

Barker Review of Land Use Planning

GLA Economics Response

This report contains the response of GLA Economics to the call for evidence on the Barker Review of Land Use Planning.

This is one of two responses that have been prepared by the Greater London Authority. A separate response has been prepared by the planning department of the GLA which approaches the subject from a perspective focusing mainly upon the institutional processes involved in, and the day-to-day operation of, the planning system.

In this response, GLA Economics provide responses to the consultation questions from an economic perspective. Through the answers to the consultation questions, this response seeks to highlight the importance of market mechanisms in the operation of a successful economy and to review land-use planning in this context. It examines the areas where the planning system has a significant impact in the functioning of the wider economy and examines the impacts on the economy of such intervention. The response seeks to provide suggestions for improving the planning system, either through reducing unnecessary negative impacts upon the economy or through increasing the extent to which market information is used in the planning process to reach informed decisions.

GLA Economics have not supplied answers to all the consultation questions. Rather, we have concentrated on those where we believe we can offer valid comments and suggestions in relation to the planning system as it relates to London.

1. Is the planning system sufficiently flexible and/or responsive to the right signals to deliver the right development in the right place, given the changing economic circumstances due to globalisation, demographic change, natural resource pressures and environmental change? If not, what policy measures might help deliver this flexibility?

The planning system is not sufficiently responsive. It does not at present provide a framework within which the economic consequences of decisions are identified and weighed and the costs and benefits of particular courses of action can be assessed against each other. One key reason is that it does not have any economic pricing mechanisms in place to ensure an efficient allocation of land space between competing end-uses or even to guide planners in their allocation decisions.

A planned system attempts to provide a degree of certainty by ensuring facilities which competitive forces by themselves either might not provide either promptly or at all. Experience shows, however, that in a fundamentally market-based society, this cannot be delivered by administrative fiat. It is important to understand and harness the competitive process, using it to discover what the best outcomes are, since these are not known a priori, and to identify policy interventions that will deliver desired outcomes.

One suggestion as to how the price mechanism could be included within the planning system has been made by Cheshire (1993)¹. He notes that discontinuities in land prices exist in London and elsewhere in the UK because the planning system controls the supply of land for each category of use individually independently of price. Cheshire (2004)² gives examples of the high levels of price discontinuity observed in Reading during the 1980's where there was a net premium in market prices for residential land over agricultural land at the urban fringe of approximately £140,000-360,000 per acre in 2002 prices, a premium for industrial land where it adjoined residential land of £400,000 per acre and a premium for retail over industrial land at its zoning border of over £4,000,000 per acre. There is no reason to believe that such discontinuities do not continue to exist both within the UK and London.

These 'price premiums' provide direct information on the shortage of land in any locality for any particular use. Cheshire's suggestion is that such price premiums could be introduced as 'a material consideration' in the planning decision making process. The idea being that developers should be allowed to change the category of use if the price premium can be shown to exceed some predetermined threshold. Such a policy would be one method whereby market forces could be introduced to the planning system to reduce current inflexibility in terms of land-use categorisation.

Another key aspect is finding ways of ensuring those setting planning policies and taking development decisions can monitor the effectiveness of what they are doing and identify where and when the approaches they are taking need review and revision. This is clearly understood in the field of environmental protection, where a considerable amount of work has been done on establishing suites of indicators. However, this is not the case in the economic field and therefore planners can often lack information on economic matters when making decisions.

To be effective, indicators should be found that address the underlying economic factors driving economic development, social inclusion and environmental protection and improvement. We would suggest that this gap should be addressed, and that this should be done on a regional basis, as national frameworks and indicators are unlikely to provide the degree of flexibility or recognition of regional distinctiveness that would be required (arguably, for example, Government guidance in retailing in Planning Policy Statement 6 fits smaller towns and cities rather better than a densely developed conurbation like London). Regional development agencies and economic observatories could work with regional planning bodies to develop an economic monitoring and evaluation framework, backed by effective indicators, which could be tested at the public examinations of regional spatial strategies, and which could then be used at regional and local levels to inform decision-making.

