

Professor Christian Hilber, Professor of Economic Geography, London School of Economics and Political Science – Written evidence (UKH0116)

Brief introduction

I am a Professor of Economic Geography at the London School of Economics (LSE). I am also an Associate at the Centre for Economic Performance and a Member of the Academic Panel of the What Works Centre for Local Economic Growth. Before joining the LSE, I was an Economist at the US government sponsored enterprise Fannie Mae (2002-2003) and a Postdoctoral Research Fellow at the Real Estate Center of the Wharton School, University of Pennsylvania (1999-2002). I hold a Ph.D. in Economics (1998) from the University of Basel.

Relevant to this written evidence, my research focuses on the functioning of land and housing markets and on the impact of policy interventions, such as Help to Buy, in these markets.

I am currently a Member of the LSE Real Estate Economics and Finance Advisory Board and of the Executive Board of the University of Zurich's Center for Urban and Real Estate Management. I previously served as a Member of the Board of Directors of the American Real Estate and Urban Economics Association. I am an Associate Editor of *Regional Science and Urban Economics* and of *Journal of Regional Science* and a Member of the Editorial Boards of *Journal of Housing Economics* and *Real Estate Economics*. I am also a member of the Editorial Advisory Board of *Public Finance Review*. I am a Fellow of the Weimer School of Advanced Studies in Real Estate and Land Economics.

I have published in numerous academic journals including *Review of Economics and Statistics*, *Economic Journal*, *Journal of Public Economics*, *Journal of Urban Economics*, *Journal of Economic Geography*, *Regional Science and Urban Economics*, *Real Estate Economics*, *Journal of Housing Economics*, *Regional Studies* and *Brookings-Wharton Papers on Urban Affairs*.

I have provided written and/or oral evidence to the *Prime Minister's Implementation Unit*, the *H.M. Treasury Select Committee*, the *House of Lords Select Committee on Intergenerational Fairness and Provision* and the *National Audit Office*, amongst others.

Inquiry questions and written evidence

1. What is the current composition of the UK's housing sector? How is the sector structured in terms of private ownership, privately rented accommodation and social housing?

1. The Government's housing statistics for England¹ suggest that in 2020, 63.8% of housing units were owner-occupied, 16.7% were privately rented, and 19.5% were socially rented.

2. It is helpful to see these numbers in a 'historic context': The homeownership rate has been on the rise since World War II until 2001/2002, peaking at 69.5%. Since then, it has fallen again quite substantially to 62.4% in 2016. Owner-occupied housing has made a slight recovery since then, rising back to 63.8%. The share of private rental units has been stable around 10-11% during the 1980s and 1990s. Since then, it has been rising steadily to over 20%, peaking at 20.4% in 2016. It subsequently fell back slightly to 19.5% today. The socially rented sector has been in decline since 1980, in part as a consequence of Right to Buy. The rate of socially rented homes was at 31.2% in 1979. It has fallen steadily to 16.7% today.

3. The ownership structure of the private rental sector in the UK is unusual in an international comparison. It is unusual in the sense that most private rental units are held by private individuals. Before the 1980s, the share of private individuals holding private residential objects was small. This changed with the Housing Act of 1988, when the assured shorthold tenancy came into effect, leading to a Buy-to-Let boom starting during the mid- to late-1990s. In contrast to many other countries, the role of the institutional sector in the private rental market is still minuscule. However, this has recently started to change. Increasingly, private rental residential stock is built and rented out by institutional investors and managed by specialist operators. This latest phenomenon has been dubbed Build to Rent. It goes hand in hand with a decline in Buy to Let.

2. What social and demographic factors shape housing demand in the UK? What are the expected future trends in housing demand?

4. Demand for housing is largely driven by real income growth and, to a lesser extent, by population movements (net migration, changing preference for peripheral space). The COVID-19 pandemic has arguably further increased demand for housing (more working-from-home) and, in particular, for single-family housing and garden space. Moreover, the pandemic has arguably altered preferences in favour of less central and greener spaces. Interestingly, these trends could already be observed before the pandemic started. However, the pandemic has reinforced these trends.² To what extent the current trends represent longer-term shifts or are transitory is difficult to say with confidence. In recent weeks there have been some signs of a partial reversal in that demand

¹ GOV.UK [Life Table 104](#).

² See Cheshire, P., C.A.L. Hilber and O. Schöni. 2021. The Pandemic and the Housing Market: A British Story. [CEP COVID-19 Analysis, No. 20](#).

for private rental housing in central areas appears to have started to increase again.

