an area.	1,000 (CFL 2015)
Dolphin Westminster Accelerator	The Dolphin Westminster Home Ownership Accelerator is an intermediate housing model that aims to support those with some savings already to purchase homes in London. Provision of these homes is supported through grant from Westminster City Council. The subsidy is not held in perpetuity nor is it recycled.	To be eligible, the tenants must be working, earning enough to cover the rent without housing benefit and have savings of at least £22,500. Priority is given to those in social housing in Westminster.	Homes are rented at 65% of market rents for three years at which point households will move and purchase a home. Tenants are also given a grant of between £20,400 to £54,500 to help them to purchase a home anywhere in London.	100s

Case studies: alternative housing products in London

Innovative models offer a different approach to making products affordable to rent or offering routes into home ownership:

- **Cheyne – rent to buy model:** Cheyne Capital has developed a rent-to-buy product to assist first-time buyers onto the housing ladder, though it is not yet in operation. Tenants initially rent the property at open market rent and are responsible for the insurance, repair and maintenance. Annual rent increases are capped at consumer price inflation (CPI). At the end of the fifth year, and annually thereafter, the tenant has the right to purchase the property at 90 per cent of the market value of the unit as valued on the day they moved in. Through the 10 per cent discount on the original price and the accrual of the house price inflation (HPI) to the tenant over the initial five-year period, tenants are expected to receive a deposit of 25 per cent on average if they purchase after five years.

  If the tenant is unable to purchase in the fifth year, the tenant will continue to receive the benefit of house price inflation (in excess of CPI) and would have an annual opportunity to buy. Eligibility would be agreed with the local authority. The product, which is not yet operational, does not require a social housing grant but would need to be considered as affordable housing for planning purposes. Any developer subsidy would not be held in perpetuity or recycled after the first sale.

- **Dolphin Living – personalised rent model:** The discounted Personalised Rent scheme applies to the New Era estate in Hackney, inner London. The New Era estate was owned by a family who had kept rents low, but when it was sold to a private firm, tenants mounted a high-profile campaign to avoid unaffordable rent hikes. The housing charity Dolphin Living acquired the estate and worked with tenants to establish the new rent policy.

  Rents are set based on tenants' incomes. If a tenant's income is sufficiently above the Minimum Income Standard (MIS) as devised by the Joseph Rowntree Foundation then a tenant's rent will increase by consumer price inflation plus one per cent. However, as well as income, the formula to provide personalised rent also takes into account how many people comprise the household and their ages and needs. If, following this, it is considered that the household can afford to pay more rent, then there will be a gradual increase in rent (to avoid a difficult-to-manage large increase of CPI), plus 4.5 per cent each year until the new target level of rent is achieved. While this scheme is currently only in operation on the New Era estate, Dolphin has commissioned research which demonstrates the potential wider benefits of the scheme (Urwin et al 2016).

- **Pocket Living homes – starter home model:** Pocket Living provides a starter home model. Compact and well-designed one-bedroom properties are sold at 80 per cent of market value. To be eligible, applicants must earn less than £90,000 per year, currently live or work in the borough and be a first-time buyer. The discount provided to the buyer remains in perpetuity, with the seller passing the effective discount on to a new buyer. The average Pocket purchasing household earns just up to £40,000 a year (Hill 2016). Pocket Living was awarded a £21.7 million loan in 2013 by the Greater London Authority (GLA), which they have agreed to recycle over a period of 10 years, delivering 4,000 new homes across London.

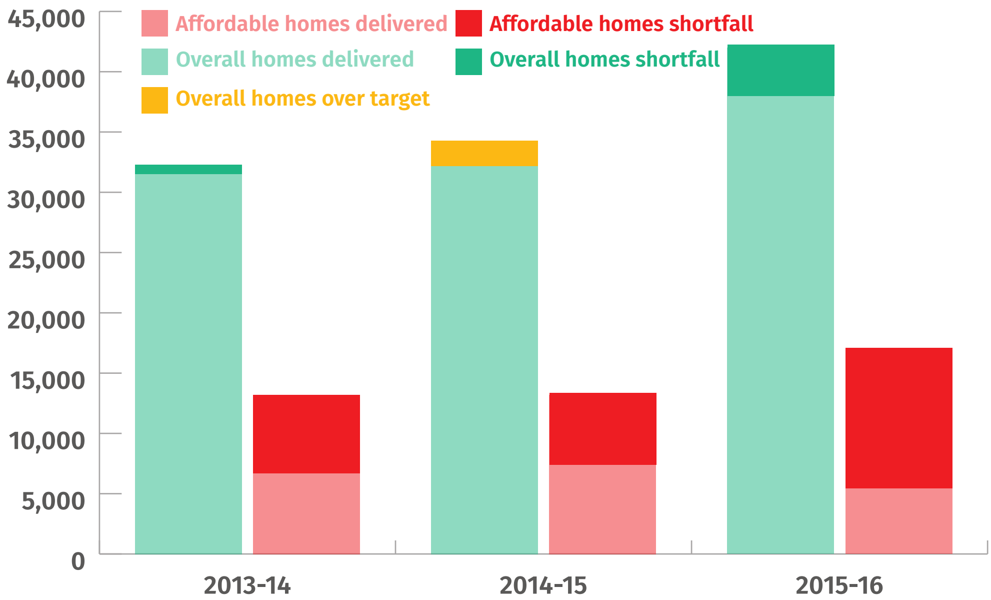
HOW MUCH NEW AFFORDABLE HOUSING IS BEING DELIVERED?