A third factor that ought to be examined is the education of planners. The scope for including some training in economic concepts, particularly of those underlying the concept of sustainable development, should be examined.

¹ *The introduction of price signals into land use planning decision-making: a proposal*, Cheshire, P (2003) – London School of Economics

² *Spatial Policies, Planning and Urban Competitiveness and the case of London*, Cheshire, P & Sheppard, S (2004) – London School of Economics

None of this is to say that planning is inherently inefficient, or that public intervention in the market is unjustified. It does, however, have to be based on an understanding of the background against which development proposals are made, the likely effectiveness of a potential intervention and an assessment of what kind of intervention is likely to be most effective. Economics and economic concepts have a real role to play in all of these things, and at present the planning system addresses them only in the crudest way.

7. Planning applications for major projects will typically take a considerable time to work through all the necessary stages. Do you consider the system puts too much emphasis on speed or do you feel that it is too slow? If there is an undue emphasis on speed, what are the negative consequences of this and how could they best be avoided? If the process is too slow, what could be done to overcome delays? In particular, what improvements might be made to the planning appeal system to improve its speed and efficiency?

In a sense, asking whether the process is “too slow” or places “too much emphasis on speed” is the wrong question. In economic terms, it is rather whether the optimum level of resourcing (whether in money or time expended by promoters, objectors or those holding the ring between them) are used to reach the best quality of decision. That the question has to be asked at all shows that the economic implications of the system are ill-understood, and that aspects like the opportunity costs of the very detailed scrutiny of major projects (some of which are dealt with below) tend not to be discussed.

Having said this, recent examples of major infrastructure projects in London have pointed to the system currently being too slow. This is a major problem as delay is a significant cost of the planning system, whether for major projects, or smaller more typical planning applications. Excessive delays in consideration of planning applications lead to significant economic losses as land and resources remain unused, and the potential benefits of investment are foregone for the period of time of the delay.

For large developments in general, delays in the decision making process can mean that some planning applications can take up to 12 to 18 months to reach a conclusion, with the possibility of this timeframe being more than doubled if a proposal is called-in by the Secretary of State or is subject to appeal. For major infrastructure projects, such as the Thames Gateway Bridge, the need to go to Public Inquiry can extend this delay, and the resultant economic costs, significantly.

The process of preparing major applications is costly, time-consuming and involves many different strands of analysis, from retail impact assessments to environmental assessments to noise and air quality and so on. There are many levels of guidance on these where detail is continually enhanced. As a result even the preparation of applications can take many months, with concomitant risks.

Moreover, the modelling required in many cases provides very severe challenges:

Environmental Statements must include noise and air quality impacts; Where there is a retail proposal or content, there must be an assessment of the impact on existing

retail centres, tested sequentially; Applications may also need to include analysis of socio-economic impacts relating to employment, unemployment and so on.

All of these suggest that it is necessary to provide detailed appreciation of the situation which will exist in the absence of the proposed development and then also how the situation will be changed once the development has been put in place.

In the case of transport projects, this is taken to extremes. Current guidance from the Department of Transport on economic benefits both gives a very restrictive definition of economic improvements (reduction in unemployment for existing residents in an area) and indicates considerable forecast detail which is required in order to establish these benefits.

There is spurious precision in the provision of these projections. The smaller the proposed development of course, the easier it may be to take an other things being equal assumption which may make such analysis more plausible. But of course it is in the case of larger projects that such analysis becomes of interest and importance. Moreover, a large project may take considerable time to implement. Providing an analysis of, say, skill needs in 10-15 years time in any detail is very risky, both for the base and implemented case.

It is crucial to realise that analytical and modelling techniques in many of these areas are limited. Moreover, it is always easier to suggest a negative than prove a positive and the burden therefore rests much more heavily on a promoter than an objector. In particular, as time passes, it is always possible to bring forward new analysis and table further objections. This leads to an excessively long public inquiry process.

