



UK COLLABORATIVE  
CENTRE FOR  
HOUSING EVIDENCE

# Thinking outside the box

Exploring innovations in affordable home ownership

Christine Whitehead and Peter Williams

London School of Economics

11 November 2020

[housingevidence.ac.uk](https://housingevidence.ac.uk)

# About the authors

Christine Whitehead is Emeritus Professor in the Department of Economics, LSE and Deputy Head of LSE London

Peter Williams is an Associate Member of LSE London and a Departmental Fellow in the Department of Land Economy, University of Cambridge

## Acknowledgements

Our thanks to Andrew Gall and colleagues at the Building Societies Association for comments and support and for organising the BSA member roundtable and to Professor Ken Gibb from the UK Collaborative Centre for Housing Evidence (CaCHE) at the University of Glasgow for his comments and guidance. We are also indebted to staff from a number of building societies for their feedback at the BSA roundtable as we are to interviewees in UK trade bodies and government departments. A number of international experts very kindly gave us advice on developments in their own countries and we are very grateful to have the support of the European Mortgage Federation and their members.





# Contents

About the authors .....	2
Acknowledgements.....	2
Executive Summary .....	6
1. The Project .....	10
1.1 Background .....	10
1.2 The Products .....	11
1.3 Market Context .....	11
1.4 The Numbers .....	12
2. A framework for analysis .....	13
2.1 Principles .....	13
2.2 The instruments .....	13
2.3 The actors .....	14
3. Government sponsored innovations .....	14
3.1 A typology of government schemes .....	14
3.2 Relative accessibility of the main scheme types .....	20
3.3 A summary of government sponsored schemes .....	21
4. Market products .....	24

4.1 Market structure: incentives and constraints .....	24
4.2 Market schemes .....	25
4.3 Market products: a chronology .....	27
4.4 Progress so far .....	29
4.5 Current innovations .....	30
4.6 Complementary innovations .....	31
5. Learning from customers, UK stakeholders and international experts .....	32
5.1 Findings from customers: the BSA Property Tracker .....	32
5.2 Findings from UK stakeholders .....	35
5.3 International experts .....	38
6. Reflections and conclusions .....	41
6.1 Reflections on the future .....	41
6.2 Barriers to expansion: the market's appetite and capacity .....	42
6.3 How government and lenders might find ways forward? .....	43
6.4 Conclusions .....	45
References .....	50
Appendix 1: Government schemes and market products: chronologies since 1980 .....	52
Appendix 2: Affordable home ownership: Some relevant literature .....	57

# Executive summary

**The Question:** The objective of the project was to clarify the role played by affordable homeownership initiatives both in policy and the market place; identify their growth potential and the barriers they face; and how affordable homeownership might be developed into the future.

**Background:** The support for and promotion of home ownership has been a continuing theme in the UK policy since the early 20th century. Partial equity products have been part of national housing policy in the UK since 1980 when shared ownership (SO) models were first introduced. Since 2013, the market for equity finance into housing more generally has increased and new products are being developed. But government is still the most important force determining market opportunities.

Instruments: We identified three main categories of government initiatives:

- **Part-rent, part own** - especially *shared ownership*; but many variations e.g. *Rent to Buy*;
- **Shared equity** - a wide range of *Homebuy* products involving a traditional mortgage and an equity loan – notably *Help to Buy*;
- **Direct subsidy products** - including the *Right to Buy* and now *First Homes*.

**Savings schemes** and **Guarantees** also play a role in achieving affordable homeownership.

We examined each product by how it addresses three main challenges: overcoming access barriers; reducing the on-going costs of purchase; and modifying the risks involved in buying from the point of view of the three main participant groups - purchasers; funders; and the government.

**Understanding their attributes:** Looking across the three categories:

- most schemes in the first two categories – part rent/part own and shared equity – have involved new building rather than existing homes;
- many of these schemes involve direct government subsidy to ensure the dwellings are built;
- but Right to Buy, the largest scheme, is very different involving the transfer of existing homes which had received subsidy when built and then discounts on the current market value;
- the 1980s were dominated by Right to Buy and Shared Ownership (SO) and its variations –both remain important - including new developments on SO;
- shared equity products, normally involving an equity mortgage grew strongly from the early 21st century and have been the main instruments ever since;
- First Homes is a different form of perpetual shared equity acting as a partial replacement for Help to Buy. It remains to be seen whether it will be a popular option;
- the proposed government mortgage guarantee scheme plays to the strengths of an already accepted instrument, although based on long term mortgages with fixed rates;
- the Right to Buy is the largest and one of the longest running schemes (over 2.6 across England, Scotland and Wales)

in 40 years). Help to Buy only in place since 2013 although of much shorter duration is second in terms of numbers and Shared Ownership (in play since 1980) is third.

SO has proved difficult to scale up for a number of reasons including; the traditional mortgage can only be secured against the proportion bought; the purchaser must pay all repair and improvement costs; most large banks have had little interest in taking a major funding role; in the absence of reliable and regular data it is perceived by some funders to have high arrears; increasing house prices (relative to wages) have slowed staircasing; they also, notably in London and the South East exclude many lower income households so those who can afford SO have been able to afford other products; there are risks to HA providers; and there is no active/widespread resale market for shared ownership homes.

**Market products:** Market based shared and partial equity products mainly address problems in obtaining a deposit or as a way of sharing risks. The two main products can be categorised as mortgage indemnity guarantee schemes and shared equity loans.

Historically the UK has been characterised by having a strong high LTV market - 90/95% and even 100% mortgages. After the GFC a considerable gap in provision opened up which innovators have been trying to fill within current regulatory, risk appetite and macro-prudential constraints.

Currently there are a number of products in play including: an investor funded top up loan blended into the lender's main mortgage product; a Peer to Peer structure where would be buyers join together to collectively fund deposits; long term fixed rate mortgages without a pre-payment penalty at least in the short term; co-investment models bringing buyers and investors together; a project that helps provide mortgage insurance on high LTV mortgages on new dwellings; and possibly a US mortgage provider prepared to take partial equity.

These all have different dimensions, purposes and market potential. Covid-19 impacts have however slowed this innovation process and not least the time taken to get to market.

**Complementary innovations:** There are a variety of 'generational' mortgage and equity release products being developed which in particular help access the 'Bank of Mum and Dad'. However, these are mainly for those purchasing in the mainstream market.

**Consumer and stakeholder views:** We also examined evidence on customer attitudes; interviewed a wide range of UK stakeholders; and surveyed EMF members and international commentators.

**The BSA Survey:** A survey of BSA customers clarified the challenges people face in putting together the deposit given current lending criteria as stronger than having the income for repayments. It also showed that help from family concentrated on the deposit with relatively few helping with monthly payments. Respondents were rather more aware of Help to Buy rather than other schemes.

**UK Stakeholders:** The interviews highlighted tensions around existing products and proposals and the relatively limited number of market innovations that had come forward. There was general acceptance of the need to improve existing offers to lower and middle income households to enable them to access owner- occupation. Since most of these interviews some initiatives have been announced that reflect these concerns – although in most cases the details are still lacking.

**International experts:** Affordable home ownership products are popular across Europe and other industrialised countries. However, our review suggests that there are few schemes that offer notable advantages over what is available in the UK.

More complex affordable homeownership products such as shared ownership and shared equity are mainly restricted to Western European countries with mature mortgage markets and depend on

governments' preparedness to develop the legal and regulatory framework and provide support.

Interest in developing wholly market products is mainly restricted to Anglo-Saxon based countries. Even in these countries these have not taken off, except to a limited extent in the USA.

**Conclusions:** The UK mortgage market is amongst the most innovative in the world – partly reflecting intense competition itself a product of a fairly open banking system. At the same time the market is highly oligopolistic and has been so for decades.

The core - but hardly surprising - finding, is that there is no immediately simple way of transforming the affordability picture for first-time buyers or lower income home owners more generally. What is perhaps more surprising is how little progress has been made on the market front albeit there are perhaps a number of "green shoots".

Government schemes put most of their emphasis on access to homeownership – with a general assumption that affordability will follow. Risk is seen as very much a lesser issue. But many government initiatives have been in response to short term pressures and have been ill-defined and poorly targeted.

We need a clearer view of the scale of the affordable home ownership "gap" – taking account of house prices; incomes; the capacity to raise a deposit and risk attitudes.

From the market point of view there is a degree of necessity building in the market. While the value of loans has gone up, the number of new mortgage loans has been falling. Increasingly the market is built around existing owners. It seems inevitable that the industry must try to re-grow the market.

Our immediate **suggestions** include:

a long overdue reform of shared ownership going well beyond the existing proposals and includes the provision of a comprehensive database;

mortgage guarantees are a cost-efficient way of expanding affordable home ownership opportunities. Here the UK could learn from abroad;

signs that market based initiatives will come forward to help supplement the higher LTV market should be encouraged;

government should set out its vision for home ownership in general and affordable home ownership in particular in some detail, looking at current provision, the risks and the potential scale of demand, funding and supply.





# 1. The Project

In late 2019 the Building Societies Association (BSA) and the UK Collaborative Centre for Housing Evidence (CaCHE) sponsored Christine Whitehead and Peter Williams through LSE London to undertake a project on *Innovative Approaches to Affordable Home Ownership*<sup>1</sup> building on a previous review they had undertaken on shared equity<sup>2</sup>.

The core aim of the project was to clarify the developing role played by affordable homeownership initiatives centred on partial equity schemes such as shared ownership and shared equity both in policy and the market place; to identify both their growth potential and the barriers they face; and how they could best be supported to play a more effective role in ensuring affordable homeownership into the future<sup>3</sup>.

## 1.1 Background

The support for and promotion of home ownership has been a continuing theme in the UK since early in the 20th century. Specifically with respect to partial equity products, these have had a role in national housing policy in the UK since 1980 when shared ownership (SO) models were first introduced<sup>4</sup>. Since that time there have been a whole range of government and private initiatives but few have really achieved scale even though there was considerable enthusiasm not just from government but also the Bank of England and some market players<sup>5</sup>.

What has worked well at least to some extent have been the range of shared equity schemes over the last decade or so with government, builders and mortgage lenders taking part (eg, First Buy, Home Buy and Open Market Homebuy but also some short term developer led and lender led market products) and to a lesser degree Rent Plus type schemes where part owners pay a higher rent to support incremental purchase<sup>6</sup>. The largest equity scheme by far has been the Help to Buy (HtB) equity loan (launched in 2013) which has mixed traditional mortgage funding with equity loans to reduce deposits, repayments and risk. From inception to the end of March 2020 some 272,852 equity loans with a value of £16.05 billion had been advanced in England (plus roughly 10,000 in each of Scotland and Wales up to the end of 2019). Importantly it was not defined as an affordable home ownership product<sup>7</sup> but rather as a way of helping the market to recover from the aftermath of the global financial crisis (GFC).

Much has happened with respect to regulation, the finance market, risk and affordability since the early part of this century and the financial crisis (and subsequently Covid-19). In particular, it has become much more difficult for developers to be directly involved in providing equity loans as they would now be required to be registered and regulated as mortgage lenders – this would be costly in every sense. Equally, mortgage lenders are far more restricted in their capacity to provide high loan to value products, a problem made worse by Covid-19 and the fear that house prices may fall.

1 The research began in early 2020. And was then disrupted by the Covid-19 pandemic. An interim report was submitted in July and after further interviews and analysis, reflecting the fast-moving policy and market environments, this is now the Final Report. We are grateful to everyone who has taken part in the research process and to our sponsors for their understanding of the complexities of the process.

2 See Smith, Whitehead and Williams (2013)

3 The specific objectives of the project were:

- (i) to gain a better understanding of what shared ownership and partial equity initiatives (which together may be called partial equity products) are currently underway across the market and what might be in the pipeline (albeit that is now less predictable);
- (ii) to clarify which parts of the market are being targeted by government and lenders and whether and how both government and lenders see the potential for further growth;
- (iii) to identify the major barriers to expansion in these markets; and
- (iv) ask how government might support growth in "affordable" homeownership.

4 Birmingham City Council had introduced its half and half scheme in the 1970s

5 A number of generally short lived private shared ownership schemes have been brought to market, eg, the BOS shared appreciation mortgages (mid-late 1990s) and the Gentoo Genie model (2011-2016) the Castle Trust Partnership mortgage (2012-2014), although others do continue (Heylo Home Reach, 2014 to date).

6 In addition, Metropolitan Thames Valley Housing Association have a Housing Plus model where shared owners opt to buy an extra 1% of their home each year at a predetermined price.

7 Except in Wales

## 1.2 The Products

It is in this environment that the government is introducing new initiatives to extend the market in partial ownership models. To date the two most important new products are (i) First Homes which works through the planning system to provide a 30 % (or more) discount to first time buyers and key workers with that discount preserved in perpetuity and (b) a new more standardised approach to shared ownership (SO) in England announced in August 2020. Most recently the Prime Minister has spoken of wanting to convert **Generation Rent** to **Generation Buy** through the wider use of longer term fixed rate mortgages, the use of government backed insurance for higher loan to value mortgages and an easing of the stress tests on affordability used by mortgage lenders<sup>8</sup>.

## 1.3 Market context

Our earlier research into partial equity products (Smith, Whitehead and Williams, 2013) was driven by an increasing market interest in developing products which would allow institutions and their customers to have a stronger stake in the residential sector while effectively measuring and pricing the risks that they faced. Earlier examples in the UK and other countries of pure market products such as shared appreciation mortgages had however proved to be both too expensive for consumers and based on inadequate data.

In the years after the GFC there appeared to be growing interest in developing new market- led products. As part of that research we reviewed a number of potential niche market products present at the time which appeared to have the potential to grow<sup>9</sup>. What is striking now is that none achieved the traction anticipated.

Since 2013 the market for equity finance into housing more generally has moved forward with a significant appetite from investors for equity exposure to the residential housing market. This has been evident in the rise of the Build to Rent and Build for Sale markets where such investors have been active as well as in increasing interest from institutions wishing to take a stake in the rental market more generally (and now more recently also extending this appetite to low cost home ownership and to social rented homes<sup>10</sup>).

In reality it continues to be the case that government has been by far the most important force determining the opportunities available to market providers. The latter's main role has been to provide traditional mortgages and bank lending within the framework of these schemes and of which the most important has been the government's provision of equity loans through Help to Buy. The government is therefore at present central to the future of the equity share market. Importantly in this context, the current policy agenda is driven primarily by concerns with easing access to home ownership rather than by any wider focus on risk reduction or any attempt to reform the underlying structure of the housing system. It therefore does relatively little to incentivise more fundamental innovation. What focus there was on risk reduction was driven by the regulatory response through the Mortgage Market review and the subsequent macro-prudential interventions of the Bank of England's Financial Policy Committee. This tightening was principally concerned with macro-economic management but it had the effect of restricting who could enter home ownership with a mortgage (see Whitehead and Williams, 2017; see also Lewis and Cumming, 2020).

Some seven years on from our last examination we have seen the government dominance in this market reinforced. Private equity backed initiatives remain small scale, with very limited market traction.

In Appendix 1 we briefly review some of the recent research literature around affordable home ownership, eg, Walker, 2016 and how best we might conceptualise the issue outside of a government policy led framework.

<sup>8</sup> In an interview in the Daily Telegraph 3rd October 2020 in advance of the Conservative Party Conference

<sup>9</sup> These included Gento's Genie home purchase plan (which was subsequently backed by the GLA), the Assettrust OwnYourHome mortgage product (which was looking to sweep a significant proportion of the remaining social rented stock into shared ownership creating 900,000 new home buyers) and the Mill Group's co-investment products

<sup>10</sup> See for instance [https://www.socialhousing.co.uk/news/68132?utm\\_source=Ocean%20Media%20Group&utm\\_medium=email&utm\\_campaign=11881493\\_SH%20weekly%2008/10/2020&dm\\_i=21XR,72NTH,ELQ8F4,SKIFY,1](https://www.socialhousing.co.uk/news/68132?utm_source=Ocean%20Media%20Group&utm_medium=email&utm_campaign=11881493_SH%20weekly%2008/10/2020&dm_i=21XR,72NTH,ELQ8F4,SKIFY,1)

## 1.4 The Numbers

Government statistics on affordable home ownership are quite limited despite work by ONS. Comparable UK level data are not readily available and exclude Help to Buy (HtB) which is separately counted because it is not formally an affordable home ownership product (except in Wales). In the financial year 2018/19 there were 19,481 SO completions and 52,444 HtB loans issued in England-again confirming the dominance of the latter product.

A further source is UK Finance, the lender trade body, which has for some years been collecting data on the mortgages advanced on specific scheme types both public and private –shared equity, shared ownership and the Right to Buy. Table 1 below gives the latest picture on numbers of loans over the last five years, while Table 2 gives the value of the lending. Such schemes fairly consistently account for around 10% of the overall market in numbers terms but for less than 10% in value terms. As will be evident equity loan schemes dominate in all years on either measure.

