

# Housing across the lifecycle

## Project summary



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### Summary

Housing wealth is for many Britons a focus of aspirations and a source of security, and it is an increasingly important political issue. But there are two major problems with how housing is financed, affecting different points of the lifecycle. At the start of adult life, the benefits of homeownership increasingly depend on parents' wealth or location, with damaging consequences for social and geographical mobility. For older people, much housing wealth is dormant and under-used – even as retired homeowners struggle to cope with low incomes. This project aims to formulate policy solutions to both these problems.

The rest of this document outlines:

- Political and policy context
- Key components
- Dissemination and stakeholders
- Why ippr?

The project is due for completion at the end of 2005.

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## Political and Policy Context

Both Tony Blair and Michael Howard have explicitly made access to homeownership a priority of the next parliamentary term. The total net value of housing wealth increased more than 40 times over in nominal terms between 1970 and 2001 (Holmes 2001), and it now accounts for almost half the net personal wealth in Britain (Inland Revenue 2004). For the individual, homeownership has important economic benefits, easing access to credit and asset accumulation. Although it is not suitable for all – and policy-makers should not encourage it for all – homeownership is frequently the focus of aspiration and self-expression. It also contributes to a sense of security.

Yet the financing of homeownership is far from perfect. Early in the lifecycle, access to homeownership is increasingly difficult – an index of first-time buyer's ability to pay is now at its lowest level since 1990 (Vass 2004). For many, this makes a house purchase dependent on parental contributions: research for the Joseph Rowntree Foundation showed that when parents owned their home, but their children did not, the parents expected to contribute an average of £17,000 to their child's first purchase (MORI Omnibus 2004).

The consequences are severe. A society cannot claim to have achieved equality of opportunity if access to such a major asset depends on one's parents; nor can an economy easily adjust if labour mobility is constrained by unaffordable housing.

One cause of the problem is that housing supply is slow to respond to demand – but it is not the only cause. The government has largely accepted the recommendations of the Barker Review into housing supply (Barker 2004), but even when all recommendations are implemented, the Sustainable Communities Plan has accelerated house building in growth areas, and the current buoyancy in the housing market has deflated, access to homeownership will still be restricted unless housing finance is also reformed.

Later in the life cycle, there is an increasing disparity between pensioners' low incomes and the high values of houses they own. In 1999, 67% of couple pensioners, and 53% of single pensioners, could be placed in the "wealth rich/ income poor" category (Rowlingson et al 1999), and people aged 65 or over may now hold as much as £460 billion worth of unmortgaged equity in their homes (Council of Mortgage Lenders 2004).

Using this wealth, perhaps by helping pensioners to release equity or trade down to smaller homes, might have the potential to help improve pensioners' incomes and alleviate some of the poverty caused by inadequate savings. It could contribute to solving the problems around council tax, inadequate pensions, and the funding of long-term personal care, amongst others. Reassuringly, it is also distributed more evenly than pension wealth or non-pension financial wealth, although not to the extent that would be required to be an alternative to private pension schemes (Pension Commission 2004).

As a result, some have argued that the size of the equity release market will grow from £2.8 billion in 2003 to £100 billion in coming years (Council of Mortgage Lenders 2004), as the need for extra money in old age is increased by longer life expectancy, more expensive care, and lower-value pensions. But others have struck a note of caution. The



Consumer Association issued a warning in 2003 against “inflexible and expensive” products, and there is a danger that homeowners will believe that equity release can be an alternative, rather than a supplement, to pension saving. Take-up is constrained by low consumer confidence, uncertainty over the final cost and high interest rates – the lenders must cover both the longevity risk, that a homeowner could live for a long period of time, and the investment risk, that the property could be worth less than the outstanding loan when the homeowner dies. On the lenders’ side, reputational risk may be preventing new products being offered.

What is needed is a clearer understanding of the costs and benefits of equity release, and of when public policy should encourage equity release. The different forms of releasing housing wealth can be made safer, cheaper and more effective.

This project comes at a time when the importance of housing as an asset is moving up the political agenda. The Treasury commissioned a report on housing supply (Barker 2004), one on fixed-rate mortgages (Miles 2004), and a consultation on the regulation of certain equity release products (HM Treasury 2004). The Deputy Prime Minister, meanwhile, as part of the sustainable communities plan, commissioned a task-force to look at low-cost homeownership (2003), and has encouraged ways to share ownership between tenants and local councils or registered social landlords.

