A National Housing Conversion Fund:

buying properties to boost affordable housing supply

Affordable Housing Commission

About us

Affordable Housing Commission

This report was published by the Affordable Housing Commission, with research by the Smith Institute and funding from the Nationwide Foundation.

The Affordable Housing Commission was formed in October 2018 as an independent group of housing leaders, chaired by Lord Best. It was founded by the Smith Institute with the support of the Nationwide Foundation. The Commission's main report 'Making Housing Affordable Again: Rebalancing the Nation's Housing System', was published in March 2020. A follow-up report, 'Making housing affordable after Covid-19' was published in July 2020.

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Executive summary

The case for a National Housing Conversion Fund rests not only on the urgent need to increase social and affordable housing and rebalance the housing system, but also as a quick and cost effective way of supporting the economy as we move forward from – what we hope – is the worst of the pandemic. And, as demonstrated in this report, such a scheme could also improve housing conditions and contribute to the government's strategic ambitions to level up the economy and reduce carbon emissions.

Why do we need a conversion fund?

A National Housing Conversion Fund will help address the chronic undersupply of affordable housing by converting private housing into low-cost, good quality homes to rent. This is set to become a more pressing challenge as unemployment and homelessness increase as a result of the pandemic. Some private landlords may wish to exit the market as arrears mount up and demand falls, providing the opportunity rebalance the housing system to improve affordability. For homeowners, the Commission is concerned that the fall-out from Covid will soon seriously dampen the housing market. This will place serious strain on homeowners unable to pay the mortgage and in negative equity. The fund, if targeted on specific markets, could help increase demand and place a floor on the market.

Alongside the challenges in the existing market, more new housing schemes are likely to be under threat. The likelihood is that housing supply in the foreseeable future will remain significantly below trend and that some sites will be stalled – with a loss of both new private sales and social and affordable homes. The build rate of new homes in England is already well below the national target and in nearly all places is failing to meet local need. On some troubled sites where development might be scaled back or mothballed, housing for sale could – with government support - be 'flipped' to social and affordable homes for rent. This would keep developments going and support the housebuilding industry.

The Commission has previously argued for a housing-led recovery programme and recently set out a 12 point plan of action, which includes the idea of a housing conversion scheme.[1] This report takes forward that recommendation, which could be introduced as part of the recovery programme and feature in the forthcoming Comprehensive Spending Review 2020.

A National Housing Conversion Fund

A National Housing Conversion Fund would make grant available for social landlords and alternative housing providers (such as community-led housing organisations) to acquire existing private rented properties and convert them into new social and affordable homes. A major part of the Fund would be targeted at lower demand areas, with grants contingent on improving housing conditions and supporting local economies.

The Fund would also be available for housing providers to acquire properties from developers on stalled sites to kickstart development. This approach – which was successful in the 1990s and 2000s – could form part of the government's recovery programme.

The report examines the strategic and economic case for a £1.3bn Fund for England, drawing on past experience and with regard to trends in the housing market. The headline cost benefit analysis concludes that a Fund could:

- Deliver 42,500 new social and affordable homes, the majority of which would be at social rents (with 35,000 in low demand areas in the North and Midlands – at an average grant of £23,000 each - and 7,500 on stalled sites, at higher grant rates)
- Provide an immediate boost to the economy and offer wider economic benefits over 30 years, such as an increase in economic activity worth £1.4bn

The strategic case

The report puts forward the strategic case for investment now. As part of a co-ordinated recovery plan a National Housing Conversion Fund could:

- Provide additional social and affordable housing and help address the immediate affordability crisis facing tenants who may lose their homes
- Help struggling homeowners who cannot meet their mortgage payments and cannot find a buyer for their home
- Help rebalance the housing system by converting private rented properties into social and affordable homes
- Provide a floor on the market in weak housing markets
- Help level up the economy by focusing investment in areas in the Midlands and North
- Help kickstart stalled sites to increase housing supply
- Improve the quality of the housing stock
- Help the government meet its net zero carbon emissions target
- Deliver wider economic benefits - creating jobs and growth

The economic and VFM case

The report sets out the economic and value for money case. Examining the benefits over 30 years it finds that the Fund would:

- Offer value for money. Over 30 years the net cost after benefits to the Treasury in the form of tax revenues and benefit savings would be £623m

- Generate wider exchequer benefits of £200m in additional income tax and national revenues and in council tax
- Deliver 9,300 additional jobs and £500m of GVA
- Provide distributional benefits of providing low cost housing - worth £700m
- Support £200m in economic benefits from additional housing supply

The proposal is relatively modest compared with the cost of other interventions, such as the recent stamp duty cut. A bigger fund is feasible, depending on the condition of the housing market and the appetite of social landlords. Indeed, the government may wish to consider the proposal in this report as the first round of an extended programme for buying distressed private rented properties.

The government could also offer tax concessions (such as exemption from Capital Gains Tax for sales) to private landlords who wish to sell to their tenants or to a social landlord. Individual landlords could use the proceeds to acquire annuities.

It is envisaged that the Fund is focused on poor quality homes in the PRS and affordable homes on stalled sites. However, it could easily be extended to homeowners who face repossession and to help with the conversion of office and retail space.

Consideration cold also be given to leasehold agreements with private landlords. This could see a social housing provider or community-led housing organisation agreeing to manage and maintain a property for five to ten years, let at social rents with the owner receiving a payment which factored in management and maintenance.

Introduction

The Affordable Housing Commission's research over the past 18 months showed that housing affordability and housing poverty has worsened over the past decade, with one in five of all households in England today living in unaffordable housing.[2] In particular, the Commission's work drew attention to the growing numbers of low income households in the PRS who are under housing stress – many of whom are living in insecure and poor condition homes.