3. Does the Government's target of 300,000 new homes per year accurately reflect housing demand? Is this target achievable?

5. The target of 300,000 new homes per year is in some sense an 'ad hoc' number, but it represents a reasonable target reflecting housing demand in the country. The target is very significantly above current and recent delivery rates, but, equally, significantly below the peak of UK house building in 1968 when nearly 426,000 new homes were built.

6. Despite rising real incomes and population growth – that is, growing demand for housing – construction of new housing in the UK has been decreasing in a cyclical fashion since the late 1960s, leading to a substantial and growing housing shortfall.³ This has led to a growing housing affordability crisis⁴ affecting large parts of the country but especially Greater London and the South East.

7. The main underlying causes are a dysfunctional planning system and lack of fiscal incentives at Local Authority level to permit development.⁵ Unless the planning and tax systems are radically reformed (see response to question 5), I do not believe it is realistic to achieve, in a sustained fashion, the target of 300,000 new homes per year.

8. All that said, it does not just matter how many new homes we produce each year, but also *where* such new housing is added to the existing stock. It is crucial that house building intensifies in the most productive places of the country (chiefly Greater London and the South East), where there is the greatest shortage, and the affordability crisis is most severe. Unfortunately, given the current institutional setting, there is a risk that house building is added in places where there is the least political resistance, rather than close to places where productive jobs are located, and new housing is most desperately needed. This has an adverse effect not only on productivity, but also on the environment in that it increases commuting times and pollution, especially to the extent residences are outside of greenbelt areas.

9. One case in point is the economic impact of Britain's most recent flagship housing policy – Help to Buy (HtB), and, in particular, the HtB's Equity Loan scheme. Carozzi *et al.* (2021) provide strong evidence that the HtB Equity Loan scheme (a demand-side housing policy) has had a detrimental effect on housing affordability in the most desirable area of the country: Greater London.⁶ The empirical analysis exploits discontinuities in the generosity of the HtB Equity

³ Not only has construction declined massively over the last 40 years, but new houses are also about 40 percent smaller than in similarly densely populated European countries (i.e., the Netherlands and Germany).

⁴ Over the last 45 years, real house price growth in the UK has been faster than in any other OECD country and has far outstripped earnings growth.

⁵ See e.g., Hilber, C.A.L. 2016. The UK Planning System – Fit for Purpose? [Planning and Building Control Today, July](#).

⁶ Carozzi, F., C.A.L. Hilber and X. Yu. 2020. On the Economic Impacts of Mortgage Credit Expansion Policies: Evidence from Help to Buy. [CEP Discussion Paper, No. 1681](#).

Loan scheme across the Greater London Authority boundary and the English/Welsh border. It suggests that the policy has had the effect of increasing prices of newly built homes in Greater London by significantly more than the present value of the HtB-subsidy. This is because not only did the HtB-subsidy increase demand for housing, but also the relaxation of credit constraints further amplified this demand increase. Since housing supply is severely constrained in the Greater London area, this has led to a substantive increase in house prices, with no statistically significant effect on construction numbers. Supply is severely constrained in London in part as a consequence of tight planning constraints and in part as a consequence of physical constraints (there is not that much undeveloped land left to build in central areas of the capital).⁷

10. In contrast, HtB has led to a significant increase in construction near the English/Welsh border, without affecting prices in a statistically significant way. This is arguably because housing supply is comparably responsive near the English/Welsh border.

11. The lesson learned from this research is that demand-side housing policies (such as HtB) may increase housing construction, but only in locations where it is comparably easy to add new housing supply (such as near the English/Welsh border), not in locations where productive jobs are located and housing is severely supply constrained (such as in Greater London). In these locations demand-side policies only further accentuate the existing housing affordability crisis. The only viable long-term solution in such areas is to reform the planning and tax system, such that more housing can be added locally.

12. If the Government were to push such demand side policies going forward, this could have the perverse effect that, although construction numbers may increase in areas with comparably responsive supply, the housing crisis would continue to worsen in those areas where young households and low incomes already are most severely adversely affected.

4. What is the balance of demand for new housing between homes for private ownership, privately rented homes, and social housing? How does this affect the type and tenure required of new homes?

13. Current trends, even pre-dating COVID-19, seem to suggest that there is strongly growing demand for single-family housing with garden space in areas outside city centres, but with good access to these centres.