The project also feeds into broader debates about asset ownership. Recent evidence has suggested that even moderate levels of wealth could help life chances, encouraging individuals to plan ahead and cope with unexpected expenses. New policies to spread opportunity through asset ownership have included Child Trust Funds, which from April 2005 will endow all new-born children with an initial £250-£500 to be used when they reach 18; and the Saving Gateway pilot, providing a government match to the savings of the poor.

There has been a corresponding burst of productive energy in the private sector. Recently-introduced products have included mortgages to which parents contribute and are liable, an increase in 100% and even 130% loans and some pilots of equity-only loans.

The role of housing across the lifecycle is unlike any other asset. Housing is an investment good, a consumption good, and a source of personal pride. This project will suggest policy reforms designed to make the process of accumulating and running down housing wealth as effective and fair as possible.



## Key components

The final output will be a published report, consisting of a context paper, a section on access to homeownership, and a section on releasing housing wealth. These are elaborated on below. Before then, a media-friendly chapter will be released to raise interest, and three high-level seminars will be held to discuss the main ideas and policy conclusions.

Context paper: what makes housing different?

A background paper will bring together the key themes that unite the project. The two main questions are:

- a. *How is owning a house different to owning other kinds of assets?* At both ends of the lifecycle, a house is seen as qualitatively different to other forms of assets. What makes housing wealth different, and what are the implications of this for the rest of the project? Separate benefits can be identified for housing as an investment vehicle and a tenure choice.
- b. *When, if at all, should public policy encourage homeownership?* Homeownership is not suitable – or sustainable – for all, and very high levels of homeownership could reduce labour mobility. Yet there is a strong sense in the UK, shared with many Anglo-Saxon countries, that public policy should help people to get on the housing ladder. This part of the context paper will look for robust reasons why homeownership should be supported, as well as identifying in what circumstances support is inappropriate.

Strand one – access to homeownership

### 1. Literature review

- a. *Which groups are particularly excluded?* For example, immigrants, north-south migrants, children of non-homeowners, ethnic minorities, and some Muslims who may be excluded by Sharia laws on paying interest (although some Sharia-compliant mortgages are now available).
- b. *What are the main financing barriers?* Basic affordability, and the ratio of house price to income, is the main driver of access to homeownership. But what are the barriers on the financing side? How important is the deposit relative to monthly payments?

### 2. Policy options

Policy options will draw heavily on the analysis above to select a focused and coherent package. Although housing supply is important it will not be looked at here. Options examined could include, but will not be limited to:

- a. *Tax changes*, such as stamp duty relief for first-time buyers (FTBs). Australia



currently exempts stamp duty for FTBs up to a certain limit; their experience would be examined.

- b. *Grants and loans.* We could learn from both Australia and the United States: the Australian First Home Owner Grant, established in 2000, provides AU\$7,000, about £2,650, for any Australian first-time buyer, without means testing or spending restrictions. Bush's American Dream Downpayment Initiative, signed into law in December 2003, is more generous (up to £\$10,000), but has restrictions on both spending and eligibility.
- c. *Changes in mortgage terms.* Innovative forms of credit-scoring and mortgage underwriting are being developed in America by Fair Isaac Corp and Country Home Loans, to recognise the contribution of pooled family savings or community funds as down-payment sources, and to allow non-occupant "co-borrowers", such as uncles or grandparents, to add some of their incomes to the primary home buyer's in order to qualify for the mortgage. Some of these changes are already taking place in the UK market, particularly joint mortgages between parents and children. It is possible that more could be done, though, to improve joint mortgages between friends; to further end-load the repayment profile to recognise that earnings rise over time; or to introduce private equity loans. Equity loans were recommended recently by an Australian commission on home ownership. Although they may be unpopular in the UK given recent gains in the property market, and might not deliver the best investment returns, they would open the tenure benefits to those currently excluded.

## Strand two - releasing housing wealth

There are three main ways of releasing housing wealth: commercial equity release schemes, tax deferrals, and moving to a smaller home.