A combination of factors has made housing more unaffordable, including flat incomes growth at a time of rising housing costs, land and house price inflation, welfare reforms and the loss of social housing. In particular, the Commission's work revealed that a main driver has been the switch of low income families from a much smaller Council/social housing sector into the PRS which has more than doubled in size in less than twenty years.

The Commission concluded that to make housing affordable again there needs to be a tenure shift away from private rented housing back to social and affordable housing, including low cost home ownership. The Commission's view was that the PRS has an important role to play but is ill-equipped to best serve the interests of low-income residents and cannot meet the aspirations of potential first-time buyers (FTBs).[3]

Alongside measures to improve the PRS and support FTBs, the Commission proposed a significant and sustained expansion in the level of new social and affordable housing. The Commission called on the government to rebalance the housing system so that no child born today should face living in housing that is unaffordable for them by the time they are likely to form a household of their own. Across tenures, this would mean access to affordable housing opportunities for all by 2045.

The Commission argued that interventions were also needed in the existing (secondary) market - including acquisitions by social landlords of PRS properties to provide additional social and affordable housing. The Commission proposed that acquiring and converting private properties to social and affordable homes would not only speed up the tenure shift but also improve the quality of the housing stock and help reduce homelessness by creating more sustainable tenancies.

The Coronavirus pandemic has underscored the Commission's analysis and demonstrated the urgent need to address deep rooted inequalities in the housing system. The Commission's recent report stated that a policy change in favour of social and affordable housing would not only provide much needed social and affordable homes, but support jobs and local growth, improve the nation's ageing housing stock, reduce carbon emissions, and combat poverty.[4] Needless to say, a recession will amplify the problems of affordability and related concerns over housing insecurity and poor housing conditions.

The immediate housing challenges will be shaped by the development and management of the pandemic and the pace of the recovery. A major concern for many households will be the lifting of the recently extended temporary ban on tenant evictions and the phasing out of help with mortgage payments – alongside the ending of the job retention scheme. These changes will be a worry to those who are most at risk of losing their jobs or face reduced income. As the Commission's work has shown, most struggling renters have low savings and can only get by for short periods without income support.

The prospect of widespread rent arrears – exacerbated by delays and shortfalls in housing welfare support – together with tax and regulatory changes and promised reforms to better protect tenants is expected to encourage some private landlords to exit the market. Much will hinge on how the pandemic impacts on local economies, but there are concerns that more rented properties – especially in low demand areas - will be left empty or fall into the hands of unscrupulous landlords.

The Commission's recent report on affordable housing after Covid argued strongly for continued housing support for vulnerable people alongside a step change in the building of social and affordable homes. The Commission pointed out that without urgent action to increase the supply of affordable housing the gap between housing need and the supply of low-cost housing will widen dramatically.[5]

The Commission's 12 point plan for housing growth included the idea of a National Housing Conversion Fund, with headline recommendation to incentivise social landlords and other providers to convert retail and office premises for residential use, acquire private developers' unsold homes and long-term empty properties, as well as state guarantees for void loss when converted homes are sold on once the market is recovered. This report takes forward these ideas and examines in more detail what form a Fund could take, drawing on past examples of similar schemes and looking at the longer term costs and benefits.

The report examines two main ways a ring-fenced National Housing Conversion Fund could be achieved. The first is targeting funds to purchase homes on the secondary (existing) market. It examines which housing markets – in broad terms – the investment might be best aimed at, factoring in how it could help improve housing condition and support jobs and growth. This option could be weighted to support weaker housing markets by providing a floor for the market and helping those struggling and desperately needing to sell. Funding could be made contingent on investing in a property to raise standards. By focusing on low demand housing areas a higher proportion of the investment would target jobs and growth rather than land costs in high demand places, where the economic rationale is weaker.

The second aspect concerns additional funding for social landlords to purchase homes for sale being built by housebuilders and converting them to social and affordable housing. With sites stalled and the prospect of construction workers losing their jobs, this approach would meet the strategic objective of making more housing affordable, as well as the shorter-term goal of supporting the recovery. It would also ensure that capacity and capabilities within the housebuilding industry is not lost due to the downturn but retained for when a recovery materialises.

Although the report does not explore in detail how the fund could be best delivered (what the implementation guidance should be, how any bidding process might work etc), the capital spending commitment by government is expected to be additional and boosted by some private borrowing by social landlords. It is also expected that the Fund could be managed by Homes England and in London by the GLA. There could also be role in designing and running the Fund for combined authorities, metro mayors and local authorities.

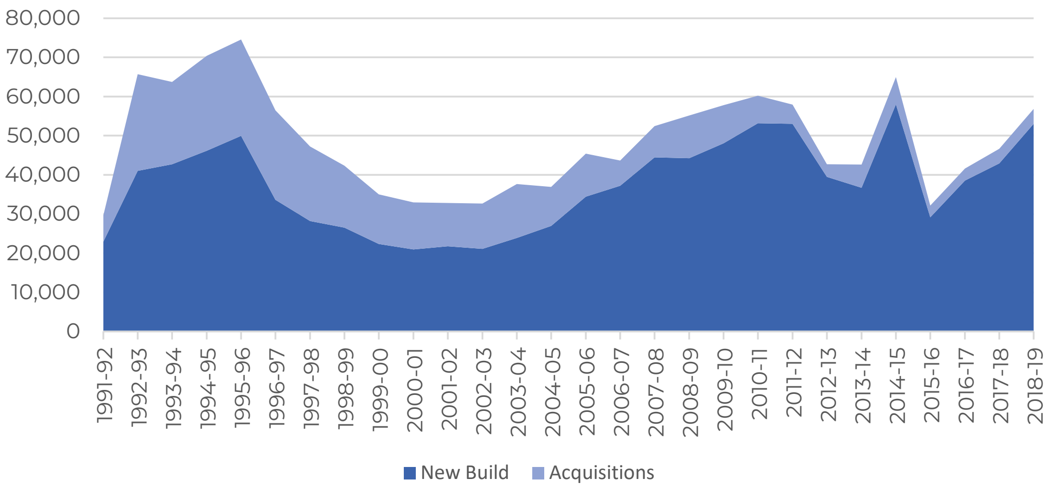
Acquisitions past and present

Acquiring private properties for social and affordable housing has a long history. Over the years acquisitions and conversions have occasionally been used to increase sub-market housing, improve housing quality and stabilise and stimulate development.