Over half of the annual housing requirement identified in London needs to be met by affordable housing, which is some 25,600 homes (20 per cent intermediate homes and 32 per cent for social or affordable rent) (GLA 2014b; GLA 2014a). However, the London Plan (GLA 2016d) only sought to ensure that an average of at least 17,000 additional affordable homes (net) are delivered each year. The London Plan target is measured in terms of net conventional supply, which includes supply from new developments or conversions, and then adjusted to take account of demolitions and other losses.

FIGURE 4.1

Delivery (net completions) against London-wide housing and affordable housing targets 2013–14 to 2015–16

The delivery of new homes and net additional affordable housing across London is well below the London Plan target



Source: (GLA 2017a)

It is clear that the delivery of net additional affordable housing across London falls significantly short of the London Plan target (50 per cent under target over three years). But the scale of delivery and the composition of affordable housing within overall net supply varies significantly across London boroughs. For instance, over the years 2012/13 to 2014/15, five boroughs delivered over 40 per cent affordable homes of total net conventional supply: Barking and Dagenham (45 per cent), Brent (40 per cent), Hackney (40 per cent), Haringey (54 per cent) and Havering (40 per cent). Four boroughs have delivered below 15 per cent: Bromley (one per cent), City of London (three per cent), Redbridge (nine per cent) and Westminster (12 per cent).

THE APPROACH OF CENTRAL GOVERNMENT AND THE MAYOR TO AFFORDABLE HOUSING

Over the past few years there has been a rapidly shifting policy landscape that is shaping the delivery of affordable housing in London and across the country. Most pertinent here are the changes made to affordable housing investment, planning policy and affordable housing obligations, and new affordable products and definitions.

Affordable housing investment

Overall investment in housing has been reduced significantly since 2010. Total housing expenditure (excluding housing benefit) fell from £12.6 billion in 2009/10 to £7.5 billion in 2014/15 with the share of government expenditure falling from 2.8 per cent to 1.6 per cent (CIH 2017). This reduction was largely driven by a 60 per cent cut to the affordable housing budget in 2010 by the coalition government (ibid).

The reduction in investment by the government saw funding on a per-home basis fall for the affordable homes programme 2015–18 in London by roughly 60 per cent compared with the previous Affordable Homes Programme (LHC 2016). More recently, last year's Autumn Statement confirmed the London affordable housing grant funding settlement for 2015–21. In return for £3.15 billion funding, London will deliver 90,000 affordable homes by 2021. This funding will deliver a mixture of low-cost rent, London Living Rent and London Shared Ownership schemes under the Mayor's Affordable Homes Programme.

While the overall sum at the Mayor's disposal for investing in affordable housing is not an inconsiderable amount, it will fall short of delivering the lower estimate (circa 25,000) of what is needed in the capital. Moreover, with the new housing needs assessment underway for the revised London Plan, it is likely that the estimate of need will only grow and the funding settlement will look even more insufficient.

Changes in planning policies

There have been significant changes to planning policies and affordable housing obligations that have had a material impact on the delivery of affordable homes since 2010. The implementation of the National Planning Policy Framework in 2012 saw the introduction of viability testing in local plans. This new test weighted assessments of planning proposals more significantly towards providing a 'competitive return to developers and landowners'. As a consequence, there has been a reduction in the number of affordable homes secured through Section 106 agreements, which is the dominant model used by 75 per cent of councils in delivering affordable housing (APSE and TCPA 2017).

In London, the Mayor has introduced the '35 per cent threshold approach' to affordable housing in new housing guidance which, broadly, waives the need for a viability assessment if a development provides for at least 35 per cent affordable homes (measured by habitable rooms). The intention of this proposal is to set a new benchmark for the proportion of affordable homes delivered in each development to drive up supply. Moreover, the Mayor has also signalled that his long-term strategic aim is to make half of all new homes in London affordable by investing more in affordable housing, bringing forward more public land for affordable homes and increasing the amount of affordable housing delivered through the planning system. The new London Plan currently being developed will incorporate the Mayor's long-term strategic aim of delivering 50 per cent affordable housing. A consultation draft of the new London Plan will be published in autumn 2017.

Redefining affordable housing, introducing new products and subsidised schemes

In 2010, driven by the large cuts made to affordable housing subsidy, the government delivered a new model of affordable housing called affordable rent, to be let at 80 per cent of market rents; a significant shift from funding social housing, which is linked to incomes. This product is particularly problematic in London, which is why the Mayor has set rent benchmarks well below the upper limit.

Moreover, although promoting ownership for first-time buyers has had cross-party support since the 1990s (SMB 2017), one of the most marked shifts in policy in recent years has been the increase in support for home ownership products in particular. The largest government intervention outside the affordable housing system has been in the form of the Help to Buy equity loan scheme. This scheme provides a 40 per cent interest-free loan to eligible buyers (both first-time buyers and home-movers) who have a five per cent deposit to buy a new-build home in London.

