The 2022-2032 Affordable Housing Funding Requirement for London

Executive Summary

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Greater London Authority
City Hall
The Queen's Walk
More London
London SE1 2AA
www.london.gov.uk
enquiries 020 7983 4100
minicom 020 7983 4458
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Working in partnership with the G15

This report has been produced in partnership with the G15 group of London's largest housing associations. It uses G15 data and was shaped through a working group with its members.

G15 members house one in ten Londoners and are the biggest providers of affordable homes in the capital. Together, they own or manage more than 600,000 homes and build more than 10,000 new homes each year.

Housing associations were set up to support people in housing need and this remains at the heart of everything G15 members do today. They are independent, charitable organisations and all the money they make is reinvested in building more affordable homes and delivering services for residents.

The G15's members are A2Dominion, Catalyst, Clarion, Hyde, L&Q, Metropolitan Thames Valley, Network Homes, Notting Hill Genesis, One Housing, Optivo, Peabody and Southern Housing Group.

Find out more at: g15.london

Executive Summary

0.1 The Mayor's draft new London Plan has identified capacity for 65,000 net new homes a year in London[1]. The draft new London Plan also includes a strategic target for 50 per cent of all new homes delivered across London to be genuinely affordable[2]. This report summarises a technical analysis of the amount of public sector grant funding required to deliver 50 per cent of 65,000 homes a year as affordable.

0.2 In addition to meeting the need for housing in London, building 65,000 new homes each year, with half affordable, may help the economy to expand significantly. Previous analysis[3] supported by the Mayor of London and the European Union established that building new homes brings a net economic benefit to the Exchequer, as dealing with the housing shortage overcomes a significant constraint on the capital's future economic growth.

0.3 The analysis has modelled the evolution of costs, revenues, and sales values until 2031/32, using the new draft London Plan evidence base and central Government data sources where possible. The parameters were developed by a working group comprised of senior experts involved in building thousands of London's new affordable homes every year.

0.4 The analysis predicts a widening gap between costs and revenues. Works costs are estimated to increase by 3.4 per cent per annum over the five years to 2023, while sales values are expected to only increase by 0.9 per cent a year until 2023. Social rents will reduce by 1 per cent annually until 2020 and are expected to subsequently increase by less than 3.5 per cent per annum.

0.5 After accounting for these cost and income trends, the model identifies average subsidy gaps (the amount needed to 'plug the gap' between costs and income) of £284,000 per social rent home and £32,000 per shared ownership home over the 2022/23 to 2031/32 period. These subsidy gaps can be plugged through a combination of in-kind financial contributions on private-led developments ('Section 106'), 'cross-subsidy' generated from the sale of market sale homes built by affordable housing providers, and Government grant.

0.6 The new draft London Plan identifies capacity for 65,000 new homes a year, 50 per cent of which should be affordable, and the 2017 Strategic Housing Market

[1] GLA, Draft New London Plan, Chapter 4: Housing https://www.london.gov.uk/sites/default/files/draft_london_plan_chapter_4.pdf
[2] Ibid.
[3] Greenwood Strategic Advisors, Mind the gap: Funding and financing city investments in the 21st century, 2018 https://www.greenwood-ag.com/files/MindTheGap-FullReport.pdf

Assessment[4] identified a high level of need for social rent homes (72 per cent of all affordable homes) in London. The central scenario in the model therefore comprises an Affordable Homes Programme of 325,000 new affordable homes (32,500 a year) running from 2022/23 until 2031/32, with a split of 70 per cent social rent, 20 per cent shared ownership, and 10 per cent intermediate rent.

0.7 The central scenario contrasts with London's 2016-22 Affordable Homes Programme, which is set to deliver around 16,600 affordable homes per year on average, with the tenure split weighted more heavily towards shared ownership due to restrictions on how funding can be spent imposed by the national Government.

0.8 The subsidy gap between the cost of building 325,000 affordable homes, and what can be borrowed against and realised from the income streams of those homes, is £74.5 billion over the ten-year period. This is an average of £7.5 billion a year.