During the Second World War around 100,000 homes were requisitioned by local authorities.[6] In peacetime acquisitions were a popular means by which housing associations grew their portfolio. From the 1960s, the Greater London Council started providing funding for housing associations to rehabilitate and convert homes. Support was extended through the 1974 Housing Act and Housing Association Grant in the form of a deficit subsidy for acquisitions, improvement works and conversions as well as new build.[7] By the end of the 1970s some 14,000 properties a year were acquired or converted for improvements.

The levels of acquisitions declined in the 1980s. However, there was a significant increase in the early 1990s following the downturn and the introduction of the government's Housing Market Package (HMP). As a result, levels rose from 7,000 acquisitions in 1991-92 to 25,000 the following year. This was the high-point and levels declined after the mid-1990s. There was a slight increase after the financial crash, but not at the scale seen in the 1990s - numbers have tailed off since to around 1,000 per year.

Affordable housing acquisitions and new build



Source: MHCLG, Live Table 1009

Both of the recent periods when acquisitions peaked (after the recessions in 1990s and 2000s) increased government support was available for social landlords to buy homes as a counter-cyclical measure.

The Conservative government's HMP (introduced in November 1992) extended public expenditure by £577m (around £1.2bn in today's money) to English housing associations' development programmes, which helped to leverage a further £328m in private finance.[8] The package was aimed at buying properties in (or intended for) owner occupation. These had been possessed by lenders, or where the homeowner wanted to sell or private developers wanted to offload newly bult stock. The objective was to prop up supply and prevent unsold properties depressing the market.[9]

The HMP was found to have:

- increased funding for development programmes in England by 38%. This acted as leverage for funding from the private sector, which totalled (alongside investment in Wales) almost £1bn
- been directed towards London and more so than ordinary allocations (even if this did not reflect the greater severity of the downturn in London and the South East)
- exceeded the overall target (in England) of taking 18,000 properties off the market - some 7% were in possession of lenders, half were sold to developers and 41% were private sales

According to Inside Housing: "the results of the HMP were not all good (some landlords found that acquired stock was unsuitable for long-term rental with high maintenance costs) but the package contributed to what I still think is the highest level of investment in social housing in the past 40 years".[10] Others questioned the extent to which houses were taken off the market if developers brought forward completion dates to meet the deadline for the scheme. Some have also suggested that much greater targeting was necessary, with more of a focus on Southern areas.[11] There were also issues with housing quality and the higher running costs that social landlords faced.

Nevertheless, the intention was to place a floor on the market with the government essentially a buyer of last resort. It also resulted in a significant investment in social and affordable housing. George Young, housing minister at the time, noted that the acquisitions exceeded their original targets, which benefited homeless families, and had a positive impact on the housing market. He noted that: "the Royal Institution of Chartered Surveyors came to the same conclusion: that the steps that we have taken have helped to restore confidence in the housing market and that, to use its words, the fundamentals for recovery are now in place."[12]

The last spike in the level of acquisitions was in the wake of the global financial crisis. The level of acquisitions was far more modest and - unlike the HMP - the focus was on new build. The Kickstart Housing Programme announced at the April 2009 Budget was aimed at unlocking stalled sites, including investment to support infrastructure and upfront development costs. As part of the government's housing market interventions, the then Housing Corporation established the National Clearing House scheme which was specifically targeted at buying up developers' unsold properties for use as affordable housing (both for social rent and local cost home ownership). The scheme was established to help facilitate the bulk sale of homes from developers (over 500 units on any number of sites across the country).[13] It was initially launched as a £200m package but later extended to £350m due to demand. According to the official assessment, the National Clearing House supported 9,600 homes in 2008-09,[14] of which 30% were for family homes with three or more bedrooms.[15]

In previous housing downturns developers have actively called for support to flip housing on mixed use stalled sites. As one housebuilder noted: "We brought in some housing association… [T]here were some associations that were looking to expand. And they took advantage of builders as well, looking to expand their asset base in the recession by buying units off-stock. But we actually built their product for them, we took their designs on board, built their product and we kept the site going… [I]t gave us our completions and kept our cashflow."[16] It was also reported that prior to the pandemic there was growing interest from developers in selling stock to housing associations. According to Inside Housing, Brexit was leading developers to offer unsold plots or pre-sale homes to the sector to reduce sales risk.[17]

Current property conversion activity

The government recently acknowledged the value of buying up properties to tackle homelessness. In May 2020, for example, MHCLG allocated £130m in capital funding (from the Next Steps Accommodation) for the acquisition or renovation of homes for rough sleepers – "to help ensure some of the most vulnerable people in society continue to have a roof over their heads".[18]

Councils facing acute homelessness problems, particularly London boroughs, have also been buying properties for temporary accommodation or to support sustainable tenancies (often via their Local Housing Companies). Others have invested in homelessness property funds or run subsidised private homebuying schemes for local residents to convert long term empty homes (such as the £1 homes in Stoke and Liverpool). In some cases councils (like Birmingham, Nottingham and Leicester) have actively sought to buy back Right To Buy (RTB) homes – often through funds raised through the RTB scheme.