Within the affordable housing system, the government has also taken a number of other steps. These include the proposals to extend the Right to Buy to housing association tenants paid for by the sell-off of high-value council homes – the former enacted by a voluntary agreement (NHF 2015) with the National Housing Federation (the representative body of housing associations) and the latter in the Housing and Planning Act 2016.

The government is also, according to the housing white paper (DCLG 2017c), still planning on introducing starter homes first committed to in the Conservative Party Manifesto in 2015. Starter homes would be priced at a 20 per cent discount to market price with a cap of £450,000 in London for eligible buyers (see Table 4.1 for more detail). However, starter homes have come in for strong criticism since they were proposed, the main criticisms being that they would not be affordable to people on low to middle incomes (particularly in London), that they would force the replacement of genuinely affordable homes and that the subsidy provided for them would be lost and not recycled for future affordable housing. As a result, these proposals have been considerably amended since they were first announced in that they will no longer be mandatory to include in all developments, there will be far greater discretion at a local level and the subsidy will be recovered over a longer time period. Having been watered down, there is now considerable doubt as to whether starter homes will ever be delivered on a scale of any significance.

Significantly in London, the new product introduced by the Mayor is an intermediate rent product, rather than one designed specifically for home ownership. The London Living Rent is aimed at those above low incomes living and working in the capital (see Table 4.1 for detail). Although the final implementation of the policy has seen the addition of a shared ownership element, it is perhaps a recognition of the need to provide products to rent as well as to buy for those on low to middle incomes, as recommended in a recent report by Centre for London (2015).

HOW EFFECTIVE IS SUB-MARKET HOUSING?

There has been considerable debate and analysis of the affordability and effectiveness of sub-market housing in London. Research by the London School of Economics (2011) points to the benefits of investing in and delivering social rented housing in terms of alleviating and addressing the costs of poor housing such as homelessness, living in temporary accommodation and overcrowding. Social housing requires high levels of subsidy, particularly in London, but the evidence has shown that it is an exceptionally effective means of reducing housing costs. Recent research has shown that social rented housing is highly targeted at people with low income and is the most 'pro-poor' and redistributive significant feature of the whole welfare state (JRF 2013).

Low-cost home ownership products supported by government have also been extensively reviewed and evaluated (SMB 2017). Research has shown that the Help to Buy equity loan scheme is not expanding home ownership to lower income households that are otherwise unable to buy, but is instead assisting households who would be able to buy at some point without support (ibid). A report by the Resolution Foundation similarly found that while Help to Buy reduces the time it takes to save for a deposit, the monthly mortgage costs remain unaffordable for those on low to middle incomes, particularly in London (Resolution Foundation 2013). The Right to Buy (which we do not include in our assessment here as this report focuses on new-build products), which offers council and some housing association tenants the chance to buy their own home, has been the most successful scheme in terms of enabling home ownership, helping 1.8 million households move into home ownership (SMB 2017). However, questions have been raised about the value of public money given the high level of subsidies to build the properties in the first place and the fact that a substantial amount of stock has never been replaced (ibid).

Shared ownership has generally been seen as more effective at supporting those on low to middle incomes into home ownership (ibid) and has been mooted as a so-called 'fourth tenure' (ibid). However, the tenure has failed to increase as expected and within London remains a little over one per cent of housing stock (HCA 2016). Three central issues have been found with shared ownership: firstly, the legal complexity, regulations and restrictions which make the tenure difficult to navigate and understand (Resolution Foundation 2013); secondly, the service provided by landlords, responsibility for repairs and service charges, and, finally, the lack of shared owners who scale up into full ownership. The latter is largely due to the costs of buying additional shares and house prices rising faster than wages – between 2001 and 2012 only 19 per cent of households had staircased to full ownership (Clarke and Heywood 2012). In high-value areas of London, while buyers are able to service a mortgage on the minimum 25 per cent share and cover the rent, the high costs leave them struggling to staircase into full ownership or move in future. There is also an inadequate return for many housing associations investing in the product (CIH 2016).

It is too soon to determine whether starter homes and London Living Rent homes are effective in achieving their aims. However, a review of the starter homes scheme proposals by the housing charity Shelter found that they will not help the majority of people on the new National Living Wage or average wages (or even many earning above average wages) into home ownership in England by 2020 (Shelter 2015). It found that London has the lowest number of areas where affordable starter homes under the scheme's threshold could be built. The development of the London Living Rent programme is a significant step forward in terms of recent policy because it links rents to incomes, though it is not aimed at those on the lowest incomes. Research by UK planning and development consultancy Lichfields on the London Living Rent found that it is predominantly focused at the higher end of intermediate housing products (Lichfields 2017).

WHAT PRODUCTS ARE AFFORDABLE IN LONDON?

To establish the affordability of each type of sub-market and subsidised product on offer in London, we have modelled the costs of monthly payments on each using a mixture of house price data, private rents, social rents and rent benchmarks at a London-wide level and at a London borough level. These monthly housing costs have then been calculated as a percentage of net household income at a variety of different household income levels.[3] As set out earlier, we have used a net income cap of 35 per cent to determine whether a particular product is 'affordable'.