One reason for this is that Planning Inquiries do not need to consider the costs and benefits of the Inquiry process. Indeed, risk of Judicial review encourages conservatism in hearing all possible objections and given that objectors do not need to establish any status beyond their willingness to provide a proof of evidence and to turn up then long inquiries become inevitable. Furthermore, the scope of an Inquiry is often drawn quite generally so that all matters can be looked at and this also extends the length of time they take.

This is an area that deserves close and rigorous examination. The current system has grown incrementally ever more complex, and our experience is that it is currently satisfying very few, whether promoters or objectors. It is swallowing ever increasing amounts of time and money, causing delays and making the process increasingly opaque to those without specialist knowledge or resources. We suspect that it is hard to justify in economic terms, and that it is in everyone's interests to examine the issue further.

8 Is there evidence to suggest that the direct costs of making a planning application are deterring investment? Are there any unnecessary burdens/how might information requirements be streamlined to reduce the regulatory burden from the process of making an application?

Evidence of how the direct costs of making a planning application deter investment is extremely difficult to obtain and we are not aware of any recent quantitative attempts to do so. However, this is not unexpected as investment deterred is not an easy concept to capture in a quantitative manner.

Nevertheless, the direct costs of a planning application, alongside the indirect costs arising from delay, are probably the most common cited criticisms of the planning system from business. These various financial and time costs can all be considered as 'transaction costs' of dealing with the planning system. By adding to the costs and uncertainty of a development decision, it is clear that these transaction costs must have some deterrent effect upon investment, in comparison to a case where such costs do not exist. The difficulty is in measuring the size of such an effect and in identifying the type of investment decision most likely to be negatively affected.

It would appear likely that the costs will be lower for companies who regularly develop (and have systems/consultants etc in place to make planning applications) than for a similar planning application from a company that rarely develops and must 'learn' the correct method of making an application. As the former is more likely to be a large company and the latter a small company, it would appear probable that investment is more likely to be deterred amongst smaller companies who are only 'occasional' users of the planning system than amongst larger more frequent developers.

Finally, it has to be borne in mind that the transaction costs of the planning process are one of the key economic levers those making planning policies possess. One reason why locational policies such as those steering retail developments to town centres are effective is that potential developers are unlikely to spend the money and time involved in making repeated applications for development running counter to development.

9. To what extent are high occupation costs in England likely to be due to planning constraints, or due to other factors such as imperfect competition or lack of transparency in the land market? What is the economic impact of these costs in terms of the main drivers of productivity?

There is little hard evidence about the impact of land use planning on occupation costs, and there is a sense in which this absence of evidence provides its own answer to the question. This is particularly marked given that these costs are again one of the key economic levers planning policy- and decision-makers have to influence developer behaviour.

London has some of the highest land and rental costs in the World. Typical data shows that space in British cities is about twice as expensive as that in similar sized and wealthy European counterparts and that the highest costs of all are to be found in London.

It should be recognised that these higher rental costs are not solely due to planning. Particularly for Central London, high rental costs whether for retail or office use, are mostly down to agglomeration economics, reflecting the high demand from both retailers and business to be sited within Central London.

The fact that London is densely populated makes it optimal for companies to use less land and more of other inputs, relative to other areas of the UK and indeed other countries such as the USA, France and Germany, where land is more abundant. A high price of land relative to other inputs sends a signal to companies to do exactly this.

So, for example, we find that the example of agglomerated areas such as Central London show that high occupation costs need not be a barrier to productivity. Within Central London, occupation costs are the highest in the UK but so are productivity levels.

However, companies would clearly benefit from a reduction in occupation-costs. In terms of economic theory, a reduction in costs for business through a reduction in occupation costs would leave more money for business to finance research and development and investment and therefore potentially raise productivity levels (or lower costs to consumers and so increase overall consumption leading to increased economic activity in the economy overall).

The UK planning system can raise land costs in two ways. Firstly, by limiting the amount of overall development land available and secondly by limiting the amount of land available for each category of use.

The existence of any type of planning system that regulates land use will tend to raise land costs above the level that would exist without such a system. Therefore, for example, policies limiting the potential land for housing, retail or office developments, will have the effect of raising occupation costs across the remainder of the UK.