Community-led housing organisations and other social landlords have also been active in buying up long term empty homes and converting and refurbishing them into affordable housing. These interventions were helped by the Empty Homes Programme, which has since been wound up.[19]

Permitted development rights (PDR) to convert commercial properties to residential use without planning consent have resulted in over 100,000 additional homes since 2013 – the vast majority office-to-residential conversions in urban areas. This trend may accelerate. The fall out from Covid is depressing high street activity and shifting sales on-line shopping[20] and planning reforms could further extend conversions of commercial to residential conversions.[21] However, while acknowledging the contribution towards overall new supply, the Commission is concerned that the extension of PDRs has all too often lead to inappropriate, poor quality development and undermined local plans that support new affordable housing. Research by the TCPA and LGA shows that PDR reforms have led to a loss of social and affordable homes.[22]

The strategic case for a National Housing Conversion Fund

The case for a National Housing Conversion Fund is predicated on mitigating the impact of Covid on the housing market, not least on the provision of affordable new homes as well as private rented properties in the existing market. The Fund is therefore a direct response to the pandemic but also seeks to complement local initiatives to help bring long-term empty properties back into use, as well as schemes aimed at tacking homelessness. The focus is on improving the supply and quality of social and affordable housing at the same time as supporting jobs and growth and meeting broader policy objectives, such as the levelling up of prosperity and reaching net zero carbon emissions by 2050.[23]

Increasing affordability

The Commission's work highlighted evidence that additional social rented housing was considerably more effective at addressing affordability problems than simply increasing overall housing supply.[24] The Commission argued that the scale of need for social rented and intermediate housing to rent and buy[25] required a national strategy and a number of supply and demand side interventions.

The Fund would seek to support additional new supply but also accelerate the tenure shift to ensure that more housing is secure and affordable – and especially for low-income households. This would also help meet long standing efforts by the government to reduce the housing benefit bill, which has increased in real terms by 30% since the early 2000s (despite caseload numbers being similar) to £21bn.[26] The Fund could also ensure a balance of affordable and suitable housing property types, not least much needed family housing.

In the short-term, a National Housing Conversion Fund would deliver new social and affordable housing at speed. This may be vital to support those at risk or made homelessness. The impact of the pandemic has been mitigated by the stay on evictions while the public health emergency meant that those who were street homeless were housed in emergency accommodation, including hotels.

However, low income renters appear to be worse affected economically and more likely to be struggling to pay the rent.[27] This will could result in a sudden spike in evictions and homelessness, and increased need for affordable and secure housing. Shelter have estimated that 230,000 renters are at risk of 'Covid-eviction' when the government's ban on evictions is lifted.[28] Generation Rent meanwhile suggest that there could be a threefold increase in homelessness cases arising from arrears to 45,000 as a result of the pandemic.[29]

Private landlords exiting the market

Despite continued steady rental growth[30] the outlook for the PRS – especially the buy to let market - remains highly uncertain. The cumulative impact of tax changes[31] and new regulations (such as reform of House in Multiple Occupation licensing) have dampened profitability to a point where growing numbers of small landlords were considering exiting the market. Aldermore Bank's buy-to-let survey of 1,000 landlords in late 2019, for example, revealed that almost half (48%) were considering divesting their portfolios and leaving the PRS.[32] The fall-out from Covid – with potentially widespread increases in arrears and more tenants reliant on housing benefit – is likely to accelerate the trend.[33]

Providing incentives for landlords to sell.

Transfers from the PRS to the social housing sector could be accelerated if government agreed to tax concessions for such sales: for example, exemption from Capital Gains Tax for sales to social landlords, or for sales where individual landlords use the proceeds to acquire annuities. This would encourage disposals by those using the PRS as a pension equivalent and enable landlords to leave the sector without getting into any financial difficulty. The think tank, Onward, proposes tax breaks for private landlords who sell homes to tenants at a discount: buy-to-let landlords would receive 100% capital gains tax relief on the sale to the sitting tenant, with half the windfall (on average £7,500) going towards the tenant's deposit.[34] The Commission was told that social landlords could form real estate investment trusts (REITs) with private companies to buy homes with sitting tenants, with the landlord holding a share option.

Buy to let landlords mortgage arrears going into the downturn were relatively low with just 0.25% of mortgages having arrears over 2.5% (compared with 0.82% of homeowners).[35] However, research by housing experts Alison Wallace and Julie Rugg suggest that while arrears are relatively small a larger proportion of landlords indicated problems with mortgage costs - and there is evidence of landlord subsidising rental property to avoid mortgage debt. They also noted that during the last recession rents dropped, tenant arrears rose, and void periods lengthened. The impacts were uneven across the different housing markets and the research also found that landlords were more likely to report issues meeting mortgage costs in northern regions.[36]

Rent levels may be more stable than house prices, and at the lower cost end of the market rents are effectively guaranteed by housing benefit. Additional welfare support in the form of increased LHA rates is also likely to have helped, alongside the stay on possessions ordered by the FCA.[37] Nevertheless, large numbers of private renters have indicated that they have had problems paying their rent.[38] This will inevitably affect landlords who have a high gearing ratio. At the moment around 5%

of landlords have a loan to value ratio of 90% or more. Crudely speaking with over 1.8m landlords this would mean at least 90,000 homes could be in negative equity if property prices fall by 10%. This figure would rise to over 150,000 if prices dropped by over 20%.[39]

Segments of the rental market could be disproportionately affected by Coronavirus, including holiday lets or student accommodation. Both these examples may require intervention to ensure the market does not collapse and could be suited to conversion funding.

