

HousingNorthwest

Credit Crunch Responding to the current market conditions

Friday 5th December 2008, The Reebok Stadium, Bolton

Session notes

Credit Crunch: Responding to the current market conditions

Philip Leather, Nevin Leather

OVERVIEW

- 1.1 Philip Leather's presentation summarised the main points from Nevin Leather's latest six monthly update of the North West Housing Market Review. The analysis itself reviews the following themes:
 - Prices
 - Turn over
 - Loan Finance
 - Affordability
- 1.2 Other areas addressed in the presentation which provide further insight into the impact of the credit crunch on the current market included:
 - New build
 - Repossessions

HOUSE PRICES

- 1.3 In the North West falls in price have not been as dramatic as reported in the mainstream press for the whole of the UK. Average prices for the region have decreased by 6 – 8% in the 12 months according to Land Registry. However, it was stressed that Land Registry data does suffer from a time lag and that other sources such as the Halifax and Nationwide may provide a gloomier picture with more significant falls in price.
- 1.4 Limited falls in price have been the result of limited activity in the market. Currently, less people are looking to sell and less people are looking to buy as many are holding back on transactions in order to see what happens in the near future.
- 1.5 The most severe falls in house prices have been in the urban areas of the North West – Merseyside and Greater Manchester. However, it was explained that house prices had also fallen by the sharpest degree in the lowest value areas of the region – often those areas which were the last to join the previous period of house price inflation.

TURNOVER

- 1.6 Turnover has been hit more dramatically as a result of current market conditions. Volume of sales by quarter in the North West is at about 40% of what it was at its peak last August – with all sub-regions experiencing sharp falls in activity.
- 1.7 The two principle reasons for the drop is the reluctance of buyers and sellers as they wait for further changes in price and the

reduction in the availability of mortgages, especially for first-time buyers. This is the credit crunch's most direct impact.

LOAN FINANCE

- 1.8 There is currently no regional data for loan finance but national data shows that there has been a sudden increase in the amount of a deposit needed to secure a mortgage for first-time buyers – the average deposit is now at 16% compared to a significant period when deposits were close to the 10% mark.
- 1.9 Equally, the average amount borrowed by first-time buyers has fallen from an income multiple of 3.4 to about 3.1. Clearly, it has become a lot more difficult for people to enter the market and to borrow the sums required to purchase property.

AFFORDABILITY

- 1.10 Due to only limited falls in house prices, the affordability ratio has seen only minor changes. The conventional CLG affordability ratio is thus still very high but as prices fall further, in theory affordability should improve.

NEW BUILD

- 1.11 The credit crunch has had a significant impact on new build projects. In the first quarter of this year new build formed only 7% of sales in the region compared to 12% in 2005.
- 1.12 Additionally, new build flats sales have been hard hit – flat sales occupy only 14% of Q1 2008 total new build sales compared to 62% in 2007. It can be concluded that it is the new build flat market that has bared the brunt of the credit crunch. With this, new build prices have fallen to a sharper extent – closer to 10%. The fall also started earlier than in the second hand market.

REPOSSESSIONS

- 1.13 A topical issue at the moment. Latest data shows that repossessions have increased significantly since 2007. CML projections find that repossessions will hit 78,000 next year on the basis of about 40,000 repossessions in 2008, compared to 8,000 in 2004.
- 1.14 Data is also available on charging orders which are orders applied to households with unsecured loans and which can enable repossessions. These orders have risen from 10,000 in 1999 to almost 100,000 for this year. This reflects a big increase in non-secured loans taken out by households over the last few years.

CONCLUSIONS AND CONSIDERATIONS

- 1.15 The main conclusions to be drawn from the available data are that house prices in the region have been affected but less significantly than the drop in turnover. However, the new build market has taken the brunt of price falls as developers are keener to sell. This is likely to feed into the wider market as other sellers will eventually be forced into selling. With prices expected to drop further, affordability is likely to improve though there has been little evidence of it up until now. Repossessions have increased significantly and are expected to rise again in the New Year.
- 1.16 The credit crunch, though a key issue, is about to be overtaken by a more significant issue which is the wider economic recession. Up until now the key characteristic has been the technical difficulty for households in obtaining finance.
- 1.17 A potential new environment of rising unemployment could have more substantial effects. Particularly, in this recession there are far more vulnerable owner occupiers than in previous downturns leading to more widespread financial difficulties.
- 1.18 Another significant impact is likely to be a growth in the private rented sector as people who were looking to buy remain tenants. Together with this, there will be a rise in involuntary landlords as people are forced to move but cannot sell their property.
- 1.19 Demand for social renting has increased over the last five years and it is likely that a recession will add to this demand through further repossessions. However long-term demand is less certain.
- 1.20 Equally, overall long-term demand is uncertain. Previously, inward migration has sustained demand. However if migration falls in tandem with the downturn then demand for housing could drop as well.