We have utilised a number of household examples at different points on the income scale in order to illustrate the affordability of each product.

3 See Annex for the assumptions used in this analysis.

TABLE 4.2

Household examples

Household type	Earnings
Single person working full time	One person on full-time earnings
Couple with one child with one person working full time and one person working part time	One person on full-time earnings + one person on part-time earnings + child benefit
Couple both working full time	Two people on full-time earnings

Source: ONS 2016b

There are a number of assumptions applied to each model, which are set out in more detail in the Annex. While alternative assumptions could be employed, the research utilises a reasonable and balanced approach to demonstrate the affordability of the variety of affordable housing products against a range of household incomes.

LONDON-WIDE ANALYSIS

In the London-wide analysis set out in the following three tables, the upfront affordability of each product is measured against a 35 per cent net income cap. However, just because certain households might be able to 'afford' these products under this measure, they might not be eligible for a mortgage.

Therefore, for the home ownership products, we have also applied a loan-to-income ratio of 3.5:1 to ensure that it was realistic that each household could access a mortgage. In some instances, the costs of a particular home ownership product might come under the 35 per cent net income target but they may still be ineligible for a mortgage as the following analysis demonstrates. For the rent-to-buy products (Rent to Buy, Cheyne rent to buy and London Living Rent), the analysis has been conducted on the monthly rent and therefore the costs in the research do not represent the costs of purchasing the homes. However, the question of whether a sufficient mortgage might be attainable if a sufficient deposit has been raised is modelled.

Key	
Colour	Housing costs as a % of net income
Red	Unaffordable under a 35% net income cap
Green	Affordable under a 35% net income cap
Amber	Affordable under a 35% income cap but above 3.5:1 loan (mortgage)-to-income ratio

TABLE 4.3

Affordability against a 35 per cent income target for a single person working full time (one person on full-time earnings across a range of deciles)

Model	10th	20th	25th	50th	75th	80th	90th
Annual Gross Earnings	£18,023	£22,027	£23,920	£32,885	£47,315	£51,324	£68,770*
Social Rent	39%	33%	31%	24%	17%	16%	13%
London Affordable Rent (Benchmarks)	51%	43%	41%	31%	23%	21%	17%
London Living Rent	75%	64%	59%	45%	33%	31%	24%
Affordable Private Rent	92%	79%	73%	56%	41%	38%	30%
Lower Quartile Rent	93%	79%	74%	56%	41%	38%	30%
Median Rent	115%	98%	92%	70%	51%	48%	38%
London Help to Buy	86%	73%	68%	52%	38%	36%	28%
Rent to Buy	92%	79%	73%	56%	41%	38%	30%
Shared Ownership	102%	87%	81%	62%	45%	42%	33%
Cheyne Rent to Buy Model	115%	98%	92%	70%	51%	48%	38%
Starter Homes	118%	100%	94%	71%	52%	49%	38%
First-Time Buyer Price	147%	125%	117%	89%	65%	61%	48%
Median House Price	169%	144%	135%	103%	75%	70%	55%

***This is above the £60,000 threshold set out by the London Mayor for intermediate products for rent in London, e.g. London Living Rent, discounted market rent, Affordable Private Rent and intermediate rent**

- With the exception of social rent and London Affordable Rent nearly all forms of tenure and intermediate products are unaffordable for a single purchaser except at the very highest income levels.
- Even the new London Living Rent only becomes affordable to someone at the upper quartile.
- In terms of home ownership products, London Help to Buy and London Shared Ownership are affordable to a single person earning in the top income decile.

TABLE 4.4

Affordability against a 35 per cent income target for a couple with one child (one person on full-time earnings + one person on part-time earnings + child benefit across a range of deciles)

Model	10th	20th	25th	50th	75th	80th	90th
Annual Gross Earnings	£21,315	£27,461	£30,118	£42,401	£62,140*	£68,182*	£92,300**
Social Rent	30%	25%	23%	17%	12%	11%	9%
London Affordable Rent	40%	32%	30%	22%	16%	15%	12%
London Living Rent	58%	47%	43%	32%	23%	22%	17%
Affordable Private Rent	72%	58%	54%	40%	29%	27%	21%
Lower Quartile Rent	72%	58%	54%	40%	29%	27%	21%
Median Rent	90%	72%	67%	50%	36%	34%	26%
London Help to Buy	67%	54%	50%	37%	27%	25%	20%
Rent to Buy	72%	58%	54%	40%	29%	27%	21%
Shared Ownership	80%	64%	59%	44%	32%	30%	23%
Cheyne Rent to Buy Model	90%	72%	67%	50%	36%	34%	26%
Starter Homes	92%	74%	68%	51%	37%	34%	27%
First-Time Buyer Price	115%	92%	85%	63%	46%	43%	34%
Median House Price	132%	106%	98%	73%	53%	49%	39%

* This is above the £60,000 threshold set out by the London Mayor for intermediate products for rent in London, e.g. London Living Rent, discounted market rent, Affordable Private Rent and intermediate rent
** This is above the £90,000 threshold set out by the London Mayor for intermediate ownership products in London, e.g. shared ownership and discounted market sale

- The London Living Rent becomes affordable much earlier to a couple earning approximately £40,000 a year.
- Renting in the private rented sector even at lower quartile rents isn't affordable until earnings are over £50,000 a year but median rent remains unaffordable until earnings are well over £60,000 a year.
- In terms of home ownership products, shared ownership becomes affordable at earnings over £60,000 a year. At earnings of nearly £70,000 a year, Cheyne and starter homes become affordable in terms of upfront costs but buyers may be unable to get a mortgage. First-time buyer house prices are not deemed affordable until the ninth decile but even then a household may not be able to get a mortgage and a home priced at the median remains out of reach.