While shared equity loans in 2020 had an average value of around £188,000, shared ownership loans were at £110,000 - a clear and unsurprising indication of the different reach of the two schemes.

**Table 1.1: Number of Loans by Type of Affordable Home Ownership schemes, UK, 2016 to 2020**

Year/Scheme	Shared Equity*	Shared ownership*	Right to Buy	Total Schemes	All mortgage Loans
<b>2016</b>	36,563	17,126	12,826	66,515	675,877
<b>2017</b>	39,129	20,892	13,531	73,552	700,769
<b>2018</b>	43,447	24,683	11,076	79,206	702,710
<b>2019</b>	38,768	27,627	11,310	77,705	693,421
<b>2020 (half year)</b>	13,537	9,381	4,518	27,436	236,403

Source: UK Finance. Note: \* includes both public and private schemes. The data may be incomplete and are presented as single totals because of uncertainty on reporting reliability.

**Table 1.2: Value of Loans by Type of Affordable Home Ownership schemes, UK, 2016 to 2020, £M**

Year/Scheme	Shared Equity: £M	Shared Own: £M	Right to Buy: £M	Total Schemes: £M	All Mortgage Loans: £M
<b>2016</b>	6,190	1,578	954	8,722	123,431
<b>2017</b>	7,096	2,281	1,042	10,419	131,477
<b>2018</b>	8,162	2,819	899	11,880	134,900
<b>2019</b>	7,443	3,171	918	11,532	137,063
<b>2020 (half year)</b>	2,546	1,034	372	3,952	48,099

Source/Note: as above

## 2. A framework for analysis

### 2.1 Principles

In principle homeownership is a more expensive product than rented accommodation because the purchaser is buying an asset as well as acquiring somewhere to live. However, it also has attributes which may make it a more appropriate tenure for some types of household, for example, because it provides longer term security, even if households cannot readily afford the additional cost. It may also be that there are imperfections in the market which mean that the costs borne by purchasers are higher than the value of the real resource costs, for instance if the market over-estimates the risks associated with that property. So there is a case for intervention. A third issue is that there may be limitations in available financing systems (whether debt or equity) which mean that the purchaser cannot structure payments in relation to their likely pattern of lifetime earnings. In all these contexts there may be a case for the development of different instruments to enable individuals to buy, some of which overcome such market failures while others may involve subsidy to meet social objectives.

At a political level the emphasis on supporting people into home ownership relates to meeting household aspirations particularly among what might be deemed key marginal voters but it also to the costs to the public purse. In the context of aspirations, the best example has always been the Right to Buy a policy that was welcomed by council tenants even if they did not expect to benefit from it (Murie, 2015). But it is just as important that, in a housing system with as clear tenure delineation as Britain, there are benefits in introducing schemes that can help meet expectations with lower levels of subsidy – especially if this means that the households will not need additional assistance when they retire. Hence the emphasis on intermediate tenures – notably affordable home-ownership which can help relatively better-off households in both the social and private rented sectors. It is these political reasons that tend to dominate policy.

### 2.2 The instruments

The more practical literature on potential instruments and their objectives tend to categorise them into three main groups:

- those that help people overcome access barriers – including both help with meeting the deposit and reducing the size of the deposit required;
- those that reduce the on-going costs of purchase –by improving supply, changing regulations and/or by subsidy; and
- those that modify the risks involved in buying – whether they be about problems in maintaining payments or mechanisms to minimise the variation in asset value.

These three elements are interlinked - for instance if the deposit is reduced – eg by enabling higher loan to value mortgages, the risks associated with higher payments increase; equally if household income falls or costs rise then such borrowers face worsening affordability and also an increase in the risk of losing the property. Equally instruments may address more than one of these objectives.

In addition to meeting individual demands and needs, instruments may also be intended to address market issues, such as reducing market volatility or increasing housing supply, as well as supporting macro-economic stabilisation policies alongside political goals.

## 2.3 The Actors

In the literature these issues are often discussed in the contexts of (a) whether the purchaser can enter owner-occupation; (b) pay for the property over the lifetime of the asset (including its maintenance) or more usually before retirement and still be able to afford the other necessities of life; (c) manage the risks of charges and costs increases; and (d) similarly address loss of income and therefore non-payment as well as asset value changes and their impact on the household.

While the housing literature emphasises the purchaser, the role of the funder is just as important in determining what works. That funder may be anyone from just the purchaser, through family members, to other equity providers and then to the most usual funders, debt financiers as well as the government. These actors need to weigh up similar factors though the emphasis will differ.

Funders need to take account of the current and future value of the property; the security of the income stream from the borrower and the alternative uses to which their funds could be put. They also need to understand and quantify their risk appetite; their understanding of the extent of that risk and the return that they are expecting to obtain, not least in competition with others. They have a range of decisions to make relating to the attributes of the instrument they deploy; the market in which they will be operating; the purchasers they wish to attract; the assets being purchased or mortgaged; and their own funding sources. They also need to make a judgement on the stability of the legal and regulatory framework, and maintain relationships with third parties, including Government and HAs, on an ongoing basis.

Finally, government has three quite distinct roles: the first is to set the regulatory environment in which the market operates; the second to determine whether they wish to fund directly; and the third is to determine whether, and why, they might wish to subsidise or indeed tax (or give tax relief to) particular instruments in order to support owner-occupation in general, to target particular groups, and/or to modify risks for purchasers, funders or the market overall.

Given all these factors it is hardly surprising that there is a myriad of instruments which might be generated to address different objectives and environments – as is reflected in the range of instruments that have been introduced since 1980 (see the next section and Appendix 2 for a detailed chronology of the government schemes in England since 1980).

## 3. Government sponsored innovations

In order to cut through the detail there is a strong case for allocating each of the different initiatives that the government has implemented into more broadly based categories and then exemplifying the differences.

### 3.1 A typology of government schemes

We identify three main categories within which almost all of the government initiatives fall:

- i. **Part-rent, part own** where the largest category is **shared ownership**; but includes many variations as well eg **Rent to Buy**;
- ii. **Shared equity** - including a wide range of **Homebuy** products which normally involve a traditional mortgage and an equity loan – of which the most important one has been **Help to Buy**;
- iii. **Direct subsidy products** - including **Starter Homes, First Homes**; and indeed the **Right to Buy**.

Two other categories which do not fit the partial ownership model but also have important impacts on overall costs are:

**Savings schemes** – such as various forms of **ISAs**; and

**Guarantees** – notably New Buy and more general mortgage guarantees.

### i) Part Rent, Part Own

**Table 3.1: Shared ownership**

	<b>Access</b>	<b>Affordability</b>	<b>Risk</b>	<b>Subsidy</b>
<b>Consumer</b>	Reduces size of deposit needed	Below market rent on rented proportion of home  Capacity to staircase?  Liability for 100% management and maintenance/ home/ service charges	Mortgage is a high proportion of the owned value  Reduces capital gains/losses as only part-owned	The subsidy on the rental element
<b>Funder - mortgage lender</b>	Opens up a new market which is relatively low risk in terms of buyers' incomes and who are not able to raise a large deposit	Opportunity cost in terms of funds used	Complex legal arrangements  Borrower unable to pay  Possibility that arrears/defaults may be higher	No direct subsidy to funder
<b>Funder: Housing Association</b>	Meets organisational and social objectives	Part of the funding (the first tranche sale) returned quickly, allowing higher housing output levels then followed by uplift on the retained share	Market volatility; management issues regarding payments, maintenance	May impact on government grant
<b>Government</b>	Increased numbers in homeownership	Lower grant levels than social and affordable rent  Use of S106 without grant  Longer term savings on welfare costs	Mainly HA rather than Government  Support for households facing problems  May not help the groups intended especially in pressured areas	Rent element  Affordable housing grant

What is clear from the above table is that shared ownership is not a straightforward product and the reasons for involvement vary greatly between participants – whether consumers, providers or funders. Moreover, the principles of shared ownership were developed in a very different economic environment where the expectation was generally that people would initially buy around 50% and high inflation and growing incomes would make staircasing to 100% a reasonable aspiration for most employed households using that product. Indeed, the 100% repairing obligation given to the shared owner at the outset was precisely to incentivise such behaviour<sup>11</sup>. Now the situation is very different for many purchasers, with initial purchase proportions often 25%<sup>12</sup> and sometimes lower and evidence that fewer households will ultimately move to owning 100% of the property. In particular, how long the purchaser remains as a partial owner affects the risks borne by all parties because the purchaser's income and personal circumstances may change as indeed may the market. In particular variations between regions in terms of house price inflation and demand may change so the experience will differ by region.

The core issues that in part explain why the SO approach has not been scaled up to the extent that might have been envisaged (the so called Fourth Tenure) include:

- (i) The traditional mortgage can only be secured against the proportion of the property bought by the occupant under current PRA capital weighting rules, rather than the total value of the property together with a range of complex legal issues about recourse on default (some schemes have included the capacity to staircase down which has alleviated some of these problems);
- (ii) All shared ownership schemes supported by Homes England and equivalent in other parts of the UK are backed by the Mortgagee Protection Clause (MPC) in the Homes England Standard Lease -this provides lenders with recourse to the full value of the property in the event of default but with complexities as above;
- (iii) The relatively small numbers mean that some of the largest banks have been less interested in taking a major funding role (there are obvious exceptions such as Halifax and Nationwide BS);
- (iv) Increasing house prices (relative to wages) have slowed the capacity to staircase;
- (v) Increasing house prices, notably in London and the South East mean that the groups able to afford to buy using a particular scheme (notably SO) have needed higher incomes. As a result, the scheme no longer covers the same range of households as initially envisaged and may overlap with other government backed initiatives;
- (vi) There are risks to HAs arising from market volatility. These have been somewhat reduced by the increased capacity to transfer unsold properties into the private rental sector - though this impacts on cash flow. Currently there are growing numbers of unsold shared ownership properties although some RSLs (including for-profit new entrants) have expanded successfully<sup>13</sup>;
- (vii) Shared owners often find it does not deliver the “ownership” they expected and the 100% repairing obligation on the back of a small share of ownership is seen by many as unfair. Associations have been slow to address perceived weaknesses;
- (viii) In the absence of reliable and regular data reporting for this product it is perceived by some funders to have higher arrears;
- (ix) There is no active/widespread resale market for shared ownership homes. Rather sellers mainly rely on back to back sales –buying out the housing association share and selling the home on the market as a 100% owner occupied home. This limits the timescale during which the affordable home remains available, albeit the associations get an HPI adjusted receipt. The rights of the housing association to nominate a buyer within a

<sup>11</sup> See Stanley (1974)

<sup>12</sup> Table 697 from the CORE data set collected by MHCLG shows that in 2018/19 the mean equity stake purchased was 42% - see <https://www.gov.uk/government/statistical-data-sets/live-tables-on-social-housing-sales>



specified period were reduced in 2015 to assist sellers but this seems to have made little difference to the outcome.

A fundamental constraint has been the government's uncertainty about whether SO is a supply side product – helping to expand supply with a given amount of government funding; or whether it is a demand side subsidy helping lower income households to access affordable home ownership. The fact that DIYSO and related product initiatives have been short lived even though there was high demand for the products reflects the continued emphasis on new build/new supply.

Instruments such as **Rent to Buy** involve different patterns of payments but are fundamentally similar. It gives the purchaser, as tenant, a subsidy equal to the difference between the rent charged and the market rent. However, it also requires tenants to buy or part-buy the home at a fixed time in the future or to move out. What is not clear is whether the product has real benefits for a significant number of potential users given the other products available. For instance, many might choose to move directly to part ownership.

## ii) Shared Equity: Help to Buy

The most important example of shared equity, involving a traditional mortgage and an equity loan, is **Help to Buy** which has overtaken **Shared Ownership** as the second most popular affordable home ownership product (after the **Right to Buy**). Importantly the initiative was also seen as having two quite distinct objectives – to help people to buy but also to support developers to expand new supply.

The biggest benefit of the scheme has been that it is seen as market led and thus has raised relatively few problems for traditional mortgage lenders given lower loan to value ratios and lower repayment costs<sup>14</sup>. There is also far less of the bureaucratic overhang that has dominated shared ownership. Further, the generous rules with respect to the house price cap have meant that large numbers of people who could have afforded to buy anyway have been able to access the scheme. This in turn makes it a much lower risk product from the point of view of lenders. Thus an important aspect of the scheme (inherent in these attributes) is that while it has helped people lower down the income scale to access homeownership, especially in the Midlands and Northern England, it is not formally part of the affordable housing offer.

Another important attribute of the scheme has been the government's preparedness to fund all those coming forward who meet the criteria. Scale therefore was only constrained by demand and by the availability of appropriate new build housing. Earlier schemes which involved developer funding were limited by the government's short-term financial commitment and the negative impact on builder balance sheets which in turn impacted on output levels.

Not all those eligible have used the scheme even among those choosing to buy new property, but up to 40% of those who have done so have stated that they would not have been able to buy at least within a similar timescale. Two negative issues from the point of view of government have been the identified deadweight loss in the scheme from those who would have bought anyway and the excess profits which have accrued to developers.

<sup>13</sup> See *UK Housing Review Briefing Paper*, October 2020, page 6

Table 3.2: Help to Buy

	<b>Access</b>	<b>Affordability</b>	<b>Risk</b>	<b>Subsidy</b>
<b>Consumer</b>	<p>Reduces deposit requirement and makes it easier to meet mortgage regulations</p> <p>But restricted to new build</p>	<p>Lower monthly payments</p> <p>Interest is charged after 5 years</p> <p>Liability for 100% management and maintenance / improvement / service charges</p>	<p>Lower payments reduce likelihood of default</p> <p>But capital uplift is shared with government (as is any realised loss)</p>	<p>5 years zero interest on up to 20/40% of value</p>
<b>Funder – mortgage provider</b>	<p>Minimum 5% deposit but with a lower loan to value ratio there is a lower capital weighting</p> <p>Extends market to those otherwise unable to buy. The FCA also disregarded the cost of interest payment in terms of the affordability assessment</p>	<p>Seen as part of mainstream lending so little opportunity cost although it is new build</p>	<p>Similar to mainstream mortgage lending except that concentrated on new build</p> <p>No evidence of excess arrears / default</p>	<p>No subsidy to mortgage provider except lower capital weighting and payment disregard</p>
<b>Government - Equity loan</b>	<p>Increased numbers of new entrants to home-ownership – but significant deadweight loss</p>	<p>Return and therefore opportunity cost depends on house price rises</p>	<p>Risk of price reductions and potential capacity / appetite of purchasers' rights to decide when to pay off the loan</p>	<p>Technically a joint investment on which government makes a return - but opportunity cost of cash flow</p>

14 And not least when the mortgage lender's affordability stress tests are applied

### iii) Direct subsidy: Right to Buy

The UK government, unlike many other governments, has given very few direct subsidies to owner-occupiers. Assistance has been in the form of tax reliefs and on discounts which do not directly impact on government finances.

The Right to Buy (House Sales Scheme in NI) is available to all eligible council tenants and gives the tenant the right to purchase the property they are renting at a discount based on length of time as a council tenant. The scheme has been in place since 1980 across the UK but is no longer available in Scotland or Wales. The government in England is currently piloting a Right to Buy scheme for housing association tenants and has recently announced the extension of a Right to Shared Ownership which will be available to social tenants who live in the vast majority of rented homes delivered through the government funded Affordable Homes Programme 2022-26<sup>15</sup>.

Right to Buy clearly brought a whole new stratum of income groups into the owner-occupied sector and is by far the most popular affordable home ownership product to date. However, it largely had a single generational effect enabling existing better off tenants with very similar attributes to many owner-occupiers to buy. Despite adjustments to the discount fewer equivalent households in the next generation have been able to become owner-occupiers using their own resources. Until the 1990s ex Right to Buy homes provided a significant layer of more affordable homes for new entrants into ownership but large numbers of these properties have subsequently been sold to private landlords or kept as a second property which was then rented out. Quite often, these properties have ended up being lived in by those needing housing benefit or even as temporary accommodation.

**Table 3.3: Right to Buy**

	<b>Access</b>	<b>Affordability</b>	<b>Risk</b>	<b>Subsidy</b>
<b>Purchaser</b>	Must be a council tenant  Lower deposit	Lower outgoings as compared to market purchase	Location and need for repair and improvement	The individual discount
<b>Funder – traditional mortgage</b>	Extends market by bringing in both household and dwelling but to lower income and older purchasers	Part of mainstream lending although changes mix of dwellings and households	Low because of price discount but higher because of low income and quality/ location of property	No direct subsidy to funders
<b>Government</b>	Extends homeownership	No direct financial cost – but clear opportunity cost in terms of loss per unit and need to replace lost social housing.	Fewer better off tenants and more concentrated repair/ improvement  Need to provide additional social units  Increased welfare payments as properties moved into private renting.	The discounts although may not show on balance sheet.

<sup>15</sup> See <https://www.gov.uk/government/publications/right-to-shared-ownership-initial-guidance-for-registered-providers/right-to-shared-ownership-initial-guidance-for-registered-providers>.

