



Barker Review of Housing Supply –

***“In response to your invitation for observations,
we are pleased to submit the attached letter.”***

Barker Review of Housing Supply
HM Treasury
1 Horse Guards Road
London
SW1A 2HQ

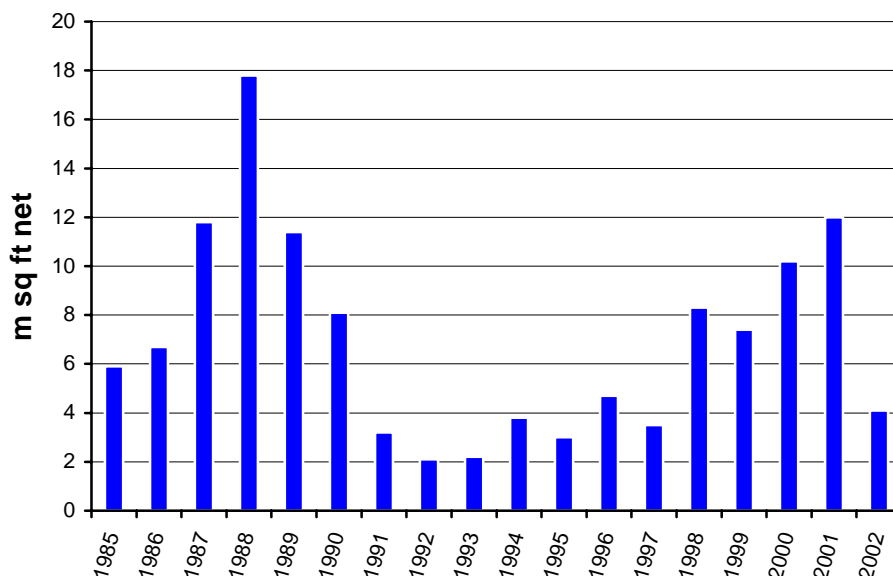
Dear Madam

OBSERVATIONS FROM LONDON RESIDENTIAL RESEARCH ON YOUR REVIEW OF HOUSING SUPPLY

You have asked for written submissions to be as brief as possible. Accordingly I shall limit my comments to just one issue. Is the planning system a major factor preventing new housing output being more responsive to rising demand and capital values? My comments only apply to London.

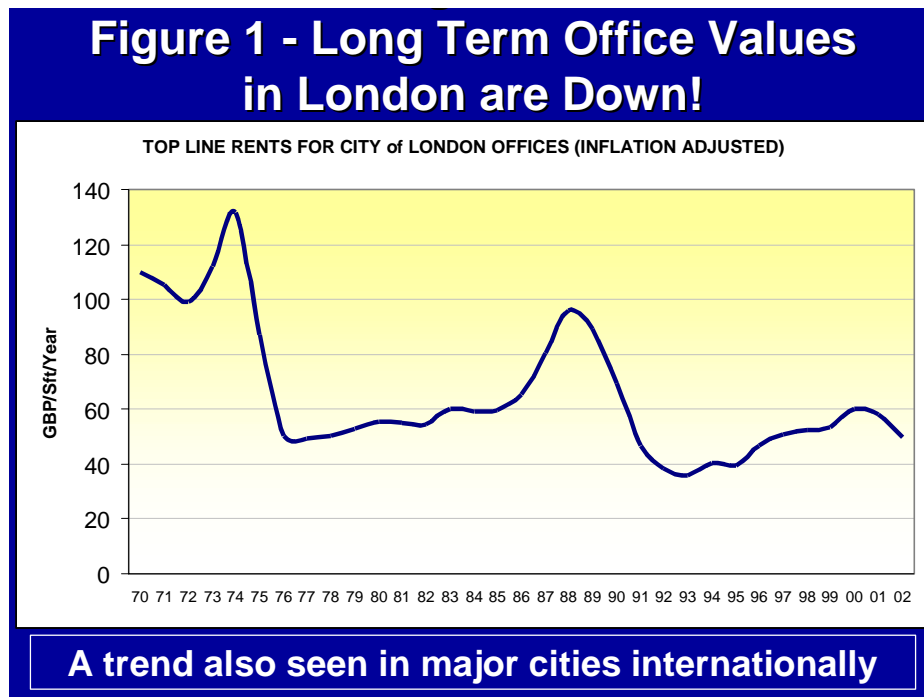
The planning regime in London works very differently for offices and housing, without deliberately setting out to do so. Figure 1 shows that office development in central London and Docklands is highly elastic in responding to demand and rising rents.