TABLE 4.5

Affordability against a 35 per cent income target for a couple both working full time (two people on full-time earnings across a range of deciles)

Model	10th	20th	25th	50th	75th	80th	90th
Annual Gross Earnings	£36,046	£44,054	£47,840	£65,770*	£94,630**	£102,648**	£137,540**
Social Rent	20%	17%	16%	12%	9%	8%	6%
London Affordable Rent	26%	22%	20%	15%	11%	11%	8%
London Living Rent	37%	32%	30%	23%	16%	15%	12%
Affordable Private Rent	46%	39%	37%	28%	20%	19%	15%
Lower Quartile Rent	46%	39%	37%	28%	20%	19%	15%
Median Rent	58%	49%	46%	35%	25%	24%	19%
London Help to Buy	43%	37%	34%	26%	19%	18%	14%
Rent to Buy	46%	39%	37%	28%	20%	19%	15%
Shared Ownership	51%	43%	40%	31%	22%	21%	17%
Cheyne Rent to Buy Model	58%	49%	46%	35%	25%	24%	19%
Starter Homes	59%	50%	47%	36%	26%	24%	19%
First-Time Buyer Price	74%	63%	59%	45%	32%	30%	24%
Median House Price	85%	72%	67%	51%	37%	35%	28%

*** This is above the £60,000 threshold set out by the London Mayor for intermediate products for rent in London, e.g. London Living Rent, discounted market rent, Affordable Private Rent and intermediate rent**
**** This is above the £90,000 threshold set out by the London Mayor for intermediate ownership products in London, e.g. shared ownership and discounted market sale**

- A couple working full time brings far more housing within reach but it remains unaffordable for those on lower incomes.
- The London Living Rent product becomes affordable with joint earnings of around £44,000, while renting at lower quartile rents and affordable private rents becomes affordable to those earning around £50,000 a year, although median rents aren't affordable until earnings are of around £65,000.
- Shared ownership becomes affordable at annual earnings of £66,000 and Help to Buy at over £90,000, once the ability of the household to get a mortgage is factored in. Buying at first-time buyer prices doesn't become affordable until household income is above around £100,000.

LONDON BOROUGH ANALYSIS

In the London borough analysis set out in Table 4.6, we consider the number of London boroughs where each product is affordable against a 35 per cent net income cap and applying a loan-to-income ratio of 3.5:1.

TABLE 4.6

Affordability of sub-market housing models at 35 per cent of net income by London borough and a 3.5:1 loan (mortgage)-to-income ratio

Most home ownership products are out of reach in the vast majority of London's 33 boroughs, apart from for a couple with one child both earning in the upper quartile or for two full-time earners both earning median/upper quartile salaries

		Single person			Couple with one child			Couple		
		LQ	Median	UQ	LQ	Median	UQ	LQ	Median	UQ
		£23,920	£32,885	£47,315	£30,118	£42,401	£62,140*	£47,840	£65,770*	£94,630**
Rental	Median rent	0	0	2	0	2	18	2	18	30
	Social Rent	32	33	33	33	33	33	33	33	33
	Affordable Private Rent	0	0	10	0	9	27	18	30	32
	London Affordable Rent	0	32	33	32	33	33	33	33	33
Rent to Buy / Shared Ownership	Rent to Buy	0	0	10 (0)	0	9 (0)	27 (1)	18 (1)	30 (0)	32 (13)
	London Living Rent	0	0	23 (0)	1	28 (0)	31 (1)	28 (0)	33 (0)	33 (13)
	Cheyne Rent to Buy Model	0	0	2 (0)	0	2 (0)	18 (13)	0	18 (4)	30 (24)
	Shared ownership	0	0	11	0	6	24	13	28	31
Ownership	First-Time Buyer Price	0	0	0	0	0	1	0	0	13
	Starter Homes	0	0	0	0	0	5	0	5	23
	London Help to Buy	0	0	6	0	1	14	0	18	28

* This is above the £60,000 threshold set out by the London Mayor for intermediate products for rent in London, e.g. London Living Rent, discounted market rent, Affordable Private Rent and intermediate rent

** This is above the £90,000 threshold set out by the London Mayor for intermediate ownership products in London, e.g. shared ownership and discounted market sale

Note: For the rent-to-buy models, two figures are given. One is for the number of boroughs the product is affordable in based on the affordability of the rent payment at a 35 per cent income cap. The second figure in brackets denotes the number of boroughs where the salaries being earned would enable the household to get a mortgage under a 3.5:1 loan (mortgage)-to-income ratio and the assumed deposit levels for each model (as set out in the Annex).

