Local Government and Communities Committee

Scrutiny of the Draft Budget 2017-18

Submission from Professor Kenneth Gibb

This short submission is evidence relating to the pre-budget scrutiny of the housing supply budget looking back at recent years spending. It attempts to respond to (most of) the questions set in the call of evidence on housing and also to address more general issues relating to housing public expenditure in Scotland.

Background

Following the galvanising impact of the national housing needs study that suggested need was 12,000 units per annum\(^1\), the Scottish Government increased its affordable housing supply targets from 6,000 to 10,000 units per annum. The cornerstone of the housing budget is the Affordable Housing Supply Programme (AHSP) which seeks to build 50,000 units (of which 35,000 will be social) over the five years of the current Parliament. Cumulatively, this will involve a budget of more than £3 billion. In 2016-17 alone the total housing budget was £690m, of which £406m was for the local grant element of the AHSP, £166m was the centrally managed programme and the remaining £117m was spent on other housing initiatives such as Help to Buy (Scotland). The centrally managed element is where innovation in funding lies and there are several alternative models posited by the Scottish Government to bring forward to increase investment funds for affordable and mid-market rent (as well as seeking institutional funds for private renting too). We discuss these in more detail below.

General Points

Before turning to the questions set in the call, it is important to make three more generic points about the housing budget and spending on housing in Scotland more broadly.

First, housing is complex and, as Audit Scotland and others have noted, tracking and making sense of the housing budget is not easy. For transparency reasons it would be very useful for Government to explicitly set out, for each element of the programme (suitably defined and explained), how much is being spent in a given year and what the expected level of units invested in will be. Subsequent years can then add an extra column to historical spend by showing the actual delivered outcomes. In a target-oriented system, this should be the standard way of presenting

\(^1\) Powell, Dunning, Ferrari and McKee (2015) Affordable Housing Need in Scotland (SFHA, CIH & Shelter Scotland)
the budgetary information. It should also make clear the difference between on-budget spend and financial transactions and also the budgetary implications of loans and guarantees. The SPICE document (16/49 Housing Supply Budget, by Kate Berry) does an excellent job pulling together the material from diverse sources but we should be able to see a transparent analysis and retrospective monitoring of outcomes as part of the standard budgetary and housing policy communications process.

Second, there is a strong case for providing relevant but non-budgetary housing spend information i.e. tax breaks and benefit spend from reserved sources – since they impact directly on the housing system (which is highly interdependent) and hence on the deliverability of the AHSP programme and broader value for money. Housing benefit spending is the largest single part of the ‘real’ housing budget in Scotland (£1.8B in 2014-15\(^2\)) and continues to make rents affordable and also underpin new investment in affordable housing.

In time, the new social security powers, including powers over the housing costs elements of Universal Credit, will be enacted in Scotland but even before then we should be thinking about the HB budget alongside the supply budget. The same reasoning applies to looking explicitly at the tax benefits (and disadvantages) applying to buy to let landlords (mortgage interest tax deductibility, higher LBTT rates and (relatively) higher CGT rates). We could go further and look at the costs of other interventions such as section 75 planning agreements that support social and affordable housing.

Third, a fundamental challenge for the programme is that meeting its targets is not wholly within the power of government. It is largely down to the individual providers and the array of incentives, opportunities and objectives that shape their development plans. Government can provide capital subsidy and mitigate risks such as the spare room charge (‘bedroom tax’) and it can support innovative alternative funding models and is now contemplating taxes on vacant and derelict land – but that does not guarantee targets will be met. Housing associations concerned about the balance between protecting existing tenants versus new development may often be risk averse. There may be what economists call exogenous shocks – forces outside of the control of the principal parties that inhibit or prevent development e.g. macro shocks impact on the housing investment environment but also so might the proposed deregulatory response to the recent re-classification of the sector.

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Specific Questions

While I do not address all aspects of the questions posed I have grouped my responses below.

1. How well the centrally managed programmes are managed, what outcomes they deliver and do they represent value for money?

2. To what extent are the innovative funding packages leading to a change in the way affordable housing is being delivered?

In a context of sustained budgetary pressures, a much changed private finance environment (compared to pre-2008) and a need to target scarce public resources, it is surely right that Government seeks to move beyond traditional funding models, especially for affordable (e.g. midmarket rent) as opposed to social housing. Government policy has evolved recognising the difficulties and risks in bringing alternatives to the table. The emerging environment and set of possibilities, often funded by financial transactions money is clearly set out in the SPICE paper (pp.12-13):

- charitable bonds (a charity receiving a loan to build affordable housing, the interest on which can be used to support social housing investment);
- local affordable rent housing trust (LAR) involving long term affordable homes via a charity funded by a loan form the Scottish Government;
- local government pension fund investment in mid-market rented homes;
- guarantee-backed midmarket rent schemes building on the earlier National Housing Trust model;
- the Housing Association Resource for Investment Scheme (HARIS) which is a not for profit partnership established by SFHA and the Scottish Futures Trust that will reduce borrowing costs and ability to borrow for providers with covenant or financial capacity problems (SPICE, p.13);
- a proposal for time-limited rental income guarantee schemes to support institutional investment in the private rented sector (i.e. underwriting a proportion of the revenue risk for PRS developments);
- Help to Buy involves the Scottish Government using financial transactions monies investing in up to 15% of the equity in approved new build either for affordable homes or for small developers. The maximum price is being reduced over time though the average realised price (SPICE, p.14) has been £189,000 (2015, Q3) and higher in certain Scottish regions – this is above the overall average house price in Scotland.