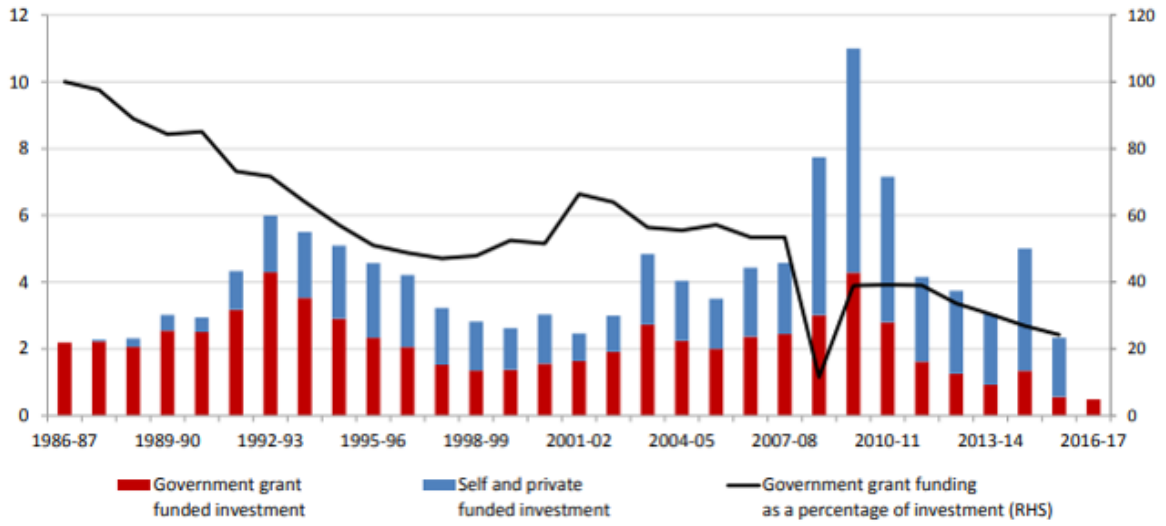
0.9 Assumptions adopted for the purposes of this research suggest that 9,600 affordable homes could be supported by private developers each year, equivalent to a financial contribution of £2.3 billion a year. This leaves a subsidy gap of £5.2 billion a year to be filled from other sources.

0.10 Affordable housing providers (both housing associations and councils) are expected to build an average of 5,700 market sale homes a year, reinvesting the profits into new affordable homes. This market sale delivery generates 'cross subsidy' of an average of £0.3 billion a year, with the ups and downs of the housing market leading to significant income variability across the new programme period.

0.11 The grant required to deliver a new affordable homes programme of 22,750 social rent homes, 6,500 shared ownership homes and 3,250 intermediate rent homes is therefore estimated to be £4.9 billion per year (nominal). This is equivalent to grant covering 48 per cent of the costs of non- Section 106 affordable homes, a figure which is at the lower end of the typical range of grant rates prior to 2008 (see Figure 1 below).

[4] GLA, Strategic Housing Market Assessment (SHMA) 2017, 2017
https://www.london.gov.uk/sites/default/files/london_shma_2017.pdf

Figure 1: Housing provider gross investment by source of finance (£ billions, 2017-18 prices) and grant funded investment share of investment in England (Capital Economics/Shelter, 2019)



0.12 This level of grant is equivalent to around seven times what London currently receives. The significant increase is primarily due to the larger size of the new programme, the new programme's focus on social rented housing, and expected cost inflation. The analysis also demonstrates that a larger programme would lead available cross-subsidy to be spread across three times more rented affordable homes than under the 2016-22 Affordable Homes Programme. The analysis also demonstrates that even when costs and revenues increase at the same rate, grant must also increase in cash terms.

0.13 The calculations underpinning the central scenario have been subjected to sensitivity analysis, testing the impact of changes in key parameters. For instance, the grant requirement would be significantly higher if the predicted increase in affordable housing delivery on private-led developments does not materialise. This demonstrates how strong planning policies relating to affordable housing can serve to reduce the cost to the Exchequer of expanding affordable housing supply.

0.14 The analysis also explores different programme scenarios that have lower subsidy requirements, such as through delivering fewer than 32,500 affordable homes or tenure mixes that are not consistent with London's needs. While all these options can reduce the subsidy gap, in every scenario the grant requirement remains at least several multiples higher than the £690 million per annum London currently receives. Even repeating the 2016-22 Affordable Homes Programme after 2022 would entail grant increasing to around £1 billion per annum.

0.15 In conclusion, the analysis supports the basic and inescapable economic logic of funding social rent homes in London. Doing so requires subsidy, and due to past and forecast cost inflation the level of subsidy per home needs to be far greater in cash terms than even a decade ago.