### 1. Commercial equity release schemes

Equity can be released through "lifetime" mortgages, in which the interest is rolled up and repaid at the end of the loan period, or through "home reversions", whereby the homeowners sell all or part of their homes in exchange for a lump sum or a regular income. But this leaves two questions:

- a. *Should equity release schemes be encouraged?* For pensioners, equity release schemes increase income and provide security. For the government, they may ease the pension crisis or provide funds for long-term personal care, currently means-tested. Yet some people in the financial services industry have voiced the concern that equity release could be "the next big mis-selling scandal": the values of houses fluctuate, and most houses will not have enough equity to provide an adequate pension. Because of the inherent risks involved and the lack of cash flow for lenders, equity release products are expensive. How seriously should the government and others take these concerns, and how should they respond to them? What would the effects of more widespread equity release be on housing supply, inheritance tax yields, saving rates and other areas?



- b. *How can equity release be improved?* What action can the government and others take to minimise or pool the risk born by the industry and consumers? What are the main obstacles?

## 2. Deferring council tax payments until death or house sale

Council tax could be deferred against housing wealth for those over a certain age and with a minimum level of equity. Denmark, for example, allows pensioners to defer their annual housing tax until the house is sold. This could release moderate sums for pensioners: the average council tax in 2004-5 is £1,167 before transitional reliefs and benefits or rebates (Office of the Deputy Prime Minister, 2004). Would this be popular, or would it be seen as inheritance tax through the back door? Who would benefit, and who might lose out? Is it clearly more efficient to do this through government rather than private companies? And would administrative burdens be prohibitive?

## 3. Making it easier to move down the housing ladder

If a pensioner is living in a home larger than their requirements, but has low income, then in theory he or she could release funds simply by moving to a smaller house. Trading down from a semi-detached house to a terraced one would release almost £25,000 in England and Wales, equivalent to around 30% of the implicit value of the state pension. This figure falls to £20,000 in Greater London, although it exceeds £45,000 in the North West this figure (Pension Commission 2004). There is often sentimental attachment to the family home, but what other barriers might be preventing them? Could public policy do anything to make it easier? Is there a case for the government treating pensioners differently to other homeowners in this respect?



## Why ippr?

*Housing across the lifecycle* is situated within ippr's Centre for Asset-Based Welfare, and draws on the centre's expertise to complement previous work on how assets can improve life chances, and how the benefits of asset-holding can be extended.

This project also ties into specific work on housing. ippr proposals on "equity stakes", giving ownership shares to tenants of social landlords, were adopted in Labour's 2001 manifesto, and the Social Housing Forum was influential after its report in 2000. We also have a strong history of collaboration with external housing experts. John Hills worked with ippr on the equity stakes proposals. Chris Holmes, Visiting Research Fellow at ippr and a former director of Shelter, has written an ippr pamphlet on *Housing, Equality and Choice* (2003), and will soon be releasing a new book on housing policy. Jim Bennett, from the Policy Unit at Shelter, will soon be starting a secondment in ippr to look at the new growth areas proposed in the Sustainable Communities Plan. And Professor Glen Bramley, from Heriot Watt University, is writing for ippr as part of our Commission on Sustainable Development in the South East.

The research is being carried out by Kate Stanley, Jim Bennet, and Dominic Maxwell.

- Kate Stanley

Kate Stanley is Head of Social Policy and a Senior Research Fellow at the Institute for Public Policy Research (ippr). Prior to joining the ippr, Kate worked in the Policy and Research Unit at Save the Children UK where she specialised in asylum and refugee issues, children's rights and child poverty. Before that she was Programmes Manager for humanitarian assistance programmes in Bosnia, Angola and Lebanon for an international NGO and worked as a Researcher for the Planned Parenthood Association of Ghana and for a Member of Parliament in Westminster.

- Jim Bennet

Jim Bennet is currently a Senior Research Fellow at ippr, on secondment from the policy unit at Shelter.

- Dominic Maxwell

Dominic Maxwell has previously worked as a Research Assistant for a Labour MP, and at HM Treasury, the Overseas Development Institute, and Progress. His first report for ippr, *Fair Dues: Towards a More Progressive Inheritance Tax*, was short-listed for Publication of the Year in the 2004 Prospect Think Tank Awards.



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