Supporting homeowners

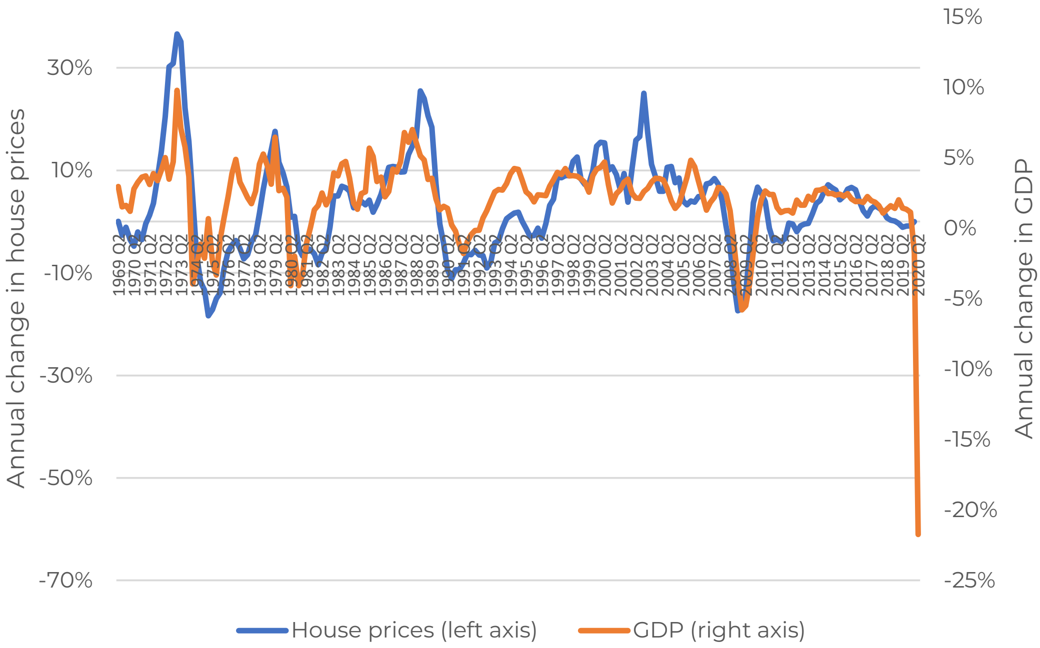
Consistently low interest rates have kept housing costs for homeowners relatively low. Indeed, mortgage arrears and repossessions have been in decline for some time.[40] Mortgage holidays have helped during the pandemic, but the prospect of rising unemployment at a time when the support is withdrawn will leave some homeowners in the financial and emotionally stressful position of being unable to service their mortgage and unable to sell their home. The Bank of England, for example, has modelled that a rise in unemployment to 8% would result in a doubling of households with a high debt servicing ratio (over 40% of gross income), which would be similar to levels in 2007 and the early 1990s.[41]

The role of mortgage lenders will be critical, but not all homeowners facing financial problems will be in a position to agree repayment and deferral plans. This may be a particular challenge in housing markets where prices have not seen much growth in recent years or where they fall rapidly. In these circumstances the Fund would enable homeowners to sell and limit the financial costs associated with mounting mortgage arrears. This could help limit the risks associated with negative equity. The evidence suggest that the threat of a negative equity crisis are not as large as in the 1990s, but there are still significant numbers at risk if property prices fall significantly.[42]

Placing a floor on the market

House price growth tracks the overall economy. As the graph below indicates, price and GDP growth are correlated and standard economic models of house prices feature factors associated with economic growth and the jobs market, such as incomes and employment rates.[43] As such any steep recession is expected to feed through to lower prices. Current reports suggest that Covid has yet to have an impact on house prices. Short term pent up demand seems to be maintaining house price increases – especially in the prime markets[44] (which currently account for around 15% of total property sales).[45] However, while government interventions have propped up employment rates and people’s incomes unemployment is set to increase. The mortgage holiday and the cut in stamp duty will also had a positive impact on the housing market but the first is time limited and the impact of the second may already have been felt.

House price and GDP change (year-on-year)



Source: ONS, House Price Index adjusted by ONS, GDP Deflator, and ONS, Gross Domestic Product: chained volume measures: Seasonally adjusted £m

The impact of the downturn on the housing market is therefore expected to soon feed its way through to lower prices, probably assisted by the reduction in lending under lower loan to value mortgages. House prices are widely forecast to fall significantly over the next 12 months. The OBR's central forecast suggests that prices will drop by around 8% and will be around 5% lower than pre-crisis expectations by 2025. Similarly, Savills have stated that they expect prices to fall by around 7.5%. The OBR's downside scenario would see prices slump further and return to around 10% lower than expectations by 2025.[46] Any prolonged decline could create issues of negative equity and freeze up the housing market as people hold onto their properties and wait for prices to rise.

A National Housing Conversion Fund could place a floor on the market in some places, although it would need to be delivered at significant scale to have a noticeable impact on house prices nationally. However, if targeted on low demand areas, for example, it could support transactions and prices in those local markets. This may not have a negative impact on homeownership rates if targeted on low demand areas where the market is dominated by private landlords rather than first time buyers.

Kickstarting stalled development

Housing supply is highly cyclical and the business models of developers and increasingly housing associations (due to cross subsidy) is pro-cyclical. The speculative nature of housebuilders means that land is bought - and the price paid - on a forecast of house prices (and build costs) a number of years down the line.[47] When house prices fall some sites no longer become viable to develop and therefore become stalled.

The level of housing completions has increased sharply in recent months, although still significantly down on pre Covid levels.[48] Housing starts overall are low by recent levels, and despite the summer surge in sales there are growing reports of stalled sites.[49] Shelter forecast housebuilding to decline by as much as 300,000 homes over the coming five years.[50] Knight Frank expect the delivery of new homes to drop by 35% in 2020.[51] The Construction Products Association forecast a 60% fall in new housing starts.[52]

Without action on stalled sites the government's objective of building 300,000 homes per year by the middle of 2020s[53] looks a long way off. Furthermore, failure to keep the sector going is likely to have a negative impact on capacity and capabilities of the construction sector, as it did in the past downturn.[54] Despite the sector experiencing a strong rebound after social distancing measures were relaxed, expectations are that there will be job losses. Shelter predicts some 116,000 job losses in construction and another 128,000 in the wider supply chain.[55] The Government could mitigate some of the lost output and corresponding job losses by buying homes designed for sale and converting them to social and affordable homes.