As Table 4.6 shows, there are few options for those on lower quartile incomes, with only social rent and London Affordable Rent catering for most household types across London. London Living Rent is affordable to couples and Rent to Buy in terms of the rent, but buying those properties would still be unaffordable in most areas. Shared ownership is affordable for a couple both of whom work full time on lower quartile earnings in just over a third of boroughs.

For those on median incomes, a greater number of the home ownership products open up in terms of upfront costs but fewer allow transitioning into home ownership due to the ratio between house prices and earnings and their likely inability to get a mortgage. Shared ownership allows a couple with one child to get on the housing ladder in a handful of boroughs and a couple to do so in 28 of the 33 London boroughs. However, a greater share of their properties through staircasing would be beyond the reach of many households who buy the minimum share (25 per cent) modelled here due to the additional costs – this explains why so few people staircase to full ownership. London Help to Buy also allows a couple both working full time and earning median salaries to be able to purchase a home in just over half of London boroughs.

For those on higher incomes, a greater range of home ownership products become affordable, but, with the exception of shared ownership, transitioning into home ownership is only viable in a handful of boroughs for a couple with one child. For a couple on higher earnings, the Cheyne, Help to Buy and starter homes/discounted market sale products become realistic options for purchasing a home.

RENT-TO-BUY MODELS

The analysis below considers the number of London boroughs in which the rent-to-buy ownership models effectively enable households to successfully raise a deposit.

TABLE 4.7

Number of London boroughs where a household can successfully raise a deposit through rent-to-buy schemes

The existing rent-to-buy schemes perform poorly in raising a deposit for outright home ownership, except London Living Rent over a 10-year period

Model	Number of London boroughs where a sufficient deposit can be raised for purchase (10%)			
	Full Ownership		Shared Ownership	
	5 Years	10 Years	5 Years	10 Years
Rent to Buy	0	0	33	33
London Living Rent	1	24	33	33
Cheyne Rent to Buy Model	33	33	N/A	N/A

As Table 4.7 shows, the performance of the existing rent-to-buy models in enabling households to save for a deposit is mixed.

In terms of outright ownership, Rent to Buy, which offers a discounted rent of 80 per cent of market rate, would not enable a household saving the difference between market rent and the rent they were paying to accrue a deposit over a five- or a 10-year period. London Living Rent would provide the opportunity of raising a deposit over a five-year period in one borough only but performs far better over a 10-year period, allowing a deposit to be saved in more than two-thirds of London boroughs. The Cheyne model would enable a household to save for a deposit successfully in all London boroughs over both a five- and a 10-year period.

Both Rent to Buy and London Living Rent models would enable households to raise a deposit for a shared ownership home in all London boroughs. This is because raising a 10 per cent deposit for a 25 per cent stake in a shared ownership property significantly lowers the threshold. In all cases, households could be restricted from purchasing a home outright in a number of London boroughs by their inability to get a mortgage as set out in the previous analysis.

5. CONCLUSION AND RECOMMENDATIONS

There is an array of affordable housing and subsidised housing products available for people on a range of incomes within London. Social rent and London Affordable Rent (at the new benchmark rent levels set by the Mayor) are the only products that serve those on the lowest incomes across the capital. It is essential that investment in these rented products remains consistent or is increased in order that housing is provided in London for those most in need. Any policies to boost intermediate housing must not come at the expense of genuinely affordable social rented housing.

However, since the turn of the century there has been a sharp decline in home ownership in London and a rapid increase in households living in the private rented sector. This is particularly marked among low to middle income earners who would have previously bought their own home. The unaffordability of home ownership, both in terms of the upfront costs of saving for a deposit and the ongoing costs through monthly mortgage payments, has stopped many people staying in London. Within this context, it is hardly surprising that successive governments have focused on providing low-cost home ownership and subsidised schemes to lower the barriers to owner-occupancy both inside and outside the capital.

However, the evidence presented in this report demonstrates that the overall proportion of low-cost and subsidised home ownership products remains extremely small. Moreover, there are also questions about the affordability of these products for those at which they are targeted, as well as the effectiveness of these options in scaling up into home ownership. In addition, some of the evidence suggests that subsidised products, like the Help to Buy equity loan scheme, are benefitting those who are able to afford a home without support. Despite being the best performing product across a range of income groups, shared ownership is increasingly difficult to stack up in high-value London areas, with few buyers being able to afford to staircase into full ownership and housing associations increasingly unwilling to invest due to the returns (CIH 2016).

This does not mean that supporting people to meet their aspiration to buy their own home is an impossible task. However, there should be a constant review of the affordability of products on the market and their effectiveness in achieving their aims and how they could be improved. Consideration should be given to innovative products that might offer new rented options that are affordable to people on low to middle incomes and home ownership products that might help them into buying their own home.

In response, we recommend a focus on four areas.

1. DEVOLVED FUNDING AND INCREASED INVESTMENT

The deal to secure £3.15 billion of devolved funding in affordable housing spend for the Mayor to build 90,000 homes was a major step forward, but, as set out in this report, it will not be enough to support the minimum number of affordable homes (25,000) needed in the capital each year. In the short term, the government should consider boosting the capital subsidy to the Mayor in order to increase the number of affordable homes that can be built in London. However, in the medium to long term, the capital grant should be gradually replaced in exchange for additional devolved powers for the Mayor to set and retain property taxes in the capital as recommended by the London Housing Commission (2016). This should include the devolution of Stamp Duty – the revenue from new-build homes in particular would be a strong incentive for local authorities to build more homes in their area.