QUESTIONS AND COMMENTS

- 1.21 The phenomenon of bankrupt landlords and developers as a result of the credit crunch has left many properties unmanaged and unsecured with owners and renters trapped with very little cover.
- 1.22 It was added by another attendee, whether there was information on the impact on portfolio landlords as they were a key player in the private rented sector and they were often more knowledgeable and able than 'reluctant landlords'.
- 1.23 In response to these points, it was agreed that maintaining standards within the private rented sector was one of the key

challenges presented by the changing market and one which local authorities had to tackle.

- 1.24 The speaker highlighted a situation whereby many private sector tenants had very little security of tenure and that much of the stock was in the hands of a large number of amateur managers rather than a small number of professional managers.

Challengers for the lenders and how to move forward

Peter Williams, IMLA

OVERVIEW

- 2.1 Peter Williams presented the lenders position in relation to the credit crunch and the current economic conditions. In summary, he outlined how the current climate had emerged, what the situation was like at present and the outlook for the future with recommendations for going forward. The opening sentiment was that the situation for lenders was extremely difficult and was getting worse in the short-term.
- 2.2 Explaining the causes of the credit crunch, it was stressed that the overlying reason was the economic boom producing a surplus of cash funds for a shortage of households which in turn led to a disproportionate rise in value of property compared to the basic value of the asset.
- 2.3 However, it was still stated that the US sub-prime was the key trigger in that it was the first market to show this gap between the value of the asset and the price being charged. This then rippled to a wider set of banking crises and led to a contraction in lending abilities. While the contraction was not unexpected, it was the sharpness of the fall that came as such an event.
- 2.4 In terms of the situation now, the housing market is still trending down and the mortgage market, which is now short of funds, has meant terms and costs are higher. As a result affordability has not improved for first-time buyers and non-prime borrowers which has distributional consequences and could add to market downturn.
- 2.5 Beyond the crunch, it is difficult to ascertain as to how long the current market conditions will be sustained. However it is likely to bring a contraction in home ownership which will change tenure pattern in the UK with a growing private rented sector. The lending market is likely to see greater regulation and reworked funding models with lenders looking for higher and stronger risk-based returns.
- 2.6 Key recommendations given to ensure the crisis include a more flexible and adaptable approach with business plans being restructured and greater focus given on efficiency / effectiveness. Partnership working will require greater emphasis, especially between RSLs and local authorities as housing associations are probably in the healthiest state in the current environment. A greater role for the HCA as an investor and lender could also help kick-start flagging developments especially in regeneration areas.

QUESTIONS AND COMMENTS

- 2.7 The first statement from the floor called for a greater focus on funding for regeneration models at the long end of the yield curve which involved the HCA, government and the banks. Peter Williams responded by suggesting that the cross-subsidy model had been suspended rather than fundamentally broken. He added that government would have to play a major role and expected that more direct cash would be injected into the mortgage market.
- 2.8 Another comment came from the floor which sought to ask whether there was sufficient consumer demand for mortgages and whether shared ownership was dead. Peter Williams confirmed there would be continued demand for mortgages and lenders would have to work tactfully to manage their cash flow in current circumstances. In terms of shared ownership, Peter Williams disagreed that it was a failed initiative. He argued that as long as shared ownership schemes were sold responsibly then it was a sustainable option but needed more publicity.
- 2.9 The final question related to the scope for public sector pensions funds to make direct investment in housing and regeneration. The speaker confirmed that there were no significant indices to measure its effectiveness as an investment vehicle and so could not be guaranteed as a safe option by fund managers. However, he suggested that a small holding of residential real estate within a public sector pension fund would be sensible and relatively low-risk. In particular, housing associations could be a key portfolio for potential investors due to their secure position within the market but there had been a failure by public sector agencies to recognise these funding opportunities.

New ways of working

Eammon Boylan, Housing and Communities Agency

OVERVIEW

3.1 Eammon Boylan outlined the tasks of the newly-formed Homes and Communities Agency, providing a specific focus on the current market conditions. In particular, Eammon outlined a six point plan through maintaining activity during the credit crunch which would prioritise:

- flexibility on grant and investment for housing associations,
- exploring joint venture models with developers
- maintaining clearing house and homebuy direct schemes
- supporting local authorities to play a strong role in affordable housing developments
- establishing a direct development capacity for the HCA for a new joint venture (HCA land)
- ensuring that all of the above have strong local labour initiatives

Question and Answer session

Eammon Boylan, Deborah McLaughlin, Peter Williams
and Philip Leather

A significant number of councils have many properties with very little debt on them but are prevented from using the equity from the national HRA system. However, this could be a significant source for affordable housing

Deborah McLaughlin: There is a review ongoing on HRA and how it affects on local authorities.

Peter Williams: There is a greater debate about a 4th way and the government is looking at the role of the local authorities and possibly reviving local authority housing – especially in these times this could be a serious option for the government.

Eammon Boylan: The review needs to look at the issue of raising equity in this market but could not comment until this review is finished.

What chances are there that developers will find sufficient buyers as part of the homebuy direct schemes?