Levelling up

The impact of Covid and the downturn on different regions is still unclear. Data from the job retention scheme suggests a similar take up across the country.[56] This could of course change when emergency support is withdrawn. Forecasting by Oxford Economic suggests that regions such as the North East will be worst hit in 2020 and slower to recover in 2021.[57] There may also be specific challenges where local housing markets have high levels of hard to let and empty properties – which are often churned through auction to private landlords.

The emerging evidence suggests that there has been a rise in the number of benefit claimants in lower value areas, notably where the PRS is dominant. For example, in Blackpool where the majority of private renters claim housing support, Universal Credit claims per working age population jumped by over 10 percentage points over the five months to May 2020. There are similar trends in other low housing demand areas such as Middlesbrough and Knowsley.[58]

In many low demand areas the need for additional affordable housing is less than in London and the South East.[59] However, the Commission found was that many households in these areas still had affordability problems as well as a specific challenge around non-decent housing. Supporting housing conversions and improvements in low value market – sometimes as part of wider place-making regeneration schemes - could play an important economic role in supporting jobs and growth, with additional benefits to people's health and well-being.[60]
In so doing, it could help to level up housing grant allocations, which have been disproportionately concentrated in the South.[61]

Stock quality and net zero

The Coronavirus has laid bare the health implications of poor-quality housing. Higher death rates from covid have been associated, for example, with overcrowding and poor housing conditions.[62] The spotlight has been placed on cramped conditions and lack of space and amenity, especially for those living in House in Multiple Occupation. Additional (and improved) social housing provided through a Fund could help address some of these issues.

The lack of poor condition housing – with low thermal comfort for example - comes not only at the expense of people's health but has an environmental cost. The government has enshrined its commitment to net zero emissions in the 2019 Climate Change Act. However, to reach net zero by 2050, the National Grid's Future Energy Scenarios suggests that 60% of homes will be required to be EPC C rated or above by 2035.[63] At present just 30% of properties are energy efficiency EPC C or above (22% by environmental EPC ratings) with a lower proportion in the private sector - and lower standards in the Midlands and North.

EPC rating below C

Source: Analysis of English Housing Survey 2017

Improving energy efficiency standards even with current grants may not be enough to incentivise (or make affordable) upgrades if the property is low value. Those properties within the PRS with rents within the bottom quartile are more likely to have energy efficiency rating below C[64] and average cost of upgrading the property to meet this standard would be over half the annual rental value of the property.[65] A National Housing Conversion Fund centred on improving stock quality within low demand areas could help overcome the financial hurdles.

Converting homes: low demand and kickstart components

Converting homes in low demand areas

The main component of a National Housing Conversion Fund would be targeted at those housing markets where demand is weak, property prices low and where investment is required to improve the quality of the housing stock. Funding would be available to councils, housing associations and community-led housing groups.

The bottom 10% of the housing market could be taken as the focus of the Fund. This equates to homes valued under £100,000.[66] Using the English Housing Survey we can see that many of these lower valued homes are more likely to be non-decent. Using these probabilities, the level of homes sold in 2019 that were non-decent can be estimated (cognisant of the fact that different property types might be sold). This gives a sense of the possible level of sales, but it is expected the grant would increase demand and therefore sales activity.

During the early 1990s, acquisitions ran at around 20,000 homes and this appears to be a credible benchmark for a similar programme - which could be run over a two period (and extended if proven successful).

House prices, sales volumes and non-decency in 2019

	Proportion of sales	**Proportion non-decent**	**Estimated non-decent sales**
0-50,000	2%	42%	8,000
50,000-75,000	3%	31%	8,000
75,000-100,000	5%	23%	10,000
Total			26,000

Source: Sales volumes are taken from the Land Registry data for 2019, proportions of non-decent housing are based on English Housing Survey stock condition survey and based on equity in home of those who own outright

Examining the costs, the main expense will be buying the home. Using the 2019 figures, the price average of properties sold under £100,000 was £68,000. If property prices fall by 7.5% (as Savills forecast[67]) it would cost around £63,000 to buy (costs could be reduced further if the programme is skewed towards lower priced homes). Investment would also be required to make the homes habitable which would also generate immediate economic activity.

The cost of returning empty homes to use has been estimated at around £12,000,[68] plus costs of meeting new energy efficiency standards. According to estimates from the Scottish government, the median cost of making homes EPC C is £3,500.[69] Using these figures it is assumed that investment would be around £15,000 per property to undertake major works, increase the energy efficiency and be habitable for renting. The total investment required would then be around £75,000.

To maximise the impact that a Fund could have, private finance would be leveraged in through lending to housing providers. To understand the grant required assumptions about the rental income and costs of managing the homes can be made.[70] Using these figures the gap between the investment required and the net rental income is calculated. This gap gives an average grant level to support the conversion of properties at around £23,000 for properties valued within the bottom 10% of the market. It would be more than the grant per unit under the Empty Homes Programme, however that programme included lease arrangements as well as acquisitions.[71]

On these assumptions the Fund would seek to deliver around 35,000 unit at an average grant of £23,000 each. This would form 82% of the total output and 65% of a £1.3bn budget.

Leasehold arrangements

An alternative (and complementary) approach to a National Housing Conversion Fund would be to seek leasehold agreements with landlords. This could see a social housing provider or community-led housing organisation agreeing to manage and maintain a property for five to ten years, let at social rents with the owner receiving a payment which factored in management and maintenance. For some segments of the PRS this could be an attractive proposition. Short term lets and housing usually used to accommodate students (non-purpose built) could see a sudden drop in demand in some areas. This could provide appetite amongst landlords to receive a steady income stream rather than risk leaving the home empty for a prolonged period resulting in lost income and cashflow challenges. However, experience with leasehold arrangements under the Empty Homes programme was mixed. The Commission was told that PRS properties often required too much in the way of capital works and leases of less than 10 years rarely added up. Leasing PRS properties in better condition might be more feasible.