Figure 1 - Central London Office Construction Starts 1985-2002



The planning regime for office development in London is in effect deregulated. By this we mean that there are strong policies to promote office development in central London, particularly in the City of London and Tower Hamlets. This essentially "*laissez-faire*" approach is based around a strong strategic policy emphasis to provide sufficient new office stock to maintain and enhance London's "World City" role. Planning gain requirements for large-scale offices in The City and Docklands are minimal. Indeed, policies to promote office development have been so successful, that office rents have gone down in both nominal and in 'inflation adjusted' terms since the mid 1980s, as shown in Figure 2.

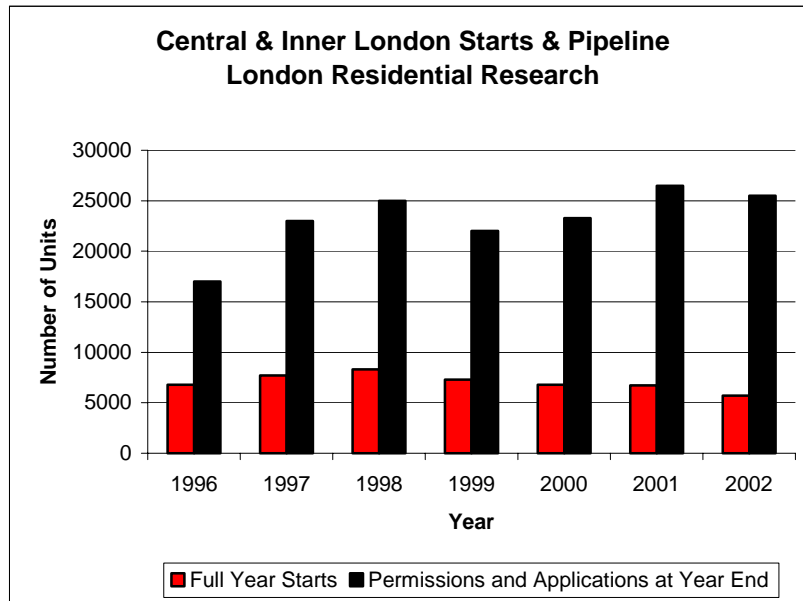
Figure 2 – Long Term Rental "Growth" for City of London Offices



In contrast, the residential planning regime is in practice highly regulated. Residential developers frequently complain that the planning system is a nightmare journey of uncertainty, delay, community opposition to any change in the local street scene, and unreasonable requirements for a wide range of "community goodies". Most problematic of all the obstacles, they claim, is the affordable housing issue, which is of course a form of hidden taxation, whether it hits the land owner, which is often the public sector, the developer, or the buyers who end up paying more for less. Again, we have a good deal of sympathy with this general sentiment.