The government should also free up local authorities to invest and build more affordable homes by removing the cap on the housing revenue account which prevents many local authorities from borrowing prudently against long-term rental streams to invest in affordable housing.

2. A CLEAR MEASURE OF AFFORDABILITY – AND MAPPING THE AFFORDABILITY OF SUB-MARKET HOUSING PRODUCTS

Recent changes by central government to affordable housing have driven a rapid change in what is understood as 'affordable'. Increasingly, affordable housing products have become divorced from earnings and linked to market prices or rents instead. The generally understood definition of affordable housing, of 35 per cent of net earnings, is rarely applied to new affordable housing products. The Mayor has made a promising start by introducing the London Living Rent, which is linked to earnings, and there is a 40 per cent net income target for intermediate housing in London. However, there is a need for a universally understood affordability measure, linked to earnings, that should be developed and agreed for London and applied transparently for every affordable housing product – with the development of an affordability matrix that sets out when each product becomes affordable. This is particularly necessary for affordable home ownership products, many of which this report has found perform poorly in terms of affordability but also helping people into full ownership.

3. CLEAR TARGETING OF SUBSIDY TO MEET STATED AIMS

This research has demonstrated that many home ownership products designed to help people on lower to middle incomes in to home ownership are only affordable in a large number of cases to those on higher incomes. Moreover, the evidence suggests that many products are assisting those who would have been able to buy anyway. Subsidy should be targeted at those products which are clearly affordable, and it should be withdrawn from products that do not meet the need of those for whom they are designed to assist. This should include London Help to Buy, the funding for which should be placed under the control of the London Mayor to direct as they see fit.

4. SUPPORT OF INNOVATION AND ENCOURAGEMENT OF THE DEVELOPMENT OF ALTERNATIVE AFFORDABLE HOUSING MODELS

There are clear examples of innovation outside the traditional products within affordable housing, some of which are highlighted in this report. The government and the Mayor should consider how new and innovative products might contribute to meeting the capital's affordable housing need. It will also be essential to consider other alternative delivery models. The Conservative Party Manifesto at the general election set out bold plans for new council housing deals, which included the reform of compulsory purchase orders to make them easier and less expensive for councils to use, and to enable them to buy land at a lower value. The Mayor and London boroughs should pursue the devolution and implementation of such powers from central government, which would allow affordable housing to be funded at lower costs, ensuring more affordable housing to rent or buy and greater potential benefits for local communities. This model of delivery would also allow greater innovation in the type of affordable products delivered.

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ANNEX

To understand how affordable each affordable housing product is, we compared the affordability of each product to rent and to buy against a 35 per cent of net income target. For each product to buy, we also applied a loan-to-income ratio of 3.5:1 to ensure it was realistic that each household could access a mortgage.

OWNERSHIP MODELS

House prices

Median house price: The median house price used in the affordability modelling was based on Land Registry data (ONS 2017b) using third quarter of 2016 data.

First-time buyer price and house price used in the modelling for each home ownership product: The first-time buyer price and the house prices used for each home ownership product have been based on a modelled first-time buyer price for across London and in each local authority. Median first-time buyer prices are not available at the borough level. The average ratio of the all-property price available from Nationwide House Price Index compared with the first-time buyer price was calculated over four quarters (third and fourth quarter of 2016 and first and second quarter of 2017) (Nationwide 2017a, 2017b) and then applied to the median house price figure for London and every London borough available from ONS data (ONS 2017b) using third quarter of 2016 data. There is likely to be some variation of first-time buyer prices in London which the ratio will not sufficiently account for – however the ratio has been applied to the starting price for each home ownership product and therefore impacts each one in the same way.

Mortgage, deposit and rent calculations

Outright ownership (median house price and first-time buyer price): The mortgage costs are calculated assuming a 90 per cent loan-to-value (LTV) mortgage over 25 years with an annual interest rate of 3.34 per cent APR.[4] It is assumed that each buyer can provide a 10 per cent deposit of the value of the property.

London Help to Buy: The mortgage costs are calculated assuming a 55 per cent LTV mortgage over 25 years with an annual interest rate of 3.34 per cent APR. It is assumed that each buyer provides the minimum five per cent deposit of the value of the property and takes out a Help to Buy equity loan of 40 per cent. Equity loans through Help to Buy are fee free for the first five years, and these calculations have not included the fee which is levied from the sixth year. The fee is 1.75 per cent of the loan's value in the sixth year and then increases every year according to the Retail Prices Index plus one per cent. The value of the property against which these calculations are made is the modelled first-time buyer price, set out above, at the London level and the borough level.

Starter homes and discounted market sale: The mortgage costs are calculated assuming a 90 per cent LTV mortgage over 25 years with an annual interest rate of 3.34 per cent APR. It is assumed that each buyer can provide a 10 per cent deposit of the value of the property. The value of the property against which these calculations are made is the modelled first-time buyer price, set out above, at the London level and the borough level, with the 20 per cent discount applied on top.