Kickstart conversions

Despite the prospect of much slower growth the volume house builders appear to be a better position than a decade ago.[72] As such, the assumption used for the Fund is that there would be an appetite for support to unlock stalled sites - albeit less than in 2008.

The level of interest will of course depend on grant rates, which would need to be higher in high demand areas like London.[73] The grant per unit of the previous National Clearing House scheme, for example, was around £49,000 in today's prices and helped deliver around 9,600 affordable homes -6,300 for social rent and 3,300 for low cost homeownership.[74]

Given house price inflation since the last downturn and current grant levels[75] adjusted for a drop in prices, it is expected that grant required for one third low cost home ownership and two thirds social rent would average £60,000 per unit. On this basis the Fund would aim to deliver a modest 7,500 units on stalled sites. This of course could be scaled up.

Conversions and costs

Element	Units	Grant per unit	Total grant
Conversions in low demand	35,000	£23,000	£805,000,000
Kickstarting stalled sites (shared ownership and social housing)	7,500	£60,000	£450,000,000
Total	42,500		£1,255,000,000

Value for money and the economic case

A National Housing Conversion Fund would represent a relatively small proportion of government expenditure (less than 0.2% and around 2% of capital expenditure). At the level outlined above it would be similar in ambition to the previous Housing Market Package. To put this in context, a £1.3bn Fund would be worth around a third of the value of the temporary cut in stamp duty.[76]

The £1.3bn is also the gross cost and excludes the income it generates in the form of additional revenue from income tax and national insurance and savings on jobseeker's allowance.[77] For new build properties, there would also be revenue from additional council tax.[78]

As outlined later, the Commission's analysis over 30 years shows the net cost to HMT would be £600m whilst delivering wider economic benefits of around £1.4bn. There are also other savings from improved housing conditions and distributional benefits, as well as productivity improvements.[79]

The Fund would also have positive employment affects. Low-income households would financially benefit from housing which is more affordable and of a higher quality, while central government would reap some payback from reduced housing benefit costs. Not all households would claim housing benefit and the savings would be greater in Southern areas where private rents are higher. Nevertheless, the government would make significant savings. Based on analysis of survey data, it is estimated that around three quarters of new social renters are supported through housing benefit or Universal Credit and this covers 85% of their rent (with 10% of homes lived in new households expected to form because of greater affordability).[80]

Even in lower demand areas private rents are higher than social rents.[81] Savings would therefore mount up over time, especially as social rents are expected to grow at a slower rate than private rents.[82] The difference between the costs of private renting and social housing would also have sizeable distributional benefits from the additional social housing. As those on lower incomes gain greater utility from an additional pound than someone higher up the income distribution then - in line with the government's Green Book[83] - the extra welfare impact could be factored into the economic assessment of investing in affordable housing.[84]

The financial benefits for poorer households would also take the form of reduced energy bills.[85] Those on lower incomes spend a higher proportion of their income on fuel costs.[86] Thus poorly insulated housing is regressive and action to improve standards would be part of broader efforts to reduce financial hardship and combat poverty. Professor John Hill's review of fuel poverty in 2012 found that thermal efficiency of homes was a main driver of fuel poverty and that efforts to improve thermal efficiency of low income households would have a positive impact on the 'low-income, high cost' indicator of fuel poverty.[87] There would also be wider health benefits, which reduce demand on the NHS.

Investment in maintenance and major repairs generates employment. Using the Homes and Communities' Agency's 2015 best practice guide and adjusted for inflation, the investment in maintenance and major works suggests that buying existing properties would create 25 jobs per £1.2m, compared to new build job creation at around 16.[88] In both cases the high input demands are likely to create multiplier effects. Estimates of multipliers vary with one analysis finding the affect for construction was 2.84[89] (every pound invested generates £2.84 of activity), while Treasury assumptions about capital expenditure have put the multiplier at 2.[90] However, in line with departmental assumptions for housing a multiplier of 1.59 is applied in this analysis.[91]

It is envisaged that most of activity from the Fund will be additional, especially in low demand areas where public investment is less concentrated.[92] However, it is expected that some homeowners and landlords would have invested in renovations. An impact assessment of the House into Homes programme in Wales (which sought to bring 5,000 properties back into use in low demand areas between 2011-2016) found that 73% of the works would not have taken place without the loan scheme.[93]

But additionality depends on markets and time periods.[94] Expectations around the additionality of new build component of the Fund would be different. The central departmental scenario when the economy was not in recession was that 0.5 additional homes would be built for every affordable home delivered. However, given the current backdrop their upper scenario of 0.6 homes may be closer to actual additionality. The economic benefit from the additional housing would result in more productive use of land (e.g. the difference in land values between residential and agricultural or industrial use), which would total around £50,000 per additional home.[95]

As mentioned, investment in maintenance and housebuilding would create employment opportunities. But not all jobs created by this increased economic activity would be new and there would be some expectation that economic activity would displace activity that would have occurred. With unemployment rates expected to reach at least 7.5%, there is material spare capacity in the labour market.[96] Nevertheless, there will be displacement and conservatively a third of jobs created might be expected to be additional.[97] On this basis the Fund would support over 9,000 people into work. This would mean that the government would receive additional revenue from income tax and national insurance and savings on jobseeker's allowance.[98] For new build properties, there would also be revenue from additional council tax.[99]

It would also have wider benefits. Supporting the house building sector would, for example, ensuring that expertise and capacity are retained – avoiding the long-term scarring effects of unemployment (which inhibit future job prospects and pay, and cause reduce health, happiness, and job satisfaction years later).[100]

What would the overall impact be?

Based on the assumptions mentioned it is possible to quantify the costs and benefits of the Fund.[101] The overall grant costs would be around £1,255m but with housing welfare savings and wider benefits the net cost to government would be £623m. The net economic benefits of increased housing, economic activity and distributional benefits over 30 years would meanwhile total £1,369m.