Also important, however, is the fact that the planning system raises occupation costs for certain types of development through its allocation of land to particular land uses. Without such a system, adjacent areas of land would be expected to be similarly priced. However, under the UK planning system, adjacent sites of land can have very different occupation costs depending on the use class which has been assigned to them by the planning system. Thus, it is arguable that high occupation costs for some retail, office and residential land across the UK stems from a lack of provision of retail, office and residential land in these areas through a lack of designation of such land by the planning system and an over-provision of other types of land such as industrial and agricultural.

In the case of London, one way in which these restrictions could be eased in order to allow for a reduction in occupation costs across the city would be to reduce the extent to which sites are designated a single use-class and leave more land available for the market to determine its optimum use. The most obvious effect of such a policy would be to sharply reduce the amount of land used by industry within Inner London. Market prices would lead to other land-uses, particularly housing, taking the place of much industrial land (particularly when it is near to public transport) at such sites, and industrial activities such as logistics and warehousing moving further away from the centre of London to areas where demand for land is less intense.

To the response that this would remove vital land required for logistics, warehousing etc, the fact is that there is no reason why location decisions for such industries should not be based on market prices, rather than planning designations. Such industries balance the costs of land and transport etc when making location decisions, and if occupation costs (for industrial uses) rose close to Central London, they would simply shift more costs towards transport by moving further away from the Centre of the City.

10. How does the planning system impact on competition, through influencing barriers to entry and exit and economies of scale? If there are areas where there is a negative impact, how can these be addressed, while protecting other goals of the planning system?

As we have shown above, if planning is to be effective in either delivering on its underlying rationale, or in delivering wider policy objectives, the way it impacts on the economy, and the combination of market signals, incentives and disincentives it sends out, need to be understood and applied more clearly and systematically than they are currently.

As far as competition is concerned, the crucial issue is how to build flexibility into the system and also how to prevent the playing of the system in such a way as to allow acquisition of monopoly positions within the planning process. This applies both to land banks and to too rigid an application of, for example, sequential tests.

High levels of entry and exit for firms within an industry improve competition by³:-

- Raising allocative efficiency through replacement of low productivity stores with high productivity entrants which increases aggregate productivity.
- Efficiently organising production as entry may induce incumbent firms to organise work more effectively and to learn through imitation from new entrants who are using superior technology or superior organisational structures.
- Increasing innovative activity as entry or the threat of entry may increase the efficiency and innovative efforts of incumbent firms.

Low levels of entry therefore reduce each of these competitive effects, hindering industry productivity and potentially raising prices to consumers.

In terms of evidence, research on the US retail sector suggests that reallocation effects were responsible for virtually all of the booming productivity growth witnessed during the 1990's.⁴ In other words it is the opening of stores, by either new or existing firms, that has underpinned US retail productivity. UK research, by contrast, has shown that productivity improvements in the UK retail sector are less likely to be due

³ *The UK's Productivity Gap – What research tells us and what we need to find out.* ESRC Seminar Series 2004.

⁴ *The Link Between Aggregate and Micro Productivity Growth: Evidence from Retail Trade,* Foster L, Haltiwanger J & Krizan C.J July 2002.

to entry/exit effects suggesting that entry restrictions in the UK may be hindering productivity growth in this sector.⁵

It follows therefore that barriers to entry have negative consequences on competition and therefore on productivity. It should be noted at this stage that there is a difference between barriers to entry and impediments to entry. Barriers to entry are factors that prevent entry into an industry and are being considered in this answer. Impediments to entry are factors that delay, but do not prevent, entry into an industry. These are discussed in the answers to questions 7 & 8

There are many potential barriers to entry for business. In the UK retail sector, for example, capital requirements and access to distribution channels in an increasingly vertically-integrated industry are barriers in many retail sectors and may well be more significant than any planning related barriers.