#### iv) Direct subsidies to savings

The other direct subsidy approach has been to support savings through ISAs and other means of helping potential purchasers to build up deposits with the government putting in a bonus alongside any savings accumulated. These programmes have been at a significant scale (Help to Buy ISA was funded to the tune of £1.2bn and the Lifetime ISA at £2.6bn). The funding via the Lifetime ISA is available not only to help a first home purchase but also as retirement savings. The Help to Buy ISA has now been closed.

#### v) Guarantees

These generally reduce the risks to private finance of lending to individuals and indeed to housing associations. They are a form of insurance, which in many cases will cost the government nothing (it is a contingent liability and scores very little in public expenditure terms). However, guarantees have been relatively little used in the UK (unlike many other countries). The Mortgage Guarantee scheme announced in 2013 closed to new loans at the end of December 2016. Over 100,000 loans were supported by the guarantee. This scheme also encouraged other lenders to put in place their own schemes (deemed to be less bureaucratic and lower cost) and together this boosted the return to higher LTV Lending during this period. As noted earlier the Prime Minister has recently mooted re-opening this agenda.

## 3.2 Relative accessibility of the main scheme types

The attributes of the schemes in terms of who can access the scheme, what they are enabled to purchase and the affordability of each offer make it clear that schemes have been relatively siloed in terms of their development.

The variations in the schemes have usually addressed the affordability issues for the targeted groups together with the extent to which the government in question has wished to expand owner-occupation. Other objectives, eg, in terms of the expansion of total output have usually been relatively less important except in response to crises. Table 3.4 attempts to summarise the relative accessibility of the different scheme types.

**Table 3.4: Relative accessibility of main government schemes**

	<b>Part rent/part own</b>	<b>Partial equity</b>	<b>Right to Buy</b>	<b>Comparison</b>
<b>Household groups</b>	Those with incomes under a defined limit. Aim to help those excluded from market for high LTV mortgages because income too low	First time buyers and existing owners – price rather than income limits act as main constraint	Council tenants (plus attempts to include HA tenants) -	HtB – a lower risk alternative to high LTV with some increased access; SO/ Rent to Buy intermediate tenures, bringing lower income people into the market; concentrated among higher income tenants
<b>Available supply</b>	Almost entirely new build	New build below set price limits	The property in which the tenant is living (though there have been transferable discounts)	Current models almost all new build in mixed tenure sites

<b>Affordability</b>	Income/price of available new build. Mainly nationally specified SO rules - so variation in who can afford across regions  In higher priced areas, only relatively high income purchasers can afford	Capacity to support a 75% (55% in London) mortgage given new house prices - clearly varies very considerably across country  Proportions of lower income households able to afford limited in South and in London	Income (including help from family etc) /scale of discount; preference for the unit /resale capacity  In principle can choose one of the other options – but own income usually too limited?	Hierarchy between different types of scheme: currently Partial Equity; then Part Rent/Buy  Emphasis in government initiatives on replacing Help to Buy partially by First Homes and reducing the minimum % purchased in SO to expand accessibility
<b>Form of subsidy</b>	Submarket rent	No direct subsidy if equity share seen as an investment by government	The discount (plus earlier rent subsidy)	One objective is to move households into a tenure which will mean less future cost to the public purse

### 3.3 A summary of government sponsored schemes

Table 3.5 gives an indication of the range of schemes that have been introduced by government over the last forty years:

**Table 3.5: Chronology of Affordable Homeownership Schemes**

<b>Date</b>	<b>Part rent part own</b>	<b>Shared Equity</b>	<b>Direct Subsidy from central government</b>	<b>Other</b>
<b>Pre-1980</b>	'Half and half'			
<b>1980s</b>	Shared ownership  SO off the shelf  DIYSO  Right to SO  Index linked SO		Right to Buy  Tenant Incentive Scheme  Grants towards building SO	
<b>1990s</b>	Rural SO.	Homebuy, Wales  Homebuy, England	Voluntary Purchase Grant  Right to Acquire	

<b>2000s</b>	Social Home Buy Rent to Home Buy	New Build Home Buy Key Worker Living London Wide Initiative First-time buyers' initiative Open Market Home Buy - split between lender and government Home Buy Direct - split between developer and government	Government equity loans – not technically a subsidy Discounts for London wide initiative Grants for building under First-time buyers initiative	
<b>2010s</b>	Rent to Buy	Help to Buy	Grant for Rent to Buy homes Right to Buy equivalents removed by Scottish and Welsh governments	New Build Homebuy –guarantee Starter Homes Initiative - subsidy from developer contributions
<b>2020s</b>	Right to Shared Ownership and new model scheme	Help to Buy limited to first time buyers and regional price caps plus scheduled to end 2023 First Homes - 30% plus equity share retained in perpetuity		Proposed: 95% fixed rate mortgages guaranteed by government

What is evident from this chronology is that;

- there has been a myriad of schemes since 1980 in both part own/part buy and shared equity products and covering new build and existing homes. Often the variations especially in part rent/part buy have been minor. Do it yourself variants of both shared ownership and HomeBuy have been and gone from the market seemingly in part because they were too popular (as they allowed households to select an existing home) and so ran out of budget. They were also overtaken by new schemes emerging and new priorities, notably the increasing focus on increasing supply. Appendix 2, which provides greater detail, shows that they sometimes included additional types of purchasers; sometimes different types of dwellings; sometimes different owners; and different types/ levels of subsidy. Sometimes the schemes overlap; sometimes they replace other similar schemes; Starter Homes was a stillborn discounted purchase scheme now replaced by First Homes
- there is a strong relationship between the turnover of the schemes and the frequent change of Minister;

- because many of these variations have been short lived they also have limited impact and are confusing to consumers and lenders;
- most schemes in the first two categories – part rent/part own and shared equity – have involved new building rather than existing units;
- many of these schemes have involved direct government subsidy to ensure that the dwellings are made available;
- but Right to Buy, the largest scheme, has been very different in that it involves the transfer of existing units which had received subsidy when built along with the discounts on the current market value;
- the 1980s were dominated by Right to Buy and shared ownership and its variations – and, while there have been many changes in details, they remain important elements of government policy today;
- shared equity products come more strongly and explicitly into being only in the 21st century and have been the main instrument ever since;
- First Homes is a somewhat different form of shared equity which is a partial replacement for Help to Buy. If successful it will concentrate new affordable housing more on home-ownership but it remains to be seen whether it will be a popular option;
- on the other hand, the proposed government mortgage guarantee scheme plays to the strengths of a traditional and generally accepted instrument even though it is expected to be based on long term fixed rates;
- finally, in terms of impact, the Right to Buy is one of the longest running schemes and has had the most impact in terms of numbers using it (over 2 million in England; over 500,000 in Scotland; and 140,000 in Wales – in 40 years). Help to Buy although of much shorter duration (since 2013) is second in terms of numbers and Shared Ownership (in play since 1980) is then third.

### **Comparing Scotland**

While the schemes are generally quite similar, over the last few years we have also seen greater divergence between the schemes in England and Scotland in terms of affordable home ownership offerings.

Campbell (2019) summarised the schemes in Scotland as follows;

- Shared equity - as England's Help to Buy but with tighter limits;
- Shared Ownership – again as in England but very limited development in Scotland to date;
- HOME (Home Ownership made easy) targeted at first time buyers with a £5k deposit (or older purchasers with £40k) and linked to a repair and maintenance fund;
- Self-Build.

The Scottish government itself recently published a review of schemes in Scotland (2020). It recently announced the First Home Fund (£150m) to support 6,000 purchasers by providing equity loans of up to £25k to buy either a new build or an existing home<sup>16</sup>. There is also the longer running LIFT scheme (low cost initiative for first time buyers) which provides a 40% loan on the open market value of a home in return for 30% of the sale price. As this suggests the Scottish schemes are more nuanced and flexible albeit the basic structures are similar to those in England. In addition, Scotland benefits from UK wide savings schemes, eg Help to Buy ISAs. As importantly they have a more active intermediate rental market than in England. Northern Ireland has not been tempted

by all the different schemes outlined and has persevered with its co-ownership scheme supplemented by a rent to own scheme. Wales has utilised both SO and HtB alongside a number of smaller schemes<sup>17</sup>.

## 4. Market products

### 4.1 Market structure: incentives and constraints

The UK mortgage market is dominated by a small number of very large players who are able effectively to control the prime market and for whom there is little incentive to undertake radical market innovation. The key driver for large firms is to expand their business, reduce costs and improve profits. This can be done by marginal adjustments to their current market more easily than by taking on new markets altogether. Serving underserved market niches is some way down the priority list in those terms. In truth, most customers are reasonably well served. Most mortgage innovations apply to the GB market - Northern Ireland is often excluded.

Established lenders face considerable challenges not least in relation to information technology and the speed with which they can adapt systems and processes to deal with new products and procedures. Despite that, the Halifax and Nationwide BS in particular have a long history of supporting some innovation in the mortgage market and in particular for backing government schemes. More generally, although we have seen products such as the Springboard (Barclays) and Family Boost (Halifax plus Lend a Hand – the equivalent LBG product) mortgages emerge from these firms but they have not revolutionised the market. Commercial confidentiality prevents us knowing the volumes of business such products attract but one senses it is small. In practice their role may be more about bringing customers to that lender rather than to that product.

As any lender almost regardless of size will remind you –there are few if any rewards for being first into a market and all the internal instincts of firms work to hold back innovation at a product level – if no one else is doing it then is it a good idea? Typically, product development in this area is triggered partly by a government request/demand from senior executives and/or by a significant shift in the wider environment, eg around energy efficiency. When it comes to innovation the big lenders are probably technologically rather than financially constrained for taking innovation forward. Big lenders are hugely advantaged by their use of the internal ratings based (IRB) approach to capital weighting and big volumes of low risk lending ensures they get very favourable weightings and thus a competitive advantage.

By contrast small lenders, who are typically largely squeezed out of the prime market, face significant constraints not least through the use of the standardised approach to capital weighting. This is fixed rather than modelled as under IRB and in essence makes their pricing less competitive<sup>18</sup>. Building societies are also regulatorily squeezed through the PRA's Prudential Sourcebook which for example limits their exposure to shared ownership.

Generalising, it would seem big firms are less likely to take risks even though they have the greater capacity to do so. By contrast small firms are the opposite - they may lack the scale of resources and capacity to take on significant market innovation and risk. The market propels them to take on a higher

<sup>16</sup> These are defined as financial transactions and funded very specifically by the UK government. When the UK Government invests in such schemes in areas that are devolved to the Scottish Parliament, the Scottish Government receives a proportional share of the UK Government's investment. There are restrictions on how FTs can be used. The Scottish Government can only use FT funds to support equity or loan schemes beyond the public sector and cannot be used to support day-to-day 'resource' spending. The funds must ultimately be repaid to HM Treasury.

<sup>17</sup> See <https://www.gov.uk/government/publications/joint-service-housing-advice-office-leaflet-index/affordable-home-ownership-schemes-wales-updated-april-2020>

<sup>18</sup> See pages 37-38 for a good summary: <https://www.fca.org.uk/publication/multi-firm-reviews/strategic-review-retail-banking-business-models-final-report.pdf>



exposure to niches where risks are probably higher but because such lenders are more likely to have manual underwriting processes, at least in part, they are able to manage that risk quite effectively.

Bringing innovations to the market involves overcoming significant regulatory hurdles both via the FCA and PRA but also, where relevant, in terms of passing through the array of the lender's own internal committees, eg, risk and conduct, which are now part of the governance structures of all lenders. These processes are demanding with respect to evidencing and time and of course staffing. Decisions are played out against an ever-changing backdrop of priorities not only within the lenders themselves but in the wider economic and financial context. This situation is now further complicated by Covid-19 and a potential housing market downturn alongside an economic recession.

Having said that, in international terms the UK mortgage market is both very large and very innovative which suggests markets in other countries are both more constrained and perhaps less competitive. In terms of affordable home ownership solutions, as we discuss in section 8, there has been a significant reliance in other countries upon mortgage guarantee schemes, typically via government backed mechanisms, which have underpinned higher LTV markets and first-time buyers.

On the other hand, historically the UK has generally been characterised by having a strong higher LTV market - 90/95% and even 100% mortgages. At the peak in 2005 around 15% of loans advanced were in this category. After the GFC this market was much reduced. Over the last few years it had grown to around 5% of loans with the marginal cost of the extra borrowing between 90% LTV and 95% LTV loans falling from 34% at the end of 2017 to 20% by the end of that year<sup>19</sup>. The Covid-19 market shutdown led to an immediate contraction in the higher LTV market. There was then a brief recovery, before concerns about the longer term prospects for house prices led to some further downward market adjustment as well as some repricing upwards. The marginal pricing of higher LTV loans has again soared and their availability has reduced. Lenders are releasing blocks of funds on a time limited basis in an attempt to manage demand.

The market contraction after the GFC opened up a considerable gap which innovators and others have been trying to fill albeit within the regulatory, risk appetite and macro-prudential constraints that now exist.

## 4.2 Market schemes

Fundamentally most innovation is driven by the desire to help bridge the capacity of households to buy a home with their financial resources and the conditions prevalent in the market place – house prices, interest rates, deposit requirements and funding capacity.

Market based shared and partial equity products have generally been sold to consumers either as a means of obtaining a deposit or as a way of sharing risks. They may also enable non-owners to participate in the residential property market – or indeed existing owners to spread their portfolio/risk. So the objectives are similar to government sponsored products in that they affect access, affordability and risk and include opening up the market to new players, notably investment funders.

Inevitably there have been a mix of schemes over time. Perhaps the most obvious are:

(a) Mortgage indemnity guarantee schemes which since the 1930s insured lenders against the risks of offering higher LTV products. These utilise both commercial insurance and self-funded structures and all are paid for (indirectly) by the customer. In the 1991 downturn there were major disputes between lenders and insurers as to whether the loans advanced under the schemes met the specified insurance criteria and would thus pay out. This has much reduced lender appetite to utilise such schemes and the costs associated with them.

<sup>19</sup> See Thomas, 2019 for further details

**Table 4.1: Mortgage Indemnity Guarantee schemes**

	<b>Access</b>	<b>Affordability</b>	<b>Risk</b>
<b>Purchaser</b>	Lower deposit	Higher running costs plus cost of insurance	Default including costs of forced sale
<b>Mortgage lender</b>	Larger market	Help reduce mortgage interest rates though there is additional premium cost	Top tranche of loan covered – so risk of loss reduced
<b>Funder</b>	An additional market (mainly sold on in 1970s/80s)	Market rates for projected risks	Mis-pricing risk  Mainly transferred through portfolio transfer
<b>Government</b>	No direct role except in shared ownership	No direct role	Crisis support in face of defaults

Equity loan products have been offered by a variety of providers. They include shared appreciation<sup>20</sup> (ie, the provider benefits from house price increases but does not generally take on the risk of price reduction or sometimes shared equity mortgages (i.e, covering both upside and downside house prices). The costs of these products reflect the small scale of the market as well as issues around the data quality for risk assessment and pricing. So for example one product expected to be available in Denmark but funded from the USA puts up a 10% interest free zero repayment mortgage, so reduces outgoings but takes 25% of the ultimate sale price.

The main differences in these products arise from who funds the product and whether more than one funder is involved. Some (such as Castle Trust) were to be funded by individual investors who wanted a stake in the housing market but wished to spread their holding across a larger number of properties. These were seen as having significant potential at the time of our last report. To some extent they have been replaced by crowd funding products which may involve a single property but more generally enable the individual funder to spread their risk across a range of residential investments or even a mix of residential and other investments.

Latterly the funding is more likely to come from institutional investors who are looking for access to the residential market and aim to manage this risk by involvement in different markets as well as a range of individual properties. These products can in some cases be combined with a traditional mortgage to lower the LTV for the purchaser and to spread the risk through the top tranche of the loan. There has been a clear suggestion that there is a potential market for such products because the mainstream lenders are risk averse and indeed may not always measure risk effectively.

A particular problem in measuring risk is that schemes are relatively small scale, so risks may not be adequately diversified across the housing stock. Further house prices vary with individual attributes of the dwelling and its location so there are specific risks associated with that property. There is also potential for moral hazard – eg, in terms of maintaining the property effectively. All of these problems were identified in earlier schemes where price indices were used to measure market risk –while actual risks relating to particular dwellings turned out to be quite different. Better data is a prerequisite for avoiding these problems.

By definition the government is not directly involved although they may enter the equation if there is widespread default or job loss. Importantly because the prices are market determined the types of household who might demand such schemes are those looking for easy access but who are fundamentally financially literate. Evidence from Australia (quoted in Smith et al, 2013) in particular showed that take up of available schemes was from households who had a wide range of choices. Their success therefore depends on effective risk assessment and finding niche markets where risk may not have previously been effectively identified or measured by the market.