National Housing Conversion Fund: Present value over 30 years

Outputs (units)	**Kickstart conversion**	**Low demand conversion**	**Total**
Net increase in affordable housing	7,500	35,000	42,500
Net increase in housing	3,750		
Net increase in decent housing/ energy efficient		26,250	26,250
Jobs created	4,200	5,200	9,300
Net government costs (£)	**253,000,000**	**370,000,000**	**623,000,000**
Grant	450,000,000	805,000,000	1,255,000,000
Increase in housing benefit	-117,000,000	-352,000,000	-469,000,000
Wider exchequer costs (Council Tax, benefits)	-80,000,000	-83,000,000	-163,000,000
Net economic benefits (£)	**584,000,000**	**785,000,000**	**1,369,000,000**
Economic benefits of increased supply	177,000,000	0	177,000,000
Distributional	177,000,000	539,000,000	717,000,000
GVA	229,000,000	246,000,000	475,000,000

Levelling up and net zero

The Fund would aim to support the government's levelling up agenda. A feature of limiting funding by house price would be that the grants for conversion of existing properties would be targeted in the Midlands and the North. The estimated total number of jobs would also be directed towards these regions as well as the estimated additional GVA created.

Regional benefits

	Affordable homes	Additional jobs	GVA
North	20,000	3,600	£166,000,000
Midlands	15,000	2,700	£129,000,000
London	1,900	1,000	£70,000,000
South (excl. London)	5,600	2,000	£109,000,000

The targeted nature of the funding would also help place a floor on the housing market in these regions which were slowest to recover from the last housing downturn. For example, annual sales volumes in many local authorities are somewhere between one or two thousand. A Fund could help fill some of the drop in sales (10% or 20% of 2019 sales)[102] in targeted markets.

The Fund would aim to tackle non-decent housing and improve the energy efficiency of homes. While new government grants will support private owners improve home insulation, those in low demand areas where rents and house prices are low may be reluctant (or cannot afford) to make these improvements. This would address this specific challenge and when accounting for displacement it would contribute 0.4% of the change required as set out National Grid's Future Energy scenario. If extend over the decade this figure could rise to around 2%.

Can it be delivered?

Previous housing conversion schemes were not without their problems. Many housing associations who bought homes through the Housing Market Package ended up facing higher maintenance costs. This was largely due to poorer build quality and non-standard components (for example a variety of boilers to which maintenance workers were unaccustomed). Some of these problems were also apparent when buying from builders.[103] It is expected that the initial grant would help rectify some of these issues, with the upfront investment to make the properties decent and warm enabling housing associations improve build quality and standardise products. There might also be some adjustments needed to grant levels to ensure these additional maintenance costs are covered so as to make it an attractive proposition for housing associations, local authorities and community groups.

There may also be challenges around numerous housing providers competing for the same properties and bidding the price up. This could both increase the cost to government and to the provider. The scheme could therefore be made contingent on buying through an agent to prevent these inflationary risks.

The Fund will have to offer social landlords an attractive proposition. The issues around non-standardised components and stock quality may act as a barrier. Nevertheless, despite issues encountered under the previous HMP, there was appetite in 2008/09 amongst social landlords.[104] Housing associations bought through the National Clearing House scheme after the credit crunch, and as the Empty Homes Programme highlighted there was a willingness amongst community housing providers who wanted the scheme to continue. That said, any scheme would need to work closely with providers to ensure that grant levels are set at the right level, take account of lessons from previous schemes and adjust for the different economic circumstances and operational practices.

Conclusion

The Commission argued the headline case for a National Housing Conversion Fund in its main report, published at the start of the lockdown. The rationale rested on the urgent need to increase the supply of suitable, better quality and secure housing for low income households – many of whom were living in unaffordable and poor quality private rented homes. If targeted in the right way the Commission concluded that acquisitions by social landlords for tenure conversion would also have wider socio-economic benefits, including helping people into work and reducing the benefit bill.

The fall out from Covid strengthens the case for such a scheme, which could extend to empty buildings and office and retail properties. As such, the Commission recommends that in preparing the next phase of housing interventions and allocating future spending under the forthcoming Comprehensive Spending Review the government should seek to quickly establish a National Housing Conversion Fund, mindful of the forecasts of a slump in the housing market.

Although house prices seem to have rebounded since the lockdown, most housing commentators and experts expect it will not last. This appears already to be affecting the viability of some new developments and impacting on yields in some sections of the PRS, especially in low demand areas. As such a targeted Fund could both assist the tenure shift towards more social and affordable housing and help build out stalled sites.

As the Commission has previously mentioned, a Fund of this type could also benefit from tax concessions to encourage some private landlords to sell and from conditionality clauses to ensure purchased homes are improved to a decent standard.

The Fund could also play an important role in placing a floor on the market in low demand areas. It could both support homeowners struggling to pay their mortgage and finding it hard to sell and struggling private landlords. At the same time it could also support a weak labour market and help protect skills and capacity within the construction industry. Sitting and new tenants would benefit from improved housing conditions, better security and in most cases lower rents.

From the assessment in this report these benefits outweigh the grant costs. The funding proposed is also relatively modest compared to existing housing support schemes, such as the reduction in Stamp Duty.

This type of scheme is not new and has been successfully used by previous governments as a counter-cyclical intervention. Returning to the scale of ambition witnessed in the early 1990s would – as set out in this report - be feasible and offer

offer value for money. As part of a housing led recovery plan a targeted National Housing Conversion Fund could not only boost jobs and growth but improve housing conditions and help make housing affordable again.

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The Affordable Housing Commission.

The Commissioners are members of the Affordable Housing Commission in a personal capacity. The views expressed in this report do not necessarily reflect the views of their organisation.

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