It is early to assess whether many of these models will work as intended. They benefit from thinking through what works and being as it were second generation
models that learn from previous experiences. Partnerships, loan funding and charities provide a web of different models and governance which may be flexible locally provided they are adequately supported and marketed. Help to Buy has certainly been successful and supported entry to home ownership in a difficult market and development context for the private sector though as indicated above they have realised relatively high sales prices (I would echo the SPICE paper [p.14] that a Scottish evaluation would be worthwhile especially if HTB was assessed against other equity sharing and low cost home ownership products). There is clearly growing appetite for housing associations to do affordable rent and many of these projects offer a better deal on the face of it to the public purse that would conventional grant-funding of MMR (£44-46,000 per unit currently). A wide range of instruments helps deal with different problems and locations but does require intensive support centrally and locally to make the most of them. This latter issue is probably best addressed by the views of the stakeholders directly involved.

3. The extent to which the centrally managed funds support development of the appropriate mix of affordable housing to meet housing needs (such as mid market rent (MMR) as compared with social rent or private rent)?

The growing appetite for MMR and hence the array of instruments and models emerging represents a response to the growth in private renting more generally (and the growth in the group of working, non benefit-receiving, households who cannot access home ownership), the more challenging funding environment and the uncertain future of benefits that increase perceived risks with social housing. Some providers want to diversify for a wider range of social business reasons. On the demand or need side of the equation we should recognise that housing need studies do not deal particularly well with the private rented sector and I would argue neither do they address well this new intermediate demand group. Partly this is because of definitional problems with need (it is a binary – affordable or not) and also it does not capture well a non-price market failure in the form of weak private demand.

Moreover, mid market rent is still an immature product set in a wider context of a poorly understood but rapidly growing PRS which it is closer to than social renting – but clearly meets an important blockage in the system. In the sense that we require a wide range of housing solutions in our interdependent local housing systems, we do need the extra capacity that MMR or affordable rent or even shared equity can provide – but classic VFM questions remain unanswered about the social return and the cost of providing these different models especially when we take into account second round and spill-over effects e.g. how will investment to scale in mid market rent impact on the private rented sector and then entry level home ownership sectors? This is why the word appropriate in the question is critical.
4. To what extent do the resource planning assumptions and the Strategic Local Planning Agreements processes effectively enable local housing needs to be prioritised and resourced?

The system has moved on massively in recent years offering multi-year planning, evidence-led local housing strategies which help shape local plans, targets and identifying priority projects and sites. It brings together a series of linked plans (LHS, SHIPS, RPAs and SLPAs). When the SLPAs are agreed this allows for programme agreements between specific HAs and councils. This is all good and appears to be closely monitored in delivery terms by the Scottish Government (though it would be good to hear the views and experiences of councils and housing associations on this approach in practice) – but also the system needs to be evaluated and monitored as a whole – does it work consistently?

What do the users say?

5. We seek written responses on whether the increased subsidy levels will support new housing developments; and in particular whether the flexibility in subsidies will improve the provision of housing for older people or for people with particular needs.

Absolute subsidy levels for benchmark properties are considerable (urban greener association grants at £72,000 and council greener grants at £59,000) and that must reflect a judgment by the Scottish Government about overall funding and what is required on a per unit basis to make the required scale of development proceed. But there are always risks – will the developing community of associations and councils determine that they can develop, can access land and the balance of private funding required, how do they assess the risks of development, higher gearing and long term repayment. Plus, there are exogenous shocks that might reduce development demand but might also, via Barnett consequentials, increase or decrease available funds. It seems reasonable on VFM grounds that councils should have lower grant rates but it is not clear to me that this is the right differential. Similarly it is not clear that the differential between social housing grant and mid-market rent grant levels is correct. The same goes for the urban-rural divide. The ordinal differences seem plausible but what the cardinal differences precisely?

6. Do you have any other comments to make about the outcomes the Scottish Government seeks from its Housing Supply Budget and how it delivers those outcomes?

Two final points. First, I do not know the extent to which and how the housing system as a whole and the Affordable Housing Supply Programme/housing needs link into the Scotland Performs refresh exercise that is underway. The high level indicators under the old model were too few and high level although the specific housing and regeneration indicators set was quite useful. In previous years the draft budget and
housing spend have been set against the outcomes framework. Now we have an opportunity to make a much more detailed and thorough alignment between housing spend and housing/societal outcomes. This would seem to me to be a relevant topic for the committee to consider.

Finally, I would like to reinforce and agree with the many commentators who have pointed out the difficulty of effective scrutiny given the collapsed and shortened timetable for the budget process given the late UK Autumn Statement. Is this something that the UK national and devolved governments can make progress with, as it is surely bad for all if financial scrutiny of government budgets cannot be given the necessary space and time to be done to the level of detail we surely require?

Kenneth Gibb
Policy Scotland
University of Glasgow