**Table 4.2: Shared Equity Loans**

	<b>Access</b>	<b>Affordability</b>	<b>Risk</b>
<b>Purchaser</b>	Equity loan can be zero direct cost or an interest charge	Lower outgoings	Final payment - and therefore actual cost depends on appreciation/losses of value so is unknown
<b>Traditional lender</b>	Larger market and lower outgoings	Lower payments and deposit	Lower risk as lower LTV
<b>Funder</b>	New market	Lower cost of funds because risk spread	Declines in house prices; default
<b>Government</b>	No direct role	No direct role	Lower repayments so lower support if a problem.

### 4.3 Market products: a chronology

Our detailed chronology of market and product evolution (see Appendix 2) highlights the many innovations made in the mortgage market over the period 1980 to 2020. Some of these are more about process and practice as distinct from the products themselves.

It is evident that, although on the face of it, the mortgage market today looks very much like that of 1980 or indeed 1930s in terms of the reliance upon capital and repayment mortgages, there has been significant change. In terms of market products, equity loans by lenders themselves (and developers) have never featured strongly because they tie up considerable capital for a deferred and uncertain return as well as having different risk characteristics as compared to ordinary mortgages. Table 7 summarises the main trends, with an emphasis on available products but also on how funders have supported government initiatives. It shows clearly how great the emphasis has been on higher loan to value ratios and overcoming deposit constraints– with their inherent risks and need for insurance. It also shows that the market is very open to wider macro-economic volatility as well as to regulatory change (which is often an outcome of crisis). It also suggests that risk appetite appears to be closely related to the economic cycle and that developing risk sharing market products has proved extremely difficult.

Taking a wider perspective there have been a number of relevant mortgage market developments setting aside more competition on price and terms and conditions. These include:

- Longer mortgage terms –allowing the loan to amortise more slowly and thus keep payments down and/or allowing the purchaser to borrow more
- Fixed rates - giving greater payment security over a period
- Interest only – deferring the repayment of the capital and thus allowing more to be borrowed
- ‘Part and part’ products which combine interest only and repayment mortgages
- Generational products which allow parents and others to contribute to the purchase by providing more capital and so reducing the deposit constraint, part covering interest payments, or giving a guarantee so the borrower can get a better credit score
- Supporting Shared ownership and Shared equity schemes

<sup>20</sup> See [https://en.wikipedia.org/wiki/Shared\\_appreciation\\_mortgage#:~:text=A%20shared%20appreciation%20mortgage%20is,in%20the%20property%20until%20death](https://en.wikipedia.org/wiki/Shared_appreciation_mortgage#:~:text=A%20shared%20appreciation%20mortgage%20is,in%20the%20property%20until%20death). For a detailed account of the SAMS schemes

**Table 4.3: Chronology of Market Developments**

	<b>Access/Higher loan to value</b>	<b>Affordability/ Repayment flexibility</b>	<b>Risk management</b>
Pre 1980s	Higher cost top up loans above 75%  Entry of local authorities into market	Provision of mortgages for Shared ownership	Second charge lender took the top up risk
1980s	Lender required mortgage insurance (MIG)  Endowment mortgages with declining insurance cover for the borrower	Made securing higher LTV mortgages easier but at a cost  Helped provide lower cost higher LTV mortgages and with/without profits life policies	Depends on whether the loan conformed to the policy to ensure a payout in the event of default  Helped protect the mortgage payments
1990s	Sub-prime lending	Flexible and current account mortgages  Equity release	Fixed rate mortgages
2000s	Self-certified mortgages  Closure of high LTV mortgages	Longer mortgage terms  Interest only mortgages  Flexible mortgages / drawdown capacity  Interest Rate Tracker mortgages	
2010s	80% + Higher LTV return  Limited innovation during recovery  More mortgage products using Bank of Mum and Dad support  Provision of traditional mortgages for Help to Buy  By 2019 more innovative products underway	Tighter income requirements  Growth of Equity release and Joint mortgages (and subsequently Joint borrower sole proprietor mortgages)  Provision of traditional mortgages for Help to Buy  Continued affordability pressures given low wage growth	Growing interest in shared equity products  Diversified and institutional funding  Provision of traditional mortgages for Help to Buy  Continued government calls for longer term fixed rate loans
2020	High LTV mortgages withdrawn; returned; then again withdrawn		Innovations on hold or withdrawn as market uncertainty intensifies

## 4.4 Progress so far

Some innovations have been less than successful, notably the early equity loan products – shared appreciation mortgages which, in a sense, worked for the small number of lenders involved but crucially not for the borrowers as house price inflation took off. The lending industry returned to equity lending when five lenders, including Halifax and Nationwide, joined with the government in the Open Market Homebuy product (each offering a 12.5% equity loan) but the government exited the product rather rapidly; replacing it with a suite of Homebuy products.

A number of lenders participated in the local authority mortgage scheme (LAMS) with authorities placing money on deposit with lenders to secure higher LTV loans for their locality. However, the two big successes from the point of view lenders have both been government sponsored (setting aside the Right to Buy) - Help to Buy (and its earlier variants) and Shared Ownership. Both have gained market traction (albeit very slowly in the case of the latter) and both have now delivered well over 200,000 transactions each.

Outside of these partial equity schemes (there are other very small-scale initiatives) the market response to the affordability challenge for home ownership is worthy of note. Endowment mortgages did work well for many but a lot of the low start varieties failed to generate the returns needed to clear the mortgage debt. Low start mortgages similarly promised a lot but spiralling market interest rates made them problematic.

For many the sub-prime lending in the run up to the GFC in 2007/8 allowed households who previously had difficulty entering the home ownership market to have significantly expanded opportunities to do so. However, over time the sub-prime lending evolved from a market for prime borrowers with a “blip” to what was termed heavy sub-prime - borrowers with a long term poor credit history who were ill prepared to cope with any change of circumstances. Ultimately this proved to be an expansion too far.

One element in the development of the sub-prime market was an expanded level of lending to the self-employed, in part reflecting the growth in the number of people in that sector. While such lending could clearly be justified, in the event lenders became overly reliant up self-certification of earnings and this was exploited by borrowers, some of whom fabricated their income to borrow more than they could actually afford.

Likewise, the solution of term extensions leads almost inevitably to the problem of lending into retirement (over 65 years of age). This might be justified in terms of the ever more unclear boundary as to the age of retirement. However, it has allowed some borrowers to not only claim they would work for many years post the defined retirement age despite underlying health conditions and/or the physical demands of their proposed employment. However, rather than self-certifying, lenders must now take an informed and evidence based view as to the reasonableness of any such claims, particularly for physically demanding work.

The mortgage market in the UK has clearly been maturing. By 2020, although the first time buyer market had been largely restored – in part aided by the government’s Help to Buy scheme and other assistance the second stepper market has contracted – a combination of differential house price inflation and higher transaction costs. The re-mortgaging market has expanded not least as households seek to capture longer term low rates. With the arrival of more new lenders competition has intensified and mortgage margins have been shrinking. However, it is important to note that financial markets had not fully recovered from the GFC and even before Covid-19 were probably not strong enough to support lending and competition on the scale seen pre GFC. This in turn has put more power into the hands of FCA and PRA who want a smaller safer financial services industry. This does mean that opportunities for FTBs will remain constrained and many pay a good deal more in rent than they would on a mortgage but still cannot qualify on tough affordability grounds.

The outbreak of Covid-19 in the UK in the spring of 2020 saw the housing and mortgage markets largely grind to a halt. Lenders withdrew products/stopped lending and retreated to lower LTVs while the government effectively closed the sales market. Subsequently some lender partially restored their product lines. Despite

the many measures put in place to support some lenders and the economy we are likely to see a rise in unemployment alongside soaring government debt. It is a fast moving situation with unknown consequences. However, it has perhaps pushed the mortgage market back a couple of years and closed off market innovation for at least a year. If there is a quick recovery that might save the situation but it is simply too early to say.

## 4.5 Current innovations

In addition to lender provided products, the market had been poised to see the introduction of a number of schemes which have been being developed over the last few years by other actors. These include:

- An investor funded top up loan blended into the lender's main mortgage product: Market Mortgage <https://www.marketmortgage.co.uk/>. This is now being progressed both for higher LTV lending on new build and existing homes. It should be on the market in 2021
- A Peer to Peer structure where would be buyers join together to collectively fund deposits Stepladder <https://joinstepladder.com/>
- A scheme aimed at providing long term fixed rate mortgages without a pre-payment penalty at least in the short term: Perenna <https://perenna.co.uk/>. FCA approval is pending and this might make the market in late 2021/2022
- A co-investment model bringing buyers and investors together: HopHomes <https://hophomes.co.uk/about-us/> - already on the market
- A project in which a re-insurance specialist is creating a product where the housebuilder pays into a remote fund that is at arms length from the builder and this fund in turn provides the lender with mortgage insurance on higher LTV lending on the properties built by that builder. This is now being developed in conjunction with 16 UK housebuilders with a soft launch planned in 2021
- WayHome is another joint purchase structure yet to be launched (the investment partner is Allianz Global Investors (AllianzGI), part of the Allianz Group). The minimum stake is 5% and you can buy up to 40% before you have to staircase out. <https://www.wayhome.co.uk/>
- Other schemes such as Boost, a product by a Californian mortgage company rumoured to be launching in the UK with an equity stake in the home and Property Pact (<https://www.linkedin.com/company/propertypact>) seem to have made little progress.

These all have different dimensions, purposes and market potential. Some are already on sale while others have still to get to market. It is impossible to say what they might achieve although clearly they are backed by entrepreneurs who have felt that they have a place in the market. History does not provide much re-assurance, in that every year new ideas have emerged and most of them would seem then to disappear, partly through lack of backers but also because contexts change.

It is not appropriate at this stage to offer a view on these individual schemes as most have yet to arrive on the market. Without doubt there are underserved market niches in the UK and there are constant calls from the government and others for more innovation. However, the process of bringing such ideas to market is clearly very challenging, not least in the context of a highly competitive mortgage market dominated by six very large lenders (and perhaps also constantly shifting government priorities) and a wildly fluctuating external economic environment.

Legal costs tend to be high and the approvals process, if a big lender is involved, can be very time consuming. Covid-19 has further complicated this process. Lender (and probably investor) risk and innovation appetites have fallen with the upshot that some market developments will probably be further delayed. Some of the lender reluctance

to back these schemes with conventional mortgages (where relevant) has partly been a product of operational pressures given payment holidays but it is also from concerns more about conduct risk than house price risk.

On the consumer side there is also risk aversion. Many households are understandably nervous of innovative products not least given that it is often family and friends who provide the main source of advice alongside brokers who may themselves also be unfamiliar with new products. There is a natural tendency for most households to stretch – whether it be the income or the deposit or both - to secure a conventional mortgage. Innovations which blend into the existing landscape but offer new options are probably therefore most easily absorbed.

## 4.6 Complementary innovations

There have been large scale innovations in other parts of the lending market which have relevance to how households can be assisted to become owner-occupiers – notably through the Bank of Mum and Dad and indeed so called “later life borrowing”. In addition, and whatever its merits, the equity release market has also gathered considerable momentum, as larger providers have entered that segment (Scanlon et al, 2020).

The emergence of a variety of “generational” products in the lending market is an encouraging recognition of the disparities in assets and incomes which exists between generations. In this context, one relevant innovation has been the introduction of guarantor mortgagor products, where usually a family member guarantees repayments. However, lenders are required by FCA to carry out full affordability check on the guarantor, even though it is highly unlikely they would be called on to cover the costs for the full-term. This rules out many potential guarantors. This has led to the creation of the Joint Borrower, Sole Proprietor type of mortgage where not all parties to the mortgage are legal owners of the property (and group mortgages formed to allow friends to buy homes together are also more commonplace).

The recent BSA report (Pannell and Jenkins, 2019) on the Bank of Mum and Dad (BOMAD) highlighted a number of issues relevant to helping younger households into homeownership:

- Even conservative estimates place the BOMAD alongside the largest ten mortgage lenders in the UK;
- More than a third of first-time buyers rely on the BOMAD to get on the housing ladder, normally via help with the deposit (and our survey confirms).
- However, the money mainly goes to those already better placed to get on the housing ladder. As a result, the BOMAD cannot meet the needs of all would-be first-time buyers.
- Building societies have shown the capacity to innovate to support the BOMAD with a rich tapestry of niche products designed to address the key problems faced by first-time buyers of raising the deposit and satisfying affordability criteria.

A report by LSE London (Scanlon et al, 2018) stressed that parental donors are not necessarily characterised by high incomes, but rather by their level of (mainly housing) wealth. So by implication their capacity to help depends in part on broader innovations in the market for later life borrowing. It also suggested that only two thirds of support went to first time buyers – in part because of the perceived need to ensure equity between children. Policy issues raised by interviewees included (i) that the Bank of Mum and Dad was further reinforcing wealth and housing inequality and (ii) government expected older people to prioritise paying for their own health and social care and supplementing their pensions over supporting the next generation.

A second report examined innovations in later life borrowing (Scanlon et al, 2020) notably in relation to re-mortgaging against the unencumbered equity in their home (where the mortgagor continues to pay the interest and capital into retirement and may need to re-finance at intervals); and equity release mortgages

where the borrower obtains a lump sum based on a proportion of the dwelling value and existing mortgage commitments and normally does not make repayments until they die or move into long term care.

As these reports highlight there are a range of ways in which the generational market might be improved to secure more capacity for helping first time buyers (and older households to secure the homes they need). They point to the importance of partnership between industry, government and regulators in developing a joined up agenda on easing/improving the affordable home ownership market.

## 5. Learning from customers, UK stakeholders and international experts

### 5.1 Findings from customers: the BSA Property Tracker Survey

The BSA runs a regular *Property Tracker Survey* undertaken by YouGov. The survey in February 2020 was constructed to include a number of questions specific to those looking to buy and their knowledge of different affordable homeownership products.

#### The survey

The survey has a wide remit and around half of respondents are existing owners who are not looking to move. The proportions of those who are looking to move are quite small. From a base of over 2000 adults around 6% are existing owners looking to move; a similar proportion are aiming to buy for the first time; some 2% have owned in the past but not at the present time and are looking to own; and the much higher proportion of around 28% do not expect to buy in the immediate future. While this means some of the absolute numbers in a given category are small they are enough to give a reasonable indication of behaviour.

The general survey showed that even before the coronavirus people were unsure about whether it was a good time to buy – with only 22% saying it was a good time to buy; and 40% expecting prices to remain constant or fall with a further 30% saying they didn't know. Sixty per cent of respondents said they thought finding a deposit might stop people buying; while just over 40% saw both accessing and paying a mortgage as major problems.

#### Demographics

The demographics of the sample are also relevant. In terms of incomes around 60% of existing owners looking to move; potential first time buyer; and those looking to buy again (from now on called Existing Owners, FTBs and returnees from other sectors) all had incomes of less than £50,000 pa. Only 5% of those not looking to buy in the near future had incomes over £50,000. The position with respect to social grade shows 50% of existing owners in grades 1 and 2 but only 25% among FTBs; 20% among returnees; and 13% among those not looking to buy soon.

#### When do people expect to buy?

In the survey undertaken in early 2020, 50% of FTBs expected to buy within three years as did the small number of returnees. But one third did not expect to buy within five years and 11% thought they would not actually be able to do buy at all. Among those not looking to buy soon, 13% thought they might do so within 5 years and a third after 5 years. But 30% said they were unable to purchase.



## Main challenges

Forty percent of first time buyers and returnees both saw getting the deposit together as the most important challenge. Only a third of those not likely to buy soon saw a deposit as the most important challenge. Interestingly both FTBs and Returnees saw having an income that would allow them to obtain a mortgage as more important than having the income to pay the regular payments (FTBs 30% versus 17%; returnees 22% versus 16%). Around a quarter of those not looking to buy indicated that income to pay the mortgage was the most important challenge while a similar proportion saw that as being actually securing the mortgage. Overall there was a clear distinction drawn between whether the respondent thought they could pay and whether they met the mortgage providers' requirements.

## Help from Family

Table 5.1 shows the importance of assistance. Importantly well over 50% of those expecting to buy either as a FTB or a returnee expected no help. One- off loans or gifts dominated the types of assistance - a third of FTBs expected one or the other (or in some cases probably both) although the proportion was less at under a quarter for returnees. There was relatively little emphasis on helping with the mortgage itself. Those not expecting to buy soon stressed the possibility of a gift – although whether these would be forthcoming or were simply seen as a necessity is unclear.

**Table 5.1: Whether people expected assistance from family etc (%)**

	<b>FTB</b>	<b>Returnee</b>	<b>Not buying</b>
<b>Loan</b>	19	10	14
<b>Gift</b>	16	13	25
<b>Help with mortgage</b>	6	5	6
<b>Joint/guarantor</b>	8	1	9
<b>Unlikely to receive any assistance</b>	56	59	49

(excludes don't know and other; includes some getting more than one type of assistance)

## Awareness and use of affordable home ownership schemes

The four questions on awareness and use of the schemes were specifically included to assist this project. They were asked of existing owners expecting to move as well as FTBs, returnees and those not expecting to buy in the near future.