4 Based on the current UK average mortgage rate available at http://www.totallymoney.com/mortgages/rate-predictions/

Shared ownership: Shared ownership costs are calculated based on a household taking out a 25 per cent stake in their property with a 90 per cent LTV mortgage over 25 years with an annual interest rate of 3.34 per cent APR. It is assumed that each buyer can provide a 10 per cent deposit of the value of the stake of the property being purchased (25 per cent). Average national service charge costs (£93.58) are added to the monthly cost.[5] The value of the property against which these calculations are made is the modelled first-time buyer price, set out above, at the London level and the borough level.

Cheyne model: As with all of the rent-to-buy models, the monthly costs are calculated based on the rental costs (i.e. those needed to first access the property) rather than the potential mortgage costs if the household were to purchase the property. For the Cheyne model, the rental costs used are the monthly median private rent of a two-bedroom property in London or in each London borough (VOA 2017).

For the purposes of the loan-to-income calculation, it is assumed that each buyer will access a 75 per cent LTV mortgage providing a 25 per cent deposit of the value of the property based on the average deposit that can be saved through the Cheyne model.[6]

Rent to Buy: As with all of the rent-to-buy models, the monthly costs are calculated based on the rental costs (i.e. those needed to first access the property) rather than the potential mortgage costs if the household were to purchase the property. For the Rent to Buy model, the rental costs used are 80 per cent of the monthly median private rent of a two-bedroom property in London or in each London borough (VOA 2017).

For the purposes of the loan-to-income calculation, it is assumed that each buyer will access a 90 per cent LTV mortgage providing a 10 per cent deposit of the value of the property – however, as outlined in the analysis, it would not be possible in most cases for the deposit to be raised through saving the difference between the discounted rent and the market rent alone.

Loan-to-income ratio

To calculate whether a household would actually be able to attain a mortgage, we have used a standard loan-to-income ratio of 3.5:1. For each product, the loan value used in this calculation depends on the assumptions set out for each model above.

RENTAL MODELS

Social rent: The rental costs used are an average of the local authority average weekly rents (DCLG 2017d) and private registered provider weekly rents (DCLG 2017e) for London and for each London borough.

London Affordable Rent: The rental costs used are based on the London Affordable Rent benchmarks for 2017–18 provided by the Mayor of London (2016).

London Living Rent: The rental costs used are a simple London-wide or borough average of the London Living Rent ward benchmark data provided by the Mayor of London (2017) for two-bedroom properties.

Affordable Private Rent: The rental costs used are 80 per cent of the monthly median private rent of a two-bedroom property in London or in each London borough (VOA 2017).

5 Based on a market study by the Competition & Markets Authority available at https://assets.publishing.service.gov.uk/media/547d99b8e5274a42900001e1/Property_management_market_study.pdf

6 IPPR analysis of information provided by Cheyne.

Lower quartile rent: The rental costs used are the monthly lower quartile private rent of a two-bedroom property in London or in each London borough (VOA 2017).

Median rent: The rental costs used are the monthly median private rent of a two-bedroom property in London or in each London borough (VOA 2017).

DEPOSIT MODELLING

For the purpose of modelling how much could be saved for a deposit, a calculation was made for each model based on what could be saved for each year over a five-year and then a 10-year period.

Rent to Buy: Rent levels are assumed to be 80 per cent of median rent for a two-bedroom property, with households saving the difference between that and the market rate over a five-year and then a 10-year period.

London Living Rent: The rental costs used are a simple London-wide or borough average of the Living Rent ward benchmark data provided by the Mayor of London (2017) for two-bedroom properties, with households saving the difference between that and the market rate over a five-year and then a 10-year period.

Cheyne rent to buy: It is assumed that at the end of the fifth year, households are able to purchase the property at 90 per cent of its original value (providing an automatic deposit of 10 per cent), with the value of the house price inflation (HPI) over that period added to the discount. At the end of the 10th year, it is assumed that households are able to purchase a property at its original value plus five years of consumer price inflation (CPI), again with the value of the house price inflation over that period added to the discount.

We make the following assumptions about HPI, rent and CPI increases:

Annual house price inflation: five per cent

Annual private rent inflation: three per cent

London Living Rent increase: 1.5 per cent (CPI)

Rent to buy rent increase: 2.5 per cent (CPI + 1)

INCOME

TABLE A.1

For the affordability analysis, three household types were used:

Household type	Earnings
A single person working full time	Full-time earnings for all employees (ONS 2016b)
A couple with one child, with one person working full time and one person working part time	Full-time earnings for all employees + part-time earning for all employees + child benefit for one child (ONS 2016b)
A couple both working full time	Full-time earnings for all employees x 2 (ONS 2016b)

For the London borough analysis, median salaries at the borough were used but London-wide figures were used at the lower quartile and upper quartile levels due to gaps in data.

To calculate net income, a standard tax calculator was used to produce income figures after income tax and National Insurance.

LIMITATIONS

A number of assumptions have been made in order to produce an affordability assessment of a varied number of housing models. Different assumptions could be made to produce the analysis but the authors believe this is a reasonable and balanced analysis which provides a macro picture of the affordability of a different range of affordable and subsidised housing products.

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