14. The extent to which changing preferences for more (single-family) housing and garden space in more peripheral areas manifest themselves in actual

⁷ See Hilber, C.A.L. and W. Vermeulen. 2016. The Impact of Supply Constraints on House Prices in England. *Economic Journal*, vol. 126, no. 591, pp. 358-405. [Working paper version](#) (free access). The findings of this study suggest that the main culprit in England driving the affordability crisis is the planning system, with planning being particularly unresponsive in the Greater London area and the South East of the country. Put differently, planning induced constraints in conjunction with strong demand for housing in parts of the country are the main *causal* drivers of the extremely high house prices, and, to a lesser extent, rental prices. See also Hilber, C.A.L. and A. Mense. 2021. Why Have House Prices Risen So Much More Than Rents in Superstar Cities? Department of Geography [Discussion Paper](#), No. 30, November.

construction numbers does not just hinge on demand, however. It also crucially depends on the extent to which the planning system permits construction of housing of a certain type in particular areas. That is, construction numbers and the composition of the newly built stock is the 'equilibrium outcome' of demand and supply. To illustrate this point, there is for example allegedly very strong demand for single-family housing space in the zones between Central London and London's Greenbelt. However, we see little new construction in these zones as a consequence of restrictive planning regimes, very strong political resistance by local residents, and lack of fiscal incentives by Local Authorities to permit residential development. Local Authorities face the political and financial costs of such development, but they do not reap the fiscal benefits or political rewards.

5. What can be done to ensure there is a good balance of new homes where they are needed across the UK?

15. This would require two types of reform. First, it would require a radical reform of the current British planning system, away from the existing Development Control System, towards a rule-based Zoning System. It would require reducing the power of local NIMBYs (Not in My Backyard residents) in the political process. See e.g., Cheshire and Sheppard (2005)⁸, Cheshire and Buyuklieva (2019)⁹ and Hilber (2016)¹⁰ for some in-depth proposals.

16. Second, it would require a reform of the British tax system, and, in particular, of the system of property taxation. One important element of such a reform would be to provide greater fiscal incentives to Local Authorities to permit residential development. The report by Cheshire and Hilber (2021) offers a road map for such a reform of the property tax system.¹¹

17. Reforming the tax system also implies reforming the Central Government Grant "Equalisation System", which – in the medium- to long-term – more or less eliminates any revenue gain for Local Authorities that permit more development relative to those that are more restrictive.

6. Is the construction sector able to deliver the UK's housing demand? What barriers are facing the sector?

18. The UK and especially England has an exceptionally restrictive and complex planning system. It is one of the most restrictive, if not *the* most restrictive planning system in the world.¹²

⁸ Cheshire, P. and S. Sheppard. 2005. The Introduction of Price Signals into Land Use Planning Decision-Making: A Proposal. *Urban Studies*, Vol. 42, No. 4, pp. 647-663.

⁹ Cheshire, P. and B. Buyuklieva. 2019. *Homes on the Right Tracks: Greening the Green Belt to Solve the Housing Crisis*. London: The Centre for Cities, No. 25.

¹⁰ Hilber, C.A.L. 2016. The UK Planning System – Proposals for Reform. [Planning and Building Control Today](#), October.

¹¹ See Cheshire, P. and C.A.L. Hilber. 2021. *Home Truths – Options for Reforming Residential Property Taxes in England*. [Bright Blue Report](#), May.

¹² See Hilber, C.A.L. and O. Schöni. 2016. Housing Policies in the United Kingdom, Switzerland, and the United States, Lessons Learned. [Cityscape](#). Vol. 18, Nol. 3, pp. 291-332.

19. The construction sector has been held back by this planning system. Moreover, the complexity of the system creates significant 'barriers to entry', (i) favouring large developers who have the legal expertise to 'get around' the various restrictions and (ii) making it difficult for small scale developers to succeed. In fact, it could be argued that large scale developers are quite content with the existing system as it allows them to minimise competitive pressures and achieve excess profits.

20. As a consequence of all this, the development/construction sector is smaller (per capita) than in other comparable countries and construction takes considerably longer.¹³ Brexit, no doubt, poses a further challenge, at least in the short- to medium-term, to attract skilled labour into the construction sector.

21. All that said, I have little doubt that in a setting with a more rationale 'state-of-the-art' planning system and a reformed tax system, the construction sector would thrive, and smaller developers would flourish. There is plenty of evidence from around the world that the private sector can deliver large numbers of high-quality housing if the conditions and incentives are set right.

7. The Government has published its proposals for reform of the planning system. How can the planning system be shaped to meet housing demand?

- What role should permitted development rights play in this?
 - How might changes to Section 106 agreements shape the provision of social housing?
 - How should communities be engaged in the planning process?
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22. The proposed reforms – if implemented as suggested, and not watered down– would be important steps in the right direction, with the caveat being that the proposed reforms focus too much on the planning system itself, giving too little weight to reforming a similarly flawed (property) tax system.