## Shared ownership

Awareness of Shared Ownership was very high among existing owners and returnees but a surprisingly large proportion (30%) of FTBs were not aware of the scheme, a figure comparable to those not expecting to buy soon (Table 5.2). Actual usage of the scheme was very low. However, 15% of FTBs (and 9% of returnees – a tiny number) thought they probably would apply. In the main however those who were aware did not expect to apply.

**Table 5.2: Shared Ownership awareness (%)**

	<b>Existing owners</b>	<b>FTB</b>	<b>Returnee</b>	<b>Not buying</b>
	%	%	%	%
<b>Not aware</b>	12	30	8	32
<b>Aware: already applied</b>	4	2	4	0
<b>Aware: likely to apply</b>	1	15	9	6
<b>Aware not likely to apply</b>	82	54	79	62

### Help to Buy

While overall the figures for Help to Buy were not dissimilar the real difference was among first time buyers where over 50% had either applied or might apply (Table 5.3). Given that Help to Buy is only available on new homes this seems to be a very significant number both of applicants (22%) and probable application (31%). Overall both awareness and possible use was higher for Help to Buy than for Shared Ownership – in part because of high levels of publicity since 2013 but also because it may be seen as a simpler way of addressing deposit and affordability problems.

**Table 5.3: Help to Buy awareness (%)**

	<b>Existing owners</b>	<b>FTB</b>	<b>Returnee</b>	<b>Not buying</b>
	%	%	%	%
<b>Not aware</b>	13	17	15	26
<b>Aware: Used/ have applied</b>	8	22	6	8
<b>Aware: probably will apply</b>	3	31	19	14
<b>Aware not likely to apply</b>	75	29	60	52

### Rent to Buy

Awareness of Rent to Buy products was far lower across the board - with the least awareness among potential FTBs who could be expected to be the main users (Table 5.4). But not only is awareness limited but even among those who stated they knew about the product, take up and potential take-up was very low – except among returnees where the overall numbers are too small to draw any conclusions.

**Table 5.4: Rent to Buy awareness (%)**

	<b>Existing owners</b>	<b>FTB</b>	<b>Returnee</b>	<b>Not buying</b>
	%	%	%	%
<b>Not aware</b>	29	50	32	41
<b>Aware: Used/ have applied</b>	2	3	2	

<b>Aware: probably will apply</b>	4	8	15	6
<b>Aware not likely to apply</b>	65	38	51	52

Finally, they were asked about Right to Buy which has been available since 1980 but only to council tenants. Table 5.5 shows that awareness was particularly low among FTBs and those not expecting to buy soon. But in the main the figures are not really interpretable as we do not know whether respondents are council tenants.

**Table 5.5: Right to Buy awareness (%)**

	<b>Existing owners</b>	<b>FTB</b>	<b>Returnee</b>	<b>Not buying</b>
	%	%	%	%
<b>Not aware</b>	21	41	17	35
<b>Aware: Used/ have applied</b>	4	2	4	0
<b>Aware: probably will apply</b>	3	14	13	6
<b>Aware not likely to apply</b>	73	43	66	58

### **Conclusions: Customers**

The survey gives a snapshot of people's understanding shortly before they became fully aware of the Covid-19 outbreak. The survey clarified the challenges people have been facing in putting together a deposit as well as the importance of lending criteria in addition to having enough income simply to pay for repayments.

It also showed that help from family was important but such assistance mainly concentrated on the deposit with relatively few helping with monthly payments.

Respondents were relatively more aware of Help to Buy than other schemes - although the difference was not great, given the emphasis on this scheme in the media. Equally, usage (or potential usage) was higher. Awareness of shared ownership was high among existing owners and the small number of returnees, but surprisingly low among FTBs who could be expected to be the target group.

Overall, it is clear that Help to Buy has had a significant impact on first time buyers but hardly any on existing owners looking to buy. Shared ownership remains an important part of the menu of affordable homeownership but FTBs appear to be less aware – almost certainly because of the emphasis lately put on Help to Buy.

## 5.2 Findings from UK stakeholders

As part of the research we undertook a number of telephone interviews with the key stakeholders involved in providing, regulating and developing policy on affordable housing products. Although most had been completed by mid-March a small number were harder to arrange as a consequence of the Covid-19 lockdown and these were not complete until September.

## The BSA Roundtable

The starting point was a Roundtable held with BSA members held (face to face) in early February 2020. Participants mainly saw shared ownership as a natural bridge towards full ownership although it has also become increasingly clear that many purchasers would not be able to staircase fully and this raises issues around the depth of the second hand market.

A number of factors made it difficult for many building societies to increase their exposure to Shared Ownership – notably regulatory constraints on the proportion of their lending that could be for this product. In part this is because the PRA does not recognise the Mortgagee Protection clause (MPC) in the Homes England etc standard lease for shared ownership. This clause gives lenders recourse to the full value of the property in the event of default. The PRA takes the view that the lender's loan is only against the share being bought rather than the full value of the home and thus classifies it as a high LTV loan. This then impacts upon the capital weighting of such loans.

One reason for seeing the product as higher risk is a lack of high quality data about arrears – although there was considerable evidence that on average the quality of the loans was similar to (or even better than) traditional first time buyer mortgage lending.

A second issue for Building Societies is around the importance of brokers in the process of choosing products and mortgages. Brokers have their own views as to what was “normal” and many have lacked understanding of shared ownership. This sometimes means that they do not provide wider advice. As a result, some people who might have been clients for shared ownership instead stretch their budgets to take on a higher LTV traditional mortgage.

There was general agreement that, given the market environment, the SO market is well-served by lenders. However, the model has been too complicated and difficult to scale up. Whether the government's new model for shared ownership will solve this remains unknown at this stage<sup>21</sup>. Until it can be scaled up, costs remain relatively high for all parties. The new model now proposed addresses some of the costs issues alongside allowing for payments for additional 1% stakes although there are a range of issues to still overcome<sup>22</sup>.

The government is now pledged to ensure that shared owners can access the mortgages they need at competitive rates – remembering that purchasers are required to purchase a proportion in line with what they can afford. In this context we noted there have been continuing problems of communication and understanding between lenders and housing associations. This has been eased by successive rounds of joint guidance but it has not gone away completely. Much turns on having specialists on both sides who focus on and understand this market.

It was also felt in the Roundtable that there have been some attempts at innovation – notably linking lender saving schemes to purchase - and that this had potential but so far had not really made much impact. Inevitably it takes time for savings to build up and the government schemes are more readily accessible. In terms of innovation more widely there were also concerns about what new affordable home ownership models - such as First Homes - might be put forward which in turn could impact on the SO market. While it was accepted SO was far from perfect, it was at least tried and tested and there was an established market.

Participants suggested that from a lender perspective there had been some effective new entrants, partly with the support of Homes England. Heylo's shared ownership model was viewed as a success by some – using a range of funding methods and a clear management framework.

## UK stakeholder interviews: a range of perspectives

Views from housing associations suggested that the government's proposals around enabling staircasing in 1% increments and buying as little as 10% initially were seen as workable, if administrative costs could be kept down (see above and footnote 11). However, it was accepted that in a volatile market small shares might not be attractive to either purchasers or landlords. There was also considerable concern that the proposed First Homes initiative would

reduce the volume of SO properties coming forward via S106 and so could displace rather than supplement SO. SO was still seen as a complex, raising difficult issues around the resale market and how purchasers could move on<sup>23</sup>.

The more general issue of the objectives of housing associations involved in SO was raised in a number of interviews. Business plans in this area often seemed to be dominated by sales and marketing departments, who saw it as a source of cash and potential cross subsidy without taking much account of longer term issues. There had been a number of attempts by associations to create innovative products. Thames Valley's *Shared Ownership Plus* has gained some traction but Gentoo's *Genie* failed. A current initiative is Home Group's *Deposit Builder* which aims to help existing tenants to save for a deposit (<https://www.homegroup.org.uk/media/3ffpnjqs/getting-on-the-property-ladder-guide.pdf>). Currently the NHF is running an Incubate innovation group as part of its Futures programme and has launched a new national campaign to boost the public's understanding of shared ownership (see <https://www.housing.org.uk/news-and-blogs/news/national-housing-federation-launches-shared-ownership-campaign>). The G15 group of large London housing associations has been exploring reforming the current model stressing the benefits of the Metropolitan Thames Valley initiative. They have now settled on a range of improvements which will be subject to wider discussion<sup>24</sup>.

Some of the more *market oriented interviewees* have stressed that there is mileage in products that more effectively linked savings to purchase. However, others thought there were the risks of customers not using the proceeds in the planned way, and of course given the timescales how the economy or government might change – long term savings contracts bear some risks. On somewhat safer ground were the joint borrow/sole proprietor models (which get around some of the problems associated with the guarantor model). However, some saw these as tax avoidance measures and posing a range of challenges. There was considerable interest in a variety of top-up schemes where institutional funders could be brought in to take the higher risk elements either in the form of debt or partial equity. Given the current mortgage conduct regime it was clear a lot of work had to be done on establishing the potential demand from customers with surveys and focus groups as part of that process. There was a general view that 100% loans carried a bad reputation – rightly or wrongly – and the confusion over Northern Rock's Together product (a 95% loan and a 30%/maximum £30,000 unsecured loan) had added to that impression.

Discussions with *government officials* engaged on home ownership issues were inevitably constrained, given that at the time of the interviews, unannounced policy developments were in train (see footnote 19 below). Their starting point was that the core objective was always to ensure that any scheme was seen as generating additionality in terms of boosting home ownership and/or new output. In this context Help to Buy was seen as reasonably effective. It was agreed that the "reduced fat" version, which addresses some of the concerns around additionality, to be introduced in 2021 would see volumes significantly diminish (not least because of the regional price caps which will have variable impacts). There was also awareness and understanding of the different ways in which the schemes (HTB; SO and First Homes) had played or might play out in the market place.

There was continuing support for expanding the role of long term fixed rate mortgages as a way of reducing risks and therefore costs. It was part of the 2019 Conservative Party manifesto and it remains a live ambition reinforced by the conclusions of the recent CPS report on Resentful Renters (2019) and the Prime Minister's announcements at the recent Conservative Party Conference.

There was recognition that First Homes (FH), at least as initially presented, had the potential for eroding the provision of both social housing and SO via the planning system and those concerns have been repeated by critics on the back of the recent government announcements on the role of FH in developer contributions. Mortgage lenders were however indicating a willingness to support FH even though the rules are not yet finalised. Particular concerns have focussed on the discount in perpetuity and the practicalities of that structure. Housebuilders

21 See [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/915718/Shared\\_ownership\\_consultation\\_response.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/915718/Shared_ownership_consultation_response.pdf)

22 These include whether HA's funders will agree to 1% staircasing with valuation determined by a house price model and questions around who is absorbing the conveyancing costs. In addition the 10-year repair coverage will certainly make shared ownership development less attractive for HAs

were also said to be supportive, not least because it is a national scheme and lenders are at least in principle backing it. The presumption was that “details” would be resolved as the scheme is worked up for a full launch.

In the context of shared ownership, it was clear that the model lease was still seen as an important pre-requisite to ensuring lender and borrower protection - albeit some lenders would accept limited variations. The recent release of the Law Commission’s proposals on leasehold reform<sup>25</sup> was seen as a further factor in this equation. Officials recognised that the way shared ownership was currently delivered (via housing associations) imposed limitations on its impact in the market. There were also concerns about the time taken to buy and sell shared ownership property reflecting the various parties involved. The government’s newly announced proposals for reforming shared ownership begin to address some of these issues.

More generally, there was some questions about whether SO is the ideal product for supporting affordable homeownership at scale. The current debate on the efficacy of leasehold arrangements (including ground rent and service charges) raises a number of questions about the structure of SO which do need to be addressed. It is clear this is recognised by associations and work is underway to explore the solutions, but it remains a difficult issue for both providers and government.

### **Conclusions: UK Stakeholder**

The interviews highlighted tensions around existing products and proposals and the relatively limited number of innovations that had come forward. There was a general awareness that much higher interest rates could pose a significant threat to some borrowers.

There was general acceptance that there was a need both to change and improve the existing offers to lower and middle income households looking to access owner- occupation and to strengthen the commitment from the current government to support more growth in that tenure.

Since most of the interviews took place a number of initiatives have been announced that reflect these concerns – although in most cases the details are still lacking.

## 5.3 International experts

Our examination of international experience of affordable homeownership and particularly of the funding used included three elements:

- evidence from the literature including, in particular surveys, by the European Mortgage Federation (EMF), AHURI and Gibb et al (2013);
- a survey generously carried out through the EMF Research and Data Committee; and
- more detailed case studies from Australia, Canada and the Netherlands.

Here we bring the main findings together.

23 The detail of the scheme is set out in [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/907215/200805\\_Changes\\_to\\_the\\_current\\_planning\\_system\\_FINAL\\_version.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/907215/200805_Changes_to_the_current_planning_system_FINAL_version.pdf). The recent London Assembly Housing committee letter (March 2020) sets out a list of sought for improvements -<https://www.london.gov.uk/about-us/london-assembly/london-assembly-publications/affordable-home-ownership-london>

24 Subsequent to these discussions in September 2020 the government in England issued its response to its consultation on shared ownership setting out a new national model (see [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/915718/Shared\\_ownership\\_consultation\\_response.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/915718/Shared_ownership_consultation_response.pdf)). This has significant implications for the shared ownership market. We discuss these later in the report

## European examples

The EMF report on funding affordable housing in Europe (Hypostat, 2019) makes it clear that social rented housing remains the main form of affordable housing in European countries that make significant affordable provision.

Three countries where there is more emphasis on affordable home ownership are France, Germany and Spain. In France the majority of assistance is in the form of subsidised loans. Two newer schemes include reduced VAT for 'intermediate' new build housing and a leasehold arrangement for low income households which reduced the cost of housing by separating land and housing through a new social land owner (the Organisme de Foncier Solidaire) which retains ownership of the land. The details are unclear. In Germany there are first time buyer grants for lower income families as well as interest subsidised loans and regional body support for new affordable homes. In Spain the main emphasis is on providing affordable land for housing which is sold at a submarket price for specified household groups.

There were nine replies from the survey through the EMF Research and Data Committee some of which covered similar ground (Whitehead and Williams, 2020). The evidence presented reflects three main approaches to government supporting the growth of homeownership demand:

- Grants where the objective is to increase new building – sometimes only for rent, sometimes for all tenures but increasingly for owner-occupation. These types of grant are most prevalent in ex transition countries;
- Increasing numbers of grants to reduce the costs of owner-occupation – either through direct payments or a reduction in mortgage costs. Examples included: Croatia: mortgage subsidy for younger households; Hungary: grants for families; France: zero and low interest rate loans; Germany: grants for low income families; Netherlands: starter loans in addition to basic mortgage for first-time buyers from municipalities repaid when income high enough; Spain: favourable mortgage loans and direct grants.
- Government guarantees which reduce the mortgage interest rate charged. Examples include: Latvia: government guarantee; Finland: savings/guarantee for first time buyers; Netherlands: multiple levels of guarantees.

Within Europe there are only a small number of examples of shared ownership/partial ownership products. Outside the UK perhaps the three most important are:

- The Netherlands: where there has been quite a long history of shared ownership products developed and managed through housing associations. The latest, and most sophisticated, example is Koopen naar Wens. This involves enabling a delayed payment to the housing association up to 50% (although usually 25%) which must be repaid through an equity share. There appear to be two main reasons why they have been part of the affordable housing offer in the Netherlands – the importance of housing associations, many of which have strong balance sheets and the wish to grow and a legal system which enables suitable contracts between the association and the purchaser.
- Ireland: where a new shared ownership scheme was introduced in 2018 by which eligible households may ask the local authority to buy a home on which the household will pay a discounted price (up to 40%) with the relevant proportion taken as an equity share by the local authority. They are then encouraged to buy the local authority's share and must do so within twenty-five years. Earlier schemes were more similar to UK examples.
- Slovenia: where there is a demonstration project in one city where the municipality takes an equity share. So far the numbers are tiny but there is an intention to expand the scheme more generally.

<sup>25</sup> See <https://s3-eu-west-2.amazonaws.com/lawcom-prod-storage-11jsxou24uy7q/uploads/2020/07/ENF-Report-final-N8-1.pdf>

## Wider ranging international examples

Reports on innovative financing for affordable housing at an international level (eg, Gibb et al, 2013) concentrate heavily on state supported schemes with very little emphasis on market led innovation. Gibb et al highlight policies that help first time buyers with deposits, or variations on FirstBuy or NewBuy type models, such that the indemnity allows for a slightly higher (or more conservative) deposit percentage than the 5 per cent currently in practice. They also note the role of tax reliefs and other fiscal incentives.