Nevertheless, planning systems can create barriers to entry. For example, the setting of quantitative limits on floorspace in a given geographical area can have the effect of restricting competition by barring access to potential new entrants. This is especially likely when limits are endorsed by established businesses through their involvement in the decision process. The influence of local lobbies on local authorities may make entry particularly difficult for outsider (or foreign) companies wishing to enter local markets.⁶

Using the example of retail, at present quantitative limits on retail development are not set by the UK planning system. However, according to PPS6, local planning authorities will in future have to assess the need for new retail floorspace, taking account of both quantitative and qualitative factors. The authorities are then to identify and allocate suitable sites to meet this need.

Such a policy, if applied rigidly, could well cause the difficulties highlighted above in terms of barring access to potential new entrants. For example, the policy of setting quantitative limits means:-

- 1/ there is scope for local authorities to underestimate the need for retail floorspace.
- 2/ there is scope for local authorities to fail to identify and allocate enough suitable sites.

Additionally, even if the planning authority accurately identifies the need for floorspace and then identifies and allocates enough sites, it is important such a process does not seek to achieve 100 per cent utilisation of sites. Such a move would not encourage rapid entry/exit from the industry and would instead strongly benefit incumbents.

To understand why this is the case it is necessary to understand that the process of competition in an economic market will frequently lead to a temporary 'oversupply'

⁵ 'Productivity in UK Retailing' – Evidence from Micro Data, Haskel J & Khawaja N – Presentation OECD Nov 2004.

⁶ *Regulatory Reform in Retail Distribution*, Boylaud, O, & Nicoletti, G – OECD Economic Studies No 32. 2001

of a good as new entrants enter the market, seek to undercut existing players through better productivity, and over time force the least productive player out of business.

From the point of view of economic productivity, therefore, retail sites ideally need to be identified not just to meet the 'need' for retail floorspace (i.e. to match demand and supply) but ideally to provide a surplus of available floorspace, allowing the potential for new entrants and stronger competition.

Therefore, planners ought to ensure that sufficient land is made available for all different sectors of the economy, retail, office etc such that competition effects are allowed to proceed as described above.

The need for availability of potential retail sites is heightened by the fact that when only a limited amount of retail development land is available, there is a strong incentive for existing major players to acquire this land at above market prices in order to prevent new firms from entering the market. In other words, a lack of available sites can encourage rent seeking activities whereby resources are devoted to playing the system to extract pre-emptively permissions or build up land banks which largely deny others development opportunities rather than towards improving productivity and competition benefits to consumers.

In the case of London, however, demand for land is high from many different sectors and this creates additional problems. Planners are aware that having surplus land set aside for particular uses may not be the best use of that land to the economy overall. However, this lack of surplus land makes it even more important that planners seek to encourage and not constrain the take up of development opportunities. Equally, it points to the importance of there being flexibility in the planning system in terms of land use classifications, such that land can be used (allowing for social and environmental factors) according to market demand i.e that land use classification decisions are responsive to changing market conditions.

For example, the benefits from competition will be enhanced if 'need' is not used as a means of preventing a new entrant from entering the retail market. As explained above, a temporary oversupply of a product should be considered a good thing, not a problem. Competition and market forces will act in such a situation to ensure that the productive firms survive and the unproductive firms close. Furthermore, if this leads to some existing sites closing down this again should not be considered a problem. Given the demand for land in London is high, a new more productive economic use of these sites is likely to arise within a short period.

11. To what extent does the planning system effectively support innovation through fostering the formation of business clusters and wider agglomeration of economic activity?

London provides many examples of the existence of agglomeration and business clusters, from the business centres of the City of London and Canary Wharf to the retail clusters in the West End. In other words London demonstrates that agglomeration and business clusters are a fundamental part of a modern economy.

It is the existence of these clusters, and the high density of development that is a key element of agglomeration, that make the productivity of London workers substantially higher than that of workers elsewhere in the UK

The existence and location of these clusters and agglomerated areas are the result of location decisions made by private companies over a long period. In much of London, these clusters are of long origin, predating formal public sector planning, although the planning system has tended to reinforce them since its introduction. In other places, agglomerations have been the more direct result of public planning decisions, such as the development of Docklands. Both kinds of clusters are heavily influenced by issues that have been influenced by planning, such as transport. However, there are limits to the extent to which it is possible for the planning system to foster business clusters "from scratch"; they will thrive because of individual decisions of many private companies to locate in areas where they can benefit from the spillovers of co-location. This can be helped or hindered by planning decisions, but other than in exceptional cases, are unlikely to be started by them.