23. Permitted development rights are a 'second or third best solution' in my opinion. They are an improvement within the current setting (i.e., within the current deeply dysfunctional planning system). However, they are a 'drop in the bucket' and won't on their own resolve the affordability crisis facing large parts of the country.

24. Section 106 (S106) Agreements should be replaced with a Development Levy. See Cheshire and Hilber (2021) for a detailed proposal.¹⁴ S106 Agreements are essentially negotiated payments in kind, usually in the form of 'affordable housing'. While, at first glance, this may seem appealing, S106 Agreements are an extremely inefficient – even counterproductive – way of delivering more 'affordable homes' and provide other local public goods. One issue is the very significant transaction costs involved in the elaborate and lengthy negotiations of

¹³ See Ball, M., P. Cheshire, C.A.L. Hilber and X. Yu. 2021. Why Delay? Understanding the Rate at Which Sites are Built Out. Mimeo, LSE, November.

¹⁴ Cheshire, P. and C.A.L. Hilber. 2021. *Home Truths – Options for Reforming Residential Property Taxes in England*. [Bright Blue Report](#), May.

S106 Agreements. Another issue is that S106 Agreements inject a great degree of uncertainty into the development process. Often this leads to foregone construction, which in turn adversely affects the affordability of non-subsidised housing via limiting overall supply. Like HtB Equity Loans, which do not actually “help” young would-be-buyers in already unaffordable areas, S106 Agreements provide few additional “affordable homes” to a select group of fortunate tenants (who are often the ones who know how to ‘play the system’), at the (hidden) cost of making housing slightly less affordable for the vast majority of unlucky private renters and would-be homebuyers who struggle even more as a consequence of S106 Agreements. In addition, S106 Agreements, due to the involved complexities and required legal expertise, further increase ‘barriers to entry’ into the development market.

25. In principle it would of course be desirable to engage local communities in shaping their neighbourhoods. In practice, however, within the realms of the existing planning system, engaging the local community essentially has the effect of increasing the power of local NIMBY forces. This is counterproductive. It leads to the perverse outcome that most residents recognise that large parts of the country face a severe affordability crisis and this majority is therefore in favour of building more homes nationally to tackle the problem. However, at the local level, where planning decisions are made, the same group of residents opposes more construction in their backyards. The underlying fundamental problem is that there is no congruence of benefits and costs associated with permitting new local residential developments. The costs, currently, are local, the benefits are mostly for the society at large.

8. What can be done to improve the quality of new homes? How can the design and aesthetics of new homes be improved?

26. I would argue that in a reformed system, the private development sector will be capable of delivering new housing to a high-quality standard. See e.g., the example of Switzerland (Hilber and Schöni 2016).¹⁵

27. In a reformed planning system, the focus should be on correcting so-called ‘market failures’. For example, preservation policies would ensure that historic buildings and architecturally important designs are protected and that important views on landmark buildings are preserved. At the same time, a competitive development sector would focus on delivering high quality housing according to the preferences of local residents and according to agreed building standards. A reformed planning system should reduce the so-called ‘regulatory tax’ with the consequence that it should be possible to produce housing to higher standards, at overall lower costs.

9. Is the workforce equipped with the professional, digital and other skills required to meet housing demand, for example in the construction, planning and design sectors? What can be done to overcome skills shortages?

¹⁵ Hilber, C.A.L. and O. Schöni. 2016. Housing Policies in the United Kingdom, Switzerland, and the United States, Lessons Learned. [Cityscape. Vol. 18, Nol. 3](#), pp. 291-332.

28. The development/construction sector has been held back for decades by a dysfunctional planning system, which has created significant barriers to entry. This means that at current capacities, the industry probably would not be capable of delivering the targeted 300,000 new homes per year. However, there is ample international evidence that the private development sector is capable, at least in the medium-term, to cope with increased demand. Switzerland for example currently produces about three times as many new (mostly high quality) homes per capita as the UK, and these homes furthermore tend to be significantly larger in size.

10. How does the Government interact with Local Authorities to deliver more homes? How can this relationship be improved?

29. My understanding is that the Central Government has relatively little direct influence over Local Authorities' planning decisions (but I am not an expert on the nature of the interactions of the Government with Local Authorities). Indirectly, institutional settings that determine the fiscal incentives of Local Authorities to permit residential development are crucial in determining new housing supply (see above).

11. What are the main opportunities and areas of innovation for meeting the UK's housing demand?

30. See my response to question 5.

November 2021