There was considerable interest in shared equity models in Australia in the early 2000s (Whitehead and Yates, 2007) aimed mainly at increasing government interest in supporting affordable housing. However, there was also considerable interest around market products (in part because of the support from the Prime Minister and his son who developed one of the early products). A review in 2008 was optimistic (Pinnegar et al, 2008). One conclusion was that 'Australia can be considered a market leader in shared equity product development and investment mechanisms that assume no direct subsidy' (page 3). However, the findings also stressed how little lenders were convinced of its potential. Research in 2018 suggests little progress has subsequently been made (Evans, 2019).

Canada has had somewhat similar experience to that in Australia. As in Australia the legal and policy framework has been relatively supportive; equally Canadian examples differ province by province. Where experience differs is in the extent of US in addition to UK influence. Policy emphasis has been strongest in Ontario and British Columbia – but growth has been hindered by the disparate range of products and relatively little governmental financial support. The result has been, up to last year, that the impact of both government-sponsored and market developments had been very limited. However in 2019 they introduced a 5 year federal equity loan programme backed by a \$100m fund<sup>26</sup>.

There are, however, three types of instrument where other countries have far more experience than the UK:

- Individual mortgage guarantees (found in particular in the Netherlands, USA and Canada and often recommended in Australia). The UK has been reluctant to go down this path for individuals although they have been used to a limited extent for housing association funding. – as in the Netherlands.
- Community land trusts or their equivalent which separate out land and housing costs – but inherently involve a form of leasehold. France is the latest country to introduce these but they are important in a number of countries, notably the USA and Canada, where they are seen as useful local initiatives. Again the UK has a relatively small but growing number of CLTs and their role in provision is expanding.
- Co-operatives which make up significant elements of the housing system in some countries, notably in Scandinavia but are also in Germany. Prior to enabling leasehold enfranchisement in the 1980s, these were seen as a potentially important solution in the UK– but the reform meant that most of those involved in co-operative bought themselves out.

In the market place, as in the UK, there have been relatively few initiatives and most have died quite quickly. Examples are mainly limited to the USA, Australia and Denmark. Early products such as shared appreciation mortgages had fundamental flaws. Funding has mainly been through retail products, although there is said to be a growing interest from institutional investors who want to have a role in affordable housing of all types not least because of both cash flows and long term capital appreciation. In part this is about familiarity and confidence in the market backed by adequate historical data on how the market has performed. Fund managers are rightly conservative but given the weakening appetite for and performance of other funds, eg, commercial real estate and a growing understanding of the different residential markets there is clearly some appetite to explore this market more fully and a number of funds have begun to make limited equity investments in social and affordable housing.

The few examples of wider housing market products that have actually been launched suggest that they are expensive and often do not protect against possibility of capital losses. The Danish example (an interest-free and zero repayment loan until sold on, when the company gets 25% of the value in



the Danish case) has not yet been launched – and is unlikely to be so in current circumstances.

### **International experience: conclusions**

The issue of how best to support affordable home ownership is high on the list of priorities in many countries – ideally with market involvement. However, this review suggests that internationally there are few schemes that offer notable advantages over what is available in the UK and indeed that the UK is often a leader in this domain. In part this reflects our particular emphasis on owner-occupation since the liberalisation of the mortgage market from the 1970s; in part it reflects a legal system flexible enough to support the initiatives. The legal systems in many other countries do not readily enable partial ownership solutions.

In most European countries there is a growing range of government sponsored products both to help support the construction of affordable homes and to enable households to buy through grants, submarket loans and guarantees.

Overall, the evidence shows that availability of more complex products such as shared ownership and shared equity depends on governments' preparedness to develop the legal and regulatory framework as well as (often) to share some of the risks and provide direct support.

Where government support is involved, the products are often made available in partnership with municipalities or housing associations.

These products are mainly restricted to Western European countries with mature mortgage markets prepared to provide the basic traditional mortgage product.

Interest in developing wholly market products is mainly restricted to Anglo-Saxon based countries. Even in these countries these have not taken off in any country, except to a limited extent in the USA.

Covid-19 will probably bring market initiatives to a halt at least in the short term. Lenders and investors are coming back down risk curve and retreating from innovation. But it is possibly different for governments trying to support their construction industries.

## **6. Reflections and conclusions**

### 6.1 Reflections on the future

Exploring innovations in affordable home ownership at this time is challenging, surrounded as we are by considerable uncertainties in terms of government, borrower and market capacity and appetite. Having said that we also know that the current crisis will only amplify the problems we set out to address.

There is a tendency to assume that there are new product solutions (whether public, private or in combination) to the problem of creating long term and sustainable affordable home ownership. However, as this report highlights and previous reports have discussed, there are probably no immediate "silver bullets" bullets to be found. Government schemes are constantly being tailored/re-tailored to fit particular groups of customers with

<sup>26</sup> See <https://www.cmhc-schl.gc.ca/en/nhs/first-time-home-buyer-incentive#:~:text=The%20First%2DTime%20Home%20Buyer%20Incentive%20is%20a%20shared%2Dequity,of%20a%20newly%20constructed%20home&text=5%25%20for%20a%20first%2Dtime%20buyer's%20purchase%20of%20a%20new,or%20resale%20mobile%2Fmanufactured%20home>

often an unknown real demand alongside politically driven priorities. In the long distant past we had the Rent to Mortgage scheme in England – pulled after only 300 cases were processed. Recently the extension to the pilot *Voluntary Right to Buy* scheme (launched in August 2018) was stopped after only 1,526 sales went through.

At the beginning of this report we set out our basis for the evaluation of schemes around four key pillars namely access, affordability, risk and subsidy. Of these four heading the allocation of risk is perhaps the least discussed in the existing literature. Government sponsored schemes address all four to a varying degree but usually with an emphasis on access and partnership between government and private lenders. Market products on the other hand are mainly around overcoming barriers to accessing traditional mortgages and managing risk through enabling its diversification not least through a wider range of investors.

There is also a much more important role for the market in providing the mortgages that support the government sponsored schemes – and it is here that much of the growth has occurred aided by mortgage lenders. There is a natural tendency to assume that innovation around affordable home ownership will be largely based on government led market-based schemes or, possibly, fully government-based schemes. Getting market led developments off the ground has always proved to be a challenge and not least in securing “first mover lenders” who might back the scheme. There is a natural reluctance to do that. However, it has been done as we can see from the Buy to Let market and the student accommodation market.

Help to Buy is a good example of a government scheme that has helped prove the concept of equity investment in owner occupied homes. As the government moves to step back from this so we do see some small signs that the market is poised to move forward with a number of key innovations. There are at least two market based innovations that would seem to have real potential and much turns on them now getting out into the market place despite the challenging environment. Both are directed at managing the risk of higher LTV lending where it would be very good to see the market delivering its own solutions rather than remain reliant upon government.

## 6.2 Barriers to expansion: the market’s appetite and capacity

The UK mortgage market is amongst the most innovative in the world –partly reflecting intense competition itself a product of a fairly open banking system. A recent FCA report on the UK mortgage market concluded that in broad terms it was functioning well , albeit there were concerns about data, information and the tools available to ensure all customers had the right mortgage at the right price in place (see <https://www.fca.org.uk/publication/market-studies/ms16-2-3-final-report.pdf>).

At the same time the market is highly oligopolistic and has been so for decades. The FCA noted in its interim report in 2016 “The six largest lenders account for around three-quarters of the outstanding balances... larger high street lenders tend to focus on the mainstream market, with challenger and specialist lenders competing for those consumers with less common circumstances. Building societies cover a range of segments, from mainstream national, through regional, to some specialist markets”. Despite this the market was judged to be competitive.

The introduction of bank ring-fencing<sup>27</sup>, which took effect on 1 January 2019 resulted in a significant amount of extra liquidity in core banks that needed to be deployed in conventional activities such as mortgage lending. This together with 23 new lenders entering the market in the last five years has increased competition as well as to some degree risk appetite, although this has probably declined again.

Even so, there have been few incentives to innovate. Process changes have been much more significant but these are more about cost control and competition (not least in terms of access for brokers) than bringing new products to market.

As noted earlier the larger lenders who have the greatest financial capacity to innovate are probably least likely to do so – partly because of historic legacy IT; while smaller

lenders have the greatest incentive to innovate but the least capacity.

Where we have seen innovation it has tended to be government led – itself a poor innovator as is evident in the multiplicity of schemes launched and abandoned over the years. Although we have seen lenders and others introduce some equity type structures it has needed the involvement of government to accelerate the normalisation and acceptance of equity loans. However, it is important to caution that we have not seen how these loans might perform over the cycle nor how borrowers and investors might view them as circumstances change – notably if house prices fall.

Building Societies who are the main supporters of the shared ownership market face their own challenges, especially given the PRA's restrictive stance as set out in the Sourcebook<sup>28</sup>. Societies are expected to set a maximum proportion of their lending book (depending upon "approach" under 10 or 15%) for shared ownership loans, to ensure that they retain a balanced portfolio.

### 6.3 How government and lenders might find ways forward?

Perhaps rather oddly the UK government has been keener to look elsewhere in the world for innovation rather than consider the merits of policy/product transfer ideas within the UK. There are inevitably some political tensions around this but there are clear merits for looking at "home grown" solutions not least because of shared legal and tax frameworks. The evidence from all three devolved administrations is that they have been able to create more tailored solutions, reflecting an objective of greater targeting, their smaller market size and in broad terms somewhat less volatile markets. Scotland has, for example, introduced an equity loan scheme for existing homes as well as for new build, while Northern Ireland has stuck with its well established and well known co-ownership housing organisation and its co-own and rent to own schemes.

There is certainly room to improve existing products. As has now been accepted shared ownership is in need of significant re-working, better to balance the interests of the different parties. It is certainly not the case that all is needed is better promotion and information as Cowan et al (2018) make very clear in their detailed analysis of this tenure. It remains disappointing that a product which has clear value and has been on the market since 1980 has secured so relatively little traction in its 40-year life. Cromarty (2020) estimates SO has supplied around 200,000 homes to the market up to and including 2018/19.

The UK government's new model for shared ownership has, in our view, considerable merit not least as it starts to put more emphasis on improving the product from a customer perspective. Clearly there are concerns about how allowing the purchase of lower shares will change the risk profile of the product and the would be owners and thus lender appetite to support it. Similarly, allowing the buying of small additional incremental shares may tempt owners to increase their borrowing and put additional strain on household incomes. In addition, putting a 10 year repairing obligation on the housing associations shifts a burden of cost from the shared owner this could impact on associations capacity and appetite to expand shared ownership (and despite the new homes guarantee that should be in place).

However, although the government's recent announcements of reforms are on balance helpful, there is clearly more to do and the recent Housing Ombudsman Service report (2020) highlights some of the continuing tensions around repairs, service charges, estate management and complaints handling (a survey based on 2000 leaseholders over the last two years). The lack of transparency in many areas and the failure by some organisations to treat their customers as shared owners rather than tenants are continuing problems. Too many associations still see SO simply as a cash "cow" to underwrite their mainstream rental businesses.

The planned Help to Buy re-targeting and then closure seems now firmly on the agenda despite many attempts by housebuilders and others to get it put on hold<sup>29</sup>. However, the NAO progress report published in 2019 highlighted a number of the present failings which have continuing relevance. In particular, it noted that around 4% of the

interest then due had not been paid and this will have worsened considerably. It is clear from our own work on the scheme that some home owners still did not seem to realise they would pay interest or indeed repay the loan.

One important innovation which might further ease access is around getting recognition for rent payments in credit histories. There has been useful progress through the Experian Rental Exchange project but it is not clear that these data are being used widely by lenders. It only began in late 2018 so perhaps has yet to build the necessary evidence base to assist loan decisions. It is certainly a step in the right direction, not least as we think about how we ease the transition between renting and owning and the current tightening of affordability assessments. The current Rent to Buy schemes remain of limited value given it is supplying under 100 homes a year.

Two areas where we do see significant mileage are in the various mortgage guarantee type schemes and in product structures that blend equity and debt from different funders so that risk is “tranching up” and priced accordingly.

Guarantee schemes are widely used elsewhere in the world and the cost to government can be very low while the stimulus effect on market providers availing themselves of them to support higher LTV products can be very high. Most of the schemes are government backed, eg, Canada Mortgage and Housing Corporation (see <https://www.cmhc-schl.gc.ca/en/buying/mortgage-loan-insurance-for-consumers/what-is-mortgage-loan-insurance>). However as noted earlier there is a wall of lender antipathy to be overcome here in the UK and government has a role in moving that forward.

Similarly blended products which combine equity and debt but which then appear as single product and rate seem to make sense by making best use of the differing risk appetites that exist in the funding market. The recent sharp re-pricing of higher LTV loans is indicative of the arguments for a new approach.

The proposals aired by the Prime Minister in the 2020 Conservative Party Conference about the use of mortgage guarantees and the development of a much bigger long term fixed rate mortgage market are indicative of the direction of travel of government thinking. However as was evident from the market reaction there were challenges to the idea of government underwriting higher LTV loans and the scale of the market for long term fixed rate interest mortgages, given the current low interest rate environment. It is very evident that the government must work carefully to build the case and secure a degree of market support.

With incomes stretched and rising unemployment borrowers will refocus on paying off debt and this in turn offers an opportunity to strengthen the links between savings and loans –the historic nexus of mortgage lending. Given current tensions in finance markets lenders recognise the merits of stable savings books. At the same time with rate compression and intense competition around mortgages the margins for manoeuvre are limited. Government could assist as it has already via the ISA schemes and this is a well tried route in a range of countries. The biggest challenge is targeting and reducing deadweight losses.

Reworking shared ownership could help it realise its market potential. In our view to date this debate has been dominated by provider interests although the government’s new proposals do rather break that mould. There is a long history of prevarication on shared ownership (as well as a refusal to generate the necessary database on performance which of itself would be market transformative). In that respect the government’s move to put reform on the agenda is to be welcomed.

First Homes, the latest UK government initiative, while it has the benefit of apparent simplicity, raises two specific issues: because the 30% subsidy will be paid for by developer contributions it will probably substitute for low rent social housing; and second, this discount is to be in perpetuity,

<sup>27</sup> Structural reform, also known as ring-fencing, came into force on 1 January 2019. It requires the largest banking groups to separate core retail banking services from activities such as investment and international banking

<sup>28</sup> See <https://www.bankofengland.co.uk/-/media/boe/files/prudential-regulation/supervisory-statement/2017/ss2015-update.pdf?la=en&hash=12EB469400B3EBAD64650D7FB6D400CB55D3EFF8>

raising a number of complex issues around finance and resale, yet to be overcome<sup>30</sup>.

Based on previous experience it can be expected that building societies and other lenders will re-enter the more traditional market of higher LTV products -not least aided by any promised government guarantee emerging. This will reduce the demand for First Homes and thus its impact on new build rates.

Finally, there is a degree of necessity building in the market. While the value of loans has gone up, reflecting HPI, the number of new mortgage loans has been falling. Increasingly the market is built around existing owners. It would seem inevitable that the industry must give further thought to how to re-grow the market.

At present the signs are quite encouraging if launches take place as planned. However, in reality and despite the short term optimism, it is possible we will see a major market adjustment with house prices falling significantly, as a consequence of lower incomes and higher unemployment (and possibly at some point higher interest rates). Whether, based on previous experience (eg, 1991 and 2008), the government will act to "defend" house prices, is unknown at this stage, although our assumption is that this would be likely.

## 6.4 Conclusions

The core - but hardly surprising - finding, is that there is no immediately simple way of transforming the affordability picture for first-time buyers or lower income home owners more generally. What is perhaps more surprising is how little progress has been made on the market front since our last report in 2013 albeit there are perhaps a number of "green shoots".

With respect to government sponsored schemes the most obvious message from our chronology is that many of the initiatives have been in response to short term political and/or economic pressures and have been ill-defined and poorly targeted.

### **Affordable homeownership or extending the mainstream market**

The starting point for a more strategic approach is that affordable home ownership is not affordable to a significant section of the population who would like to and would benefit from ownership. For the individual, the reason for this is mainly because of inadequate income and/or savings; but it can also be an outcome of market or indeed regulatory imperfections which mean the costs are higher than necessary. The problems around low incomes can only be addressed by increasing those incomes or reducing the price of suitable housing through government subsidy (house price falls associated with income falls do not help affordability).

### **Access and affordability**

Government sponsored schemes generally target access and affordability issues by directing the products at those below an income limit and then modifying required deposits and repayments. Logically however there are two distinct problems: those who cannot find a deposit and those who cannot afford the regular repayments. Many who live in the private rented sector only face the first constraint; others can get help with the deposit but cannot afford regular repayments. It is important therefore to assess schemes on at least three counts: savings/deposits; repayment capacity and constraints to limit deadweight losses to the government.

Help to Buy was different in that it was not branded as an affordable housing product but more as a means of helping a wider range of households either become owner-occupiers or to move to more suitable accommodation. A major objective was to support the housebuilding industry by increasing demand. An important reason for its success

<sup>29</sup> The government in England has made one adjustment in the planned timetable to allow for the delays in processing purchases because of Covid-19. The recent statements by the Prime Minister have however rather muddied the water by implying there will be further consideration of the future of HtB in 2023

was that it was a market led product – but with part of the equity funded by government. The resultant lower deposits and outgoings have made it a more broadly based affordable product, successful in its immediate objectives although with significant deadweight loss. That loss has been measured unlike those schemes that are income limited.