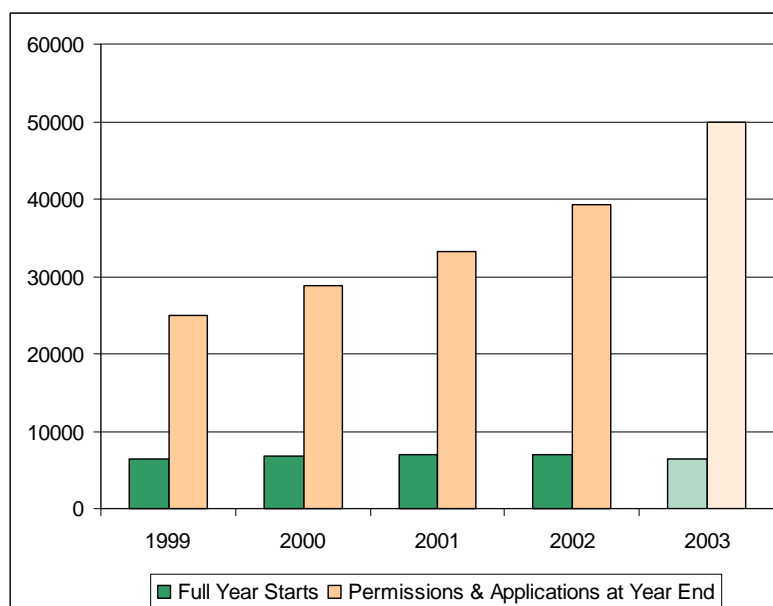
However, when we look at the hard statistics, it appears that it is not the planning system which is preventing higher levels of new private sector building, at least not in central and inner London. Figure 3 shows private sector housing starts in central and inner London for each year since 1995, compared with the planning pipeline. Clearly, the rate of starts has remained static since 1995, at around 5,500 - 7,000 units a year. (How do we know these figures are correct? Because we go and look at every site, as part of our business, that's how).

Figure 3 – Private Residential Construction Starts V Year End Planning Pipeline in Central and Inner London 1996 - 2002



If we analyse the data for each year, we can see that there has been an actual decrease in starts in real terms, from 6,000 units at end 1996 to only 5,200 at end 2002. Simultaneously, the number of new private sector homes with planning permissions and applications at each year end has been on the increase. This figure has grown from around 17,000 at end 1996, to around 28,000 at end 2002. Consequently, starts as a proportion of the potential planning pipeline have actually decreased from around 35% in 1996 to 19% at end 2002. If we look at the same data for outer London, but for a shorter period, the same story emerges.

Figure 4 – Private Residential Construction Starts V Year End Planning Pipeline in Outer London 1999 - 2002



So why has output not gone up, when the planning system has created the extra capacity, despite popular opinion to the contrary? We suspect there are three main reasons.

First, the central London market is dominated by no more than half a dozen developers, who between them account for over 50% of output. They are Berkeley Group, including St George and St James, Barratt, Galliard, and Ballymore. They build at a rate they are comfortable with, both in terms of market conditions, and their management and construction capacity. Technical regeneration skills are in short supply. Construction capacity is heavily constrained by skills shortages, not least competition for labour from public sector work. In terms of market conditions, most developers we deal with have been expecting a downturn in London since the stock market turned down in 2001, despite public utterances of super confidence. They know that a market which depends on investors for 70% of sales could go "pop" at any time, even though it is still holding up surprisingly well.

The second reason is that a planning permission doesn't automatically mean you can start build. A high proportion of land with a residential planning permission in London has an existing use and "income stream" to use the jargon. Private owners running businesses like car repairs have to sell for a high price to relocate the business or live off the proceeds of the sale. Today's "minor millionaires" will not live in luxury off interest earned, even disregarding the double taxation of capital gains tax and then tax on investment income. A lot of land with planning permission is not "oven ready" in the jargon of the industry. (The whole essence of affordable housing policy is to tax the land owner, but in reality one sure way to speed up the flow of land would be to offer capital gains tax breaks for land brought forward for affordable housing use).

Third, and here the planning system is at fault, planning permissions often require developers to build units for which there is limited demand, particularly 3 bed units. Many London boroughs hold families in high esteem, and regard pied-a-terre types as undeserving cads and bounders. In central London, developers struggle to sell 3 bed units for £500,000+, but can still sell studios and 1 bedders at up to £250,000 quite easily. The planners should let the market decide the size of units to be built for private sale.

If you would like us to expand on any of these points, or send you a copy of our annual report on Residential Development in London, please let me know.

Yours sincerely

GEOFF MARSH