Productivity is higher in agglomerated areas of London because agglomeration and clusters provide the ability to create 'deep' markets, that is markets in which there is a lot of choice. This can be particularly relevant to labour markets, where job search can be easier and the matching of jobs to people can be better done. There is the ability to exploit economies of scale – not just in production, but also in marketing and sales. This can also extend to the ability to exploit a niche, where specialisms which would be impossible in a small market can survive in a large one. And finally there are network benefits. Bringing people, activities and skills together generates spillovers. These may be of knowledge, for example networks which enable universities to get together with business. They may be of ideas, for example cultural activities which provide excitement and innovation. They may be in finance, for example the ability to find someone who is interested in what you have to offer.

In terms of planning, therefore, the key question is whether planning aids or hinders this market-led trend to cluster and agglomeration. One way that planning can help promote agglomeration economies in urban areas is by helping limit congestion (which the process of agglomeration will be increasing). This benefit could be termed the management of infrastructure and a positive example may include investment in transport infrastructure in a congested location to encourage further development and agglomeration benefits at that location. The biggest single benefit the planning system could bring to London's growth over the coming decade is therefore to ensure a smooth and successful implementation of Crossrail. This would increase transport capacity into the most successful agglomeration areas of Central London allowing these areas to expand further bringing additional high-productivity jobs to the UK economy.

The opposite is also true and a misguided planning policy could hinder the benefits of agglomeration. For example, managing congestion by simply restricting the process of agglomeration would harm growth, as would using planning to constrain the physical growth of urban areas. However, such an approach is not policy in London and the London Plan strongly supports further development in agglomerated areas of Central London where productivity is highest. It is important that such policy is supported by national government and planning policy.

15. *Economic development can help achieve the regeneration and renaissance of urban and rural areas. Are there ways which planning could strengthen economic performance in regions, sub-regions (including city regions) and at the local level?*

To achieve regeneration, it is important that where possible private development that can introduce jobs and economic development to an area is encouraged. To this end, unnecessary restrictions to development in regeneration areas need to be avoided, subject to maintaining environmental needs.

On the subject of retail regeneration, GLA Economics found two key constraints in the planning system that have restricted the potential of retail regeneration but which through a change in approach planning could aid regeneration in the future.

The first is simply the need for local authority planners to fully engage the retailers who can help regenerate an area, and then to take the opportunities that arise, rather than introducing delay. Use of masterplanning as a means of delay has been mentioned by developers as having occurred on a number of occasions (i.e. rather than agree to a major retail development in an underserved area, local authorities have decided that a masterplanning process must take place first). It is important that local authorities understand that in the context of underserved areas, potential retailers may, and indeed do, simply go elsewhere and that the offered development may no longer be on the table a year hence.

The second issue is more fundamental and involves the fact that the location of retail development as set out in the sequential test in PPG6 and the new PPS6 often conflicts with the needs to serve underserved markets (in need of regeneration) . In other words, while PPG6 encouraged retail development to occur in town centres, an underserved area is in many instances not near a town centre. In such a case, retail planning policy actively discourages major retail investments in underserved areas.

However, this issue has clearly been partially recognised in the drafting of PPS6 and there are frequent mentions of regeneration and deprived areas within the new guidance. Examples include:-

“In areas...where deficiencies are identified in the existing network of centres, new centres may be designated through the plan making process, with priority given to deprived areas.”⁷

“New centres should be designated through the plan-making process where the need for them has been established, with priority given to deprived areas where there is a need for better access to services, facilities and employment by socially excluded groups.”⁸

⁷ Paragraph 2.7

⁸ Paragraph 2.53

This new advice clearly recognizes that there exist cases where underserved areas are not located near to existing centres and that in such cases new retail provision within the underserved area is to be encouraged. This appears a clear improvement upon PPG6 and allows the possibility of retail led regeneration occurring more regularly in deprived areas in the future.