The latest initiative from the Prime Minister is similarly not an affordable housing product. Its ambition is to help a further two million households to become home owners as part of his *Generation Buy* strategy. The commitment to expand home ownership is to be built on the back of an expanded long term fixed rate interest mortgage market, the use of government guarantees and a reworking of the affordability stress tests imposed on lenders. However, how that contributes to the 2 million target is unclear and there was no mention of the impact of the new shared ownership model. The absence of detail inhibits the market and the players in that market.

One question is whether government sponsored programmes crowd out market initiatives. The evidence presented here and our understanding from talking to many different experts is that this is generally not much of an issue. What is more likely is that government sponsored initiatives help to shape market behaviour because of the opportunities they provide for traditional mortgage activity. It is no coincidence that we have a number of market led innovations emerging on the back of the planned closure of the Help to Buy scheme. This might suggest government sponsored initiatives have helped invigorate the market and this in turn has provided an incentive for innovation to support mortgage activity which would otherwise be lost when the relevant government scheme closes.

In many ways a more important issue is whether the different government sponsored schemes are effectively targeted at the groups for which they are intended and do not replicate one another – with resultant loss of scale. The BSA survey suggests that this is an important issue which is rarely addressed when further innovations are brought forward. The issue is made more complex by the very different market conditions across countries and regions – so national programmes rarely help on an equally effectively basis across the country. The clearest examples of these are Help to Buy which helps middle England while shared ownership works relatively better in London and the South East because it is more affordable than Help to Buy.

All of this suggests that if government sponsored projects are to provide for the full range of potential users there should be regular evaluations of schemes' objectives, targeting and outcomes. The question of the relative deadweight loss from particular schemes should also be addressed.

## **Risk management**

Government schemes put most of their emphasis on access to homeownership – with a general assumption that affordability will follow. Risk is seen as very much a lesser issue – even though, as the current crisis has made particularly clear, there can be very real risks to all parties, including the Government.

There are at least three main forms of risk that are relevant: individual risks, arising from personal and organisational circumstances; market risks which arise particularly from macro-economic change but also from competitive behaviour and particularly from lack of data and the capacity effectively to assess these risks; and regulatory risk that arises from both the form of regulation and from regulatory change which impact on the potential to enter and expand in the market as well as costs and pricing.

The situation is very different with respect to market products where the emphasis is both on providing products which will be attractive to consumers and addressing issues of risk whether to house price changes or to the personal circumstances of borrowers. Outside of supporting government sponsored schemes by providing traditional mortgages, the major opportunities that market players have worked to fill have been about more effective risk management, notably by enabling consumers to manage their own debt and asset portfolios more effectively and by bringing in investors that have an appetite for diversification and/or a greater risk appetite. Most of the examples of market innovations have been in this space – but even those that have been initially successful have tended to fail

<sup>30</sup> Not least as to how lenders will track the existence of the perpetual discount when valuing the home/lending

either because of macro-economic change or because data have not been adequate to ensure effective estimation of risk – particularly in the context of moral hazard. One important implication is that market schemes are often aimed at the upper end of the market with the aim of managing risk for financially sophisticated individuals and for lenders.

In this context it is important to note that partial equity products have always been seen – including by the Bank of England- as a potentially effective mechanism for reducing the risks faced by households whose major asset is a single property. In Help to Buy this risk sharing is with the government; earlier products included private risk taking by developers and in one case lenders. However, developing a market at scale which can address access, affordability and risk management has so far been difficult.

### **Incentives to Lenders and Funders**

Our analysis makes it clear that there are potential incentives for traditional lenders to develop new markets as while lending has been increasing the numbers of borrowers has actually declined.

From a lenders point of view, the ideal would be that demand should increase for the range of traditional products - which depends significantly on getting more activity in the existing housing market as well as among first time buyers.

Developing new products is a different matter. The oligopolistic nature of the market makes it difficult for others to initiate change, while the incentives facing the big six are mainly in the context of cost reduction.

It is also the case that the regulatory infrastructure has proved rather conservative as well as costly for lenders. This is in part because the volatility of the market experienced over many decades generates risk aversion. It is also because data are often inadequate to generate market innovations at scale. The hope has been that institutional investors will take on that role – but in current circumstances this appears increasingly unlikely.

International experience reinforces the view that it is extremely difficult for market innovation both to survive the strains arising from both macroeconomic volatility and the regulatory costs of entry. It maybe therefore that, as is also the case in most other comparable countries, government must take the lead. If so it is all the more important that government addresses the weaknesses in the current offering and works to develop a set of products which can both be readily understood by potential purchasers and funders and meet their objectives of achieving cost effective expansion of homeownership.

### **Ways forward?**

An urgent government priority should be to set out in some detail its vision for a long term sustainable rate of home ownership in general and affordable home ownership in particular including the scale of its ambition. Gordon Brown once set out an aspiration to get home ownership to 80% and officials did their best to cover the tracks, fearful of the practical implications of such an ambition<sup>31</sup>. Instead, the growth in owner-occupation to over 70% in England around the turn of the century and supported by government incentives has since been reversed to below the EU median level.

A target is not enough. Rather, government could do better to set out the principles by which it would proceed and the potential interventions it might make. This would then give the market much clearer signals and help to harness the potential for partnership between state and market. Part of the challenge must be to think longer term (and wider) and not just focus on access to home ownership but take account of longer term sustainability and consequences for both the housing market and the economy.

We need a clearer view of the scale of the affordable home ownership “gap” – taking account of house prices; incomes; the capacity to raise a deposit and risk attitudes. This is obviously a dynamic number

31 Boris Johnson has now expressed an ambition to ensure a further two million home owners

moving with circumstances in the economy and for households. The most recent attempt to enumerate at least part of this category was by Bramley (2018 and 2020) although it should be stressed that the focus of these reports was on the need to accommodate low income households. Unsurprisingly the bulk of the requirement is therefore to be met by new social rented housing supply.

The two major constraints households face in the home ownership market are lack of a deposit and too low an income (which may also be linked to job insecurity and credit history). This is then layered onto the uneven geography of housing markets across England delivering the varied levels of home ownership and access to home ownership that we can observe in reality.

A clearer understanding of this landscape is therefore an important starting point. Alongside this is full recognition of the regulatory constraints that the market operates under and in particular how these bear down on affordable home ownership. This means that there are limits as to how far the market can expand affordable home ownership and help to fill the gap without further intervention.

This then puts the onus largely on government to help balance out the risks being borne by people, providers and lenders which in turn could help manage down the regulatory constraints and facilitate market provision.

We would identify four priorities;

First, a long overdue reform of shared ownership and one that goes well beyond the existing proposals. It would need to consider the relative costs and benefits enjoyed by providers and purchasers; tackle the tensions around current leasehold structures, the need for proper market reporting and data; and clarify/simplify the regulatory framework and the role of Homes England.

Second, assisting with deposits and/or securing higher LTV borrowing are both important in the mainstream market. It is not immediately clear whether lifetime ISAs are playing the role they are intended for in terms of assisting FTBs. Further evidence on this (and on the role of SDLT relief) would be helpful before further thought is given to the case for more deposit assistance. There are some encouraging signs that market based initiatives will come forward to help re-open the higher LTV market.

Third, and linked to that is the question of mortgage guarantees. These are a cost-efficient way of expanding affordable home ownership opportunities. Here the UK could learn from abroad. However widespread lender suspicion about and resistance to such solutions would have to be overcome. A government backed scheme might cut through that and as in other countries once it has been built there is the potential for partnership or sale.

Fourth, government should set out its vision for home ownership in general and affordable home ownership in particular in some detail, looking at current provision, the risks and the potential scale of demand, funding and supply. At present we have only a limited sense of the government's ambition. Instead, there needs to be a longer term and more detailed vision and one which looks across generations and addresses both home ownership in general and affordable home ownership in particular. While we all understand why governments avoid firm commitments – the proverbial rod for their own back – the fact is that the purpose here is to provide a framework which helps stimulate the market to help meet the government's objectives.





# References

- Alakeson, V, Fearn, H and Cory, G (2013) One foot on the ladder: How shared ownership can bring owning a home into reach, Resolution Foundation, London
- Baxter, D and Murphy, L (2017) Priced Out? Affordable Housing In England, IPPR, London
- Booth, P and Crook, A (1986) Low Cost Home Ownership, Gower, Aldershot
- Bramley, G (2018) Housing supply requirements across Great Britain: for low-income households and homeless people, NHF and Crisis, London
- Bramley, G (2020) People in Housing Need: A comprehensive analysis of the scale and shape of housing need in England today, London, NHF
- Clarke, A, Heywood, A and Williams, P (2016) Shared ownership: Ugly sister or Cinderella? The role of mortgage lenders in growing the shared ownership market, CML, London
- Cowan, D, Carr, H and Wallace, A (2018) Ownership, Narrative, Things, Palgrave Macmillan, London
- Cromarty, H (2020) Shared ownership (England): the fourth tenure? House of Commons Briefing Paper, No. 08828, 24 February 2020
- Edwards, G (2019) Resentful Renters: How Britain's housing market went wrong, and what we can do to fix it, London, Centre for Policy Studies <https://www.cps.org.uk/files/reports/original/191222122235-ResentfulRentersFINAL.pdf>
- Evans, S (2019) 2018 Churchill Fellowship to investigate how Shared Equity can become a mainstream solution to housing affordability in Australia, [https://www.churchilltrust.com.au/media/fellows/Evans\\_S\\_2018\\_Shared\\_equity\\_-\\_a\\_mainstream\\_solution\\_to\\_housing\\_affordability\\_in\\_Aus.pdf](https://www.churchilltrust.com.au/media/fellows/Evans_S_2018_Shared_equity_-_a_mainstream_solution_to_housing_affordability_in_Aus.pdf)
- Gibb, K and Marsh, A (2019) Housing and Systems Thinking, CaCHE Working Paper, [https://housingevidence.ac.uk/wp-content/uploads/2019/07/Housing-and-Systems-briefing-paper\\_final\\_170704.pdf](https://housingevidence.ac.uk/wp-content/uploads/2019/07/Housing-and-Systems-briefing-paper_final_170704.pdf)
- Gibb, K, MacLennan, D and Stephens, M (2013) Innovative financing of affordable housing, <https://www.jrf.org.uk/report/innovative-financing-affordable-housing>
- Hypostat (2019) Latest Developments in European Housing & Mortgage Markets, EMF Brussels
- Housing Ombudsman Service (2020) A new lease of life Spotlight on leasehold, shared ownership and new builds: complexity and complaint handling, London, Housing Ombudsman Service <https://www.housing-ombudsman.org.uk/wp-content/uploads/2020/09/Housing-Ombudsman-Spotlight-report-on-leasehold-.pdf>
- Law Commission (2020) Leasehold home ownership: buying your freehold or extending your lease, Law Com No 392, HC 584, London, Law Commission
- Lewis, J and Cumming, C (2020) First-time buyers: how do they finance their purchases and what's changed, Bank Underground, London, Bank of England
- Miles, D (2004) The UK Mortgage Market: Taking a longer term view, Final Report and Recommendations, London, HMSO
- Ministry of Housing, Communities and Local Government (2019) Call for Proposals for Private Shared Ownership, [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/751981/call\\_for\\_proposals\\_for\\_Private\\_Shared\\_Ownership.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/751981/call_for_proposals_for_Private_Shared_Ownership.pdf)
- Ministry of Housing, Communities and Local Government (2020) various documents
- Changes to the current planning system Consultation on changes to planning policy and regulations, August
  - Making home ownership affordable; Summary of responses and the Government response to the discussion paper proposing a new model for Shared Ownership, September

- Guidance: Right to Shared Ownership; Initial Guidance for Registered Providers, 8 September
- Monk, S and Whitehead, C, eds (2010) *Making housing more affordable: the role of intermediate tenures*, Wiley-Blackwell, Chichester
- Morton, A (2018) *From Rent to Own: How to restore home ownership by turning private tenants into owners*, Centre for Policy Studies, London
- Murie, A (2015) *The Right to Buy: History and Prospect* <http://www.historyandpolicy.org/policy-papers/papers/the-right-to-buy-history-and-prospect>
- NAO (2019) *Help to Buy: Equity Loan scheme – progress review*, HC 2216 Session 2017–2019, 13 June 2019, London, National Audit Office
- Pannell, B and Jenkins, D (2018) *Intergenerational mortgages: Building on the Bank of Mum and Dad*, BSA, London
- Pinnegar, S, Milligan, V, Quinta, D, Randolph W, Williams P and Yates, J (2008) *Innovative financing for home ownership: the potential for shared equity initiatives in Australia*, AHURI Positioning Paper No. 106. Melbourne, AHURI
- Provan, J A, Belotti, A, Lane, L and Power, A (2017) *Low Cost Home Ownership Schemes*, Social Mobility Commission, London
- Saunders, P (2016) *Restoring a Nation of Home Owners: What went wrong with home ownership in Britain, and how to start putting it right*, Civitas, London
- Scanlon, K et al (2018) *The Bank of Mum and Dad: How it really works* <https://familybuildingsociety.co.uk/Knowledge-hub/bank-of-mum-and-dad-research.aspx>
- Scanlon, K et al (2020) *Later Life borrowing in a world that is living longer*, LSE report for the Family Building Society <http://www.lse.ac.uk/geography-and-environment/research/lse-london/documents/Reports/Family-Building-Society-Final-report-for-WEB-2020.pdf>
- Scottish Government (2020) *Evaluation of Government Shared Equity Schemes*, Social Research Report, Edinburgh, Scottish Government
- Stanley, J. (1974) *Shared Purchase: A New Route to Home-Ownership*, London: Conservative Political Centre.
- Walker, C (2016) *Government Housing Schemes: Accident or Design?* CML, Research, CML, London
- Wallace, A (2019) *Exploring Shared Ownership Markets outside London and the South East*, CAST Foundation
- Whitehead, C and Williams, P (2017) *Changes in The Regulation And Control Of Mortgage Markets And Access To Owner-Occupation Among Younger Households*, OECD Social, Employment and Migration Working Papers No. 196, Brussels, OECD
- Whitehead, C and Williams, P (2020) *Financing Affordable Home Ownership in Europe*, Hypostat 2020, Brussels, European Mortgage Federation
- Whitehead, C. and Yates, J (2007) *Increasing Affordability Problems - A Role for Shared Equity Products? Experience in Australia and the UK*, *Housing Finance International*, 21(5), pp. 16–20.

# Appendix 1: Government schemes and Market products: chronologies since 1980

## (a) Government Scheme Chronology:

**Pre 1980:** From 1975, Birmingham City Council “Half and Half” Scheme combining rent/ownership with council subsidy. The Greater London Council and other local authorities introduced similar initiatives<sup>32</sup>. The Housing Corporation piloted the Leasehold Schemes for the Elderly (LSE)

**1980:** Shared ownership (SO), often termed conventional shared ownership (CSO) as more variants came into being, was introduced under the Housing Act 1980. It also brought in Improvement for Sale (IFS) through which associations bought existing homes, improved them and then offered for outright sale. The Right to Buy is introduced.

**1982/83:** Shared Ownership off the shelf scheme (SOOTS) came into being buying up unsold new homes.

**1983:** Do it yourself shared ownership (DIYSO) – buyers selected existing open market homes with the association buying it and then creating a shared ownership home for those people. It was very successful (too successful!) and by 83/84 it was switched into the LA HAG fund (and then given the LAs were focussed on rental housing, DIYSO made little progress). In 1992 the Housing-Corporation-funded DIYSO was reintroduced but this time principally to enable social housing tenants to move into owner-occupation. In April 1999 HomeBuy replaced DIYSO (as well as the Tenant’s Incentive Scheme).

**1984:** Right to Shared Ownership (RTSO) for public sector tenants under the 84 Housing and Building Control Act. It was same as SO with the RTB discount applied according to the amount of equity purchased. By 1990 it was agreed it had not been a success after only 400 applicants over the period.

**1984/85:** Index Linked Shared Ownership was introduced supported by Nationwide BS with 90% index linked loans

**1988:** Tenants Incentive scheme (TIS) introduced with cash grant to help tenants buy homes in the private sector

**1990:** Rural Shared Ownership repurchase scheme introduced to help retain the SO stock in rural areas (even when sold outright).

**1995:** Homebuy introduced in Wales through Tai Cymru, the Welsh equivalent of the Housing Corporation with a fixed 30% equity loan from the social landlord but was also open to anyone in housing need. The equity loan was subsequently increased to 50% for a specified set of circumstances.

**1996:** Voluntary Purchase Grant scheme was put in place to assist tenants to buy their home. It was discretionary. In 1997 a Right to Acquire was added with certain exemptions

**1999:** Homebuy introduced in England (alongside a rationalisation of existing schemes including effectively abolishing DIYSO and TIS – LA funded DIYSO was subsequently retained). Homebuy was an interest free equity loan from their social landlord (even if only on waiting list) for up to 25% of the value of the property bought on the open market

**2003:** Starter Home Initiative with key workers being assisted using a variety of methods - such as

<sup>32</sup> Boris Johnson has now expressed an ambition to ensure a further two million home owners

equity loans and shared ownership. A £10k equity loan was offered to around 2,000 applicants

**2003:** Low Cost Home Ownership Task Force report

**2003:** New Build Homebuy pilot came into being. This scheme ran for X? years. A 30% equity loan was provided by government alongside a 70% mortgage. No deposit was required and incomes had to be below £60k with key workers in London and the South East eligible

**2004:** Key Worker Living was announced by the Deputy Prime Minister on 23 March 2004 and superseded the Starter Home Initiative. It helped key workers in London, the South East and East of England to buy a home, upgrade a family home or rent a home at an affordable price. 'Equity loans' of up to £50,000 were offered to help key workers buy a home on the open market or a new property built by a registered social landlord. Higher-value equity loans of up to £100,000 for a small group of school teachers with the potential to become leaders of London's education system in the future

**2005:** The London-Wide Initiative (LWI) provided discounted for sale affordable housing units across the Capital. LWI was a deferred equity model in which English Partnerships retained the unsold equity of the homes. Each site included a mix of open-market sale as well as low-cost ownership and rental homes with the aim of delivering up to 4,000 homes in total, of which 1,500 homes would be LWI units for key workers and first time buyers.

**2006:** The First Time Buyer's Initiative (FTBI), a shared equity product providing first time buyers a "stepping stone" into home ownership was introduced. The initiative was part of ODPM's (now MHCLG) New Build HomeBuy low cost home ownership initiative and was positioned to target key workers and other eligible groups that have sufficient income to sustain homeownership but are currently prevented from entering the housing market by the prevailing supply/demand conditions. FTBI was planned to deliver in the region of 15,000 housing starts supported by a budget of up to £850 million by 2010. FTBI homes were delivered through portfolio leverage on public sector land in EP ownership; development on other surplus public sector land not in EP ownership in partnership with public agency partners; and re-profiling existing private sector schemes. First Time Buyers Initiative was based on a 50% equity loan from the government paid directly to the developer.

**2006:** Open Market Homebuy with an equity loan provided by government and the lender (12.5% each).

**2008:** Social HomeBuy – a tenant buys a minimum 25% share of their home at a discounted price and pays a rent on the remainder. Social HomeBuy allowed eligible tenants of Registered Providers who participated in the scheme and who occupy eligible properties to purchase their social or affordable rented housing at discount either outright or on shared ownership terms (i.e. part buy/part rent).

Own Home HomeBuy/My Choice HomeBuy replaces Open Market HomeBuy with 8 housing. associations

**2009:** HomeBuy Direct an equity loan of 25% split between the Homes and Communities Agency (HCA) and the developer on a new build home.

**2012:** New Buy a 95% mortgage backed by a government indemnity on a new build home.

**2013:** Help to Buy introduced as previously detailed.

**2014:** Rent to Buy introduced aimed at helping young home buyers lacking a deposit. Social landlords were funded to build 10,000 new homes - mostly one or two bedroom flats. The government provided £400 million between January 2015 and 31 March 2017 (£200 million for London, a further £200 million for the rest of England). Under the scheme, first time buyers were able to rent at 80% of the market value for at least seven years and get first refusal on buying it. By paying 20% less in rent, the expectation was that the occupant would build up a deposit to buy the property (or another one after the seven years).

**2015:** Starter Home Initiative began giving a minimum 20 per cent discount of the purchase price of a new-build home to first-time buyers aged under 40. By 2019 no homes had been built.

The Help to Buy ISA was also launched with FTBs saving through this scheme getting a government bonus of 25% of the amount saved to a maximum of £3000 for £12000 savings and to be used on homes up to £250,000 outside of London and £450,000 in London. The scheme closed to new entrants in November 2019.

**2016:** The Lifetime ISA was announced in 2016 to start from 2017 under which any adult under 40 can save up to £4000 each year and receive a 25% government bonus. They can contribute up to the age of 50. Funds can be used to buy a first home after 12 months in the scheme. Property up to £450,000 was allowed. People with HTB ISAs could switch into the new product.

**2019:** Announcement that from 2021 Help to Buy would be restricted to first time buyers and with regional price caps. On the basis of current usage this could reduce usage by up to 50%. Based on current announcements the scheme is to be ended in 2023.

**2020:** First Homes scheme announced with details of a pilot scheme of 1,500 units within the 2021 – 2026 Affordable Homes programme. Twenty-five per cent of affordable homes are to be First Homes in the Planning White Paper.

Prime Minister announces the intention to introduce a government guarantee on 95% LTV long term fixed interest rate mortgages available to first time buyers.

### **(b) Market Products Chronology:**

The structuring of mortgages and the pace of innovation is crucially tied to both the macro-economic context – notably trends in inflation and interest rates and the linked scale of financial market and not least IT development as well as the intensity of competition. Alongside them is the format and scale of regulation and trade practices. Over time regulation has become more intrusive and influential. Most recently the market and innovation have retreated in the light of the Covid-19 outbreak and the consequent scaling back of housing market transactions.

**Pre 1980:** most mortgages were conventional annuity loans –capital and interest repayment over a 25-year term. Borrowers needing more than 75% LTV had to resort to top-up loans. This was a market dominated by building societies who set mortgage and savings rates via a cartel approach. There was little incentive for innovation.

**Early 1980s:** reflecting the cut back in local authority mortgage provision post the IMF intervention lenders had begun to move into higher LTV lending (80% plus). Over time the % rose to 95% (or higher). For many years the top tranches of the loan required either mortgage insurance (paid for by borrower) or came at a considerable premium thus ensuring high LTV also meant high cost or top up loans from second charge providers. Mortgage insurance guarantees (MIG) products were widespread for lenders. Low start and deferred interest mortgages became more common as a way of overcoming the high cost barrier. Index linked loans (debt uplifted by RPI on an annual basis) also made an appearance but proved to be less popular. Shared ownership was introduced in 1980 though never adopted really on a market wide basis, model SO lease was always problematic and most lenders regarded it as higher risk. In 2020 around 30 lenders now support this market.

However, all of this pales into insignificance compared to the development of competition in the mortgage market. In 1980 the “corset” by which banks were controlled was abolished thus allowing them to compete with building societies. By early 1981 they had taken 40% share of the market with a focus on larger loans and speed of decision. Although the bank share subsequently declined, the societies then abandoned their cartel rate setting as the government reformed the framework around them. By 1985 a more truly competitive mortgage

market had emerged. This resulted in more innovation, an increase in risk and a reduction in profits

**Mid 1980s:** Endowment mortgages were beginning to dominate the market. Of course these were tax efficient interest only structures – both low start and full versions with the former aiming to mature and pay off the loan/the latter produced a much more significant bonus. Endowment mortgages dominated between 1984 and 1996 and then fell away (tax relief on the endowment policy disappeared in 1984) and MITR was run down in the 1990s and stopped completely in 2000.

**Mid/Late 1980s:** Driven on by financial deregulation and increased competition by 1985 we saw the emergence of the new ‘centralised’ lenders such as National Home Loans (now Paragon) and The Mortgage Corporation with no branches, broker distribution, centralised administration and a reliance wholesale market funding and securitisation. The Mortgage Funding Corporation was set up in 1985 and the first mortgage securitisation took place in 1987. The UK was the first in Europe to establish significant funding programmes.

**1986:** The Building Societies Act permitted demutualisation with wide ranging consequences as the process gathered momentum post the Abbey National transfer in 1989.

**1991:** Recession and housing market downturn. There were high levels of unemployment and debt and interest rates moved ever higher interest rates –reaching 15%. This put a focus not only on forbearance and mortgage rescue but also on the emergence of stronger re-mortgaging market and an expanded role for brokers. The growth of centralised lenders was paused until the mid-90s and even then they struggled to compete with the high street (capital and funding cost advantage), this led to centralised lenders concentrating on specialist segments: adverse credit; BTL; high LTV – some of which played a role in the next crisis.

**1990s:** Traditionally mortgages had been funded by building societies on variable rates reflecting their reliance on savings rates. However, with financial services deregulation from early 1980s onwards banks and other firms (the centralised lenders) took an ever greater share of the market and with their wider access to funds were able to introduce fixed rate mortgages. The popularity of such mortgages has ebbed and flowed with the interest rate cycle. They dominated in the mid and then the late 90s. Fixed Rates required the use of derivatives to hedge the fixed/floating exposure. Building Societies lacked the ability/sophistication to implement these and centralised lenders were the first to structure. Flexible and current account mortgages first emerged in the late 1980s and by the mid-90s were offered by a wide spectrum of lenders.

**Mid 1990s:** with more competition and easy access to cheap funding some of the new entrants began to explore options at the margins of what became known as the prime market –this began to open up a “sub-prime” market or what we might today call a non-prime market.

**1996:** Buy to Let mortgages were ‘invented’ with the first lenders being Paragon and Mortgage Trust. Almost all loans were through brokers.

**2000s:** As house prices rose on a sustained basis so there was pressure to push loan terms out to 30 years make loans more affordable. Similarly, interest only loans became a firmly entrenched and popular part of the market –easing affordability constraints in the short term although putting considerable reliance on continued HPI to allow profitable sale to clear the outstanding principle. Flexible mortgages became more common in the 2000s with overpayment/underpayment and draw down facilities – features that to some extent have now been extended across all mortgage products. However, they were never more than 30% of the market.

The FSA came into being in 2001 (replaced in 2013 by the FCA and the PRA). The sub-prime market expanded considerably during the early 2000s as mainstream lenders began to compete in it and new lenders entered the market (before its rapid demise in the GFC). Tracker mortgages also made an appearance and have been a continuing feature of the market. We also saw the development of system assisted/automatic underwriting systems from early-mid 2000s although some firms notably RBS had been doing its underwriting

on that basis from the early 1990s. The growth of self-employment in the reshaping economy generated a demand for self-certificated mortgages – reliant upon the borrower evidencing their own income.

**2004:** The FSA introduces new Mortgage Conduct of Business (MCOB) rules.

**2005:** Mortgage Market Review (MMR) begins.

**2007/08:** The Global Financial Crisis (GFC) leads to the collapse of all mortgage markets but especially the interest only (IO), sub –prime and high LTV markets –move back to lower LTC on a traditional basis and where supported by central banks. The BoE response in 2008/09 was to lower interest rates, which have remained in place ever since, and in turn have driven up house prices (increasing borrowing capacity plus moves into Buy to Let property assets as other investment opportunities shrank). This in turn has intensified affordability pressures.

**2009:** Mortgage Market Review (MMR) published.

**2012/15:** Re-opening of higher LTV – 80% plus. Very few IO – often requiring 50% deposit. Sub- prime now known as non-prime or credit impaired re-enters the market reflecting the contraction of the prime market and the creation of what might be seen as a large unserved population of would-be borrowers.

**2014:** FCA introduces new MMR rules. Clear tension between the new rules and consumer ambition and demand.

**2014:** The FPC introduces two housing levers: 1. Lenders must check that borrowers are able to meet mortgage payments if mortgage rates moved three per cent higher on the SVR in the first five years (the “affordability test”) 2. A soft cap that limits high-income multiple loans (those at or above 4.5) to no more than 15 per cent of new loans (the “flow limit”). These impose new challenges for lenders. The mortgage market contraction continues in terms of numbers of loans. Lenders search for new niches/markets.

**2017:** Although home income plans were launched in the late 1960s it was only in the 1990s that mortgaged equity release schemes became more commonplace. By 2007 the market had grown to around £1bn but it was when major brands got involved that the market really began to secure traction. By 2017 it was running at £3bn per annum. Although now much bigger and more diverse in terms of products the market is still tiny in proportion to the number of older population. With the return of interest only loans for older people and the emergence of lifetime mortgages as a category we can expect further growth.

**2019:** Saw the return of IO on a wider basis and with lower deposits albeit it was still a small part of the market. Loan terms began reaching out to 40 years. Given widespread problem of younger persons entering the market, the BOMAD markets has built strongly aided by a number of “generational” type mortgages. Emergence of new structures such as joint borrower, sole proprietor to assist making these tax efficient. Also the creation of split mortgages – combinations of IO and fixed/variable rate C/I mortgage –again aimed at helping bridge the borrowing gaps<sup>33</sup>.

**2020:** Covid-19 and any aftermath in terms of falling house prices, reduced risk appetite and indeed reprioritisation in the recovery will impact on innovation, along with the shifting investment priorities by lenders and investors. Government also has significant house price exposure via Help to Buy although so far has made a return of more than 10% on the HTB loans redeemed.

33 Our thanks to Bob Pannell, Adrian Coles, John Heron and Tony Ward for assistance in compiling this timeline.



## Appendix 2: Affordable Home Ownership: Some Relevant Literature

Over the last decade there have been a number of reviews on the broad theme of affordable home ownership, from many different perspectives – from legal, through economic to sociological. The starting point for most of these has been a presumption that ownership is more desirable than renting; that there is a continuing need to fill the financial gap that lies between the ownership and renting tenures and that existing affordable home ownership instruments are less than perfect.

At one extreme is a formal legal analysis of property rights, ownership and the meaning of ownership (focused on shared ownership in Cowans et al, 2018) while at the other is the review by Cromarty (2020) which suggests that shared ownership is a complicated hybrid tenure, which is made more difficult for potential buyers, providers and lenders to understand by a lack of consistency about names, attributes and eligibility.

An older comprehensive review of affordable homeownership schemes looked in detail at their objectives and the extent to which these are achieved by different products –suggesting that there is a need for greater choice and for more lower-risk products (Monk and Whitehead, 2010). Provan et al (2016) pointed out that, while low cost home ownership is often seen as a universal household aspiration (with schemes across most OECD countries) many such schemes are more likely to benefit better-off buyers and are out of reach to most families on average earnings.

Criticisms of the specifics of UK schemes include that there is a high degree of spatial segmentation between individual government schemes, arising from very different sale price points (and income/access limits where applied<sup>34</sup>). Help to Buy tends to favour assisting those in the Midlands and the North (see Finlay et al, 2018) while Shared Ownership is better able to cope with the more extreme market conditions in London and the South East (Walker, 2016).

Walker shows how schemes impact differently on affordability by ‘stretching’ the attainable home price, from £160,000 all the way up to £308,000. He suggests (page 34);

- Households that are highly affordability constrained – perhaps because they live in an expensive area or because they have a family and so need a bigger dwelling are more likely to opt for shared ownership with a relatively low ownership share. Affordability ‘stretch factor’ = +90%
- In London, London Help to Buy and shared ownership with a 50% share have a quite similar impact on overcoming affordability. Affordability ‘stretch factor’ = +45% to +50%
- Outside London, Help to Buy: Equity Loan, Starter Homes, and shared ownership 75% share have a broadly similar and more modest impact on overcoming affordability. Affordability ‘stretch factor’ = +20% to +25%

Walker concludes that “at the regional level the Government schemes appear to be operating in discrete parts of the market taking account of new build dwellings or old, in terms of pricing points

for the ownership or equity shares acquired – de facto, in terms of target household groups”. And he closes by noting (page 61);

The Government housing schemes are almost inevitably more by accident than design: it is hard to conceive we would have the current array of schemes (particularly the mix of shared ownership and shared equity) if the Government was starting from scratch.

<sup>34</sup> See Table 1 in Walker (2016)

But they do appear to be coherent and they are at least fulfilling the Government's key strategic objectives. This coherence could be further conveyed through simplification.

For example, by aligning the key thresholds such as the maximum home purchase price within scheme eligibility.

Elsewhere we note that proposals for developing new schemes are often very context specific. Examples include:

private finance has an important role to play and Housing Associations need to work together to develop portfolios of sufficient scale to kick start an institutional investment market in shared ownership (Alakeson et al, 2013);

to rectify the existing generational inequality in access to home ownership, the Right to Buy (RTB), should be extended to tenants of landlords in the private sector, with discounts capped to prevent landlords incurring losses (Saunders, 2016);

providing landlords with an incentive to sell (Morton, 2018).

None of these texts, and other similar comparable discussions argue against an affordable home ownership strategy and products. Some favour adjusting the status quo, others offer more radical options. Almost all identify weaknesses in the current offerings. Most however take a government policy led stance, unlike the wider "housing systems" approach adopted here. What we recognise at the outset is that the structure of housing provision in the UK comprises a complex, interdependent and dynamic system which has many causal relationships, adaptive triggers and feedback loops in it. This results in constant change and very varied outcomes across localities. Murie, Niner and Watson took a systems approach in their book *Housing Policy and the Housing System* in 1976 and Gibb and Marsh have recently re-iterated some of that thinking (Gibb and Marsh, 2019).