EB: It is unlikely that there will be enough purchasers for the whole scheme but the plan now is to meet the demand that actually exists. There is clearly an issue of appetite among lenders and borrowers at the moment.

PW: Timing is an issue but also HAs could consider it as a short-term hold and there is a strong logic for that.

What more can be done to unlock equity in existing homes to reinvest in the system?

PW: Outlined an equity release scheme in the West Midlands that is an example of a funder who has made a bold move to fund equity release in homes where they will get a pay back only in the long-term.

Mixed tenure developments and their future in the current market conditions?

EB: The reality is that any schemes that have a sales risk will not be delivered though they may return in the future. Thus, it's important that what we put flexible tenure models up and continue with intervention funding schemes in order to deliver mix over a period of town.

PW: There are lot of different packages and tenures and it get's confusing. We need long-term aims with mixed tenure to maintain consistency in these initiatives.

Do we need greater policy direction and regulation in order to manage the growing private rented sector?

EB: The Rugg Review did not predict the seismic shift in PRS. It is not part of the HCA remit now but there maybe scope for the agency to involve itself indirectly in the sector.

Philip Leather: There are short-term impacts on the PRS but we have seen a longer term boost which was only due to a shift in income distribution. Thus we need to change our mindset and realise that owner occupation is likely to contract rather than expand.

PW: PRS' growth fits with the changing labour market but the government has been quite confused as it has never known what to do with the sector. It is hesitant over private landlords but knows it has a role to play. The Rugg Review threatened more regulation when there was a need to expand the sector – somewhat of a contradiction. In Scotland and Wales they are encouraging good standards in PRS rather than punishing poor landlords.

The current market provides a great opportunity for the social rented sector in providing high quality property with considerable diversity to be available in the marketplace for different types of households.

Repossessions

PW: The circumstance that lenders are in now compared to early 90s is very different. One there is a very significant non-prime mortgage market and it is clearly going to be difficult to manage these households through compared to prime mortgages. The government has introduced polices that will help lenders but as a result of securitisation there is significant pressure for further repossessions.

There is a greater consensus this time round that mortgage rescue schemes do not have the necessary impact in averting repossessions.

Responsive session 1: Delivery

Bill Taylor – Regenda Group

Paul Beardmore - Rochdale BC,

Les Brown – Regional Project Director Countryside Properties

OVERVIEW

Les Brown – Regional Project Director Countryside Properties

- 4.1 Les Brown was first to present on the delivery implications of the credit crunch. He outlined how regeneration projects were very complicated with many partnerships and initiatives driving costs up but with very little project finance to work with.
- 4.2 He identified the need for stabilisation in house prices and improved lender confidence to kick-start housing production. For major regeneration programmes, 'open book accounting' with the public sector was called for, whereby there is transparency over cost and what the developer can and cannot afford. Currently total cost exceeds current market value so additional gap funding is required – one possible source would be through the HCA to support costs such as land costs and remediation costs. It was stressed that this was not state aid to developers and that current processes were adequate to provide support.

Bill Taylor – Regenda Group

- 4.3 Bill Taylor's presentation explored the roles of ALMOs and RSLs in responding to the credit crunch. It was outlined that almost a fifth

of stock in the North West is social housing and that many RSLs were threatened by the credit crunch due to more exposure with the market and increased debt compared to the early '90s.

- 4.4 He gave reassurance that most RSLs had strong balance sheets and that ALMOs had more freedom than they had before. The HCA would enable flexibility to adjust programmes to meet current circumstances and will seek new investment vehicles.
- 4.5 Going forward, he confirmed the need for a long-term return investor, likely to be the HCA. It was added that flexibility on programmes was needed now with changes in mix and tenure. Off-the-shelf purchases would be considered as well as products for homebuyers.

Paul Beardmore – Rochdale BC

- 4.6 Paul Beardmore's presentation outlined Rochdale's approach to the credit crunch and offered advice on local authority interventions. It was confirmed that new house building had seen a slow down, similar to the region and nationally. With this, Rochdale was looking to expand social rented house building through working closely with its ALMO and seeking access to prudential borrowing for its own developments and RSL properties. Risk associated with this borrowing can be mitigated with grant funding and partnership working with ALMO.
- 4.7 In the private sector, Rochdale is working with partners to share risk and then take shares in any profits. Other options include Build for Rent and mixed rent schemes. For existing stock, the local authority is seeking to extend advice to households about their options. He also suggested that the council could act as a lender of last resort and provide mortgage products, underwritten by the government.

DISCUSSION – SESSION A

Market rents

- 4.8 Discussion was started with the implications of increases in market and intermediate rents and whether it was a viable option in the present climate, especially as mortgage lending rates were falling at the same time. The panel responded by stating that access to lending was a more pressing issue than affordability in a lot of cases. It was added that the market for intermediate rent was likely to grow as more people were forced out of home ownership and that a culture change towards renting was needed.

Planning System

- 4.9 One delegate highlighted the need for a more flexible planning system to kick-start delivery. In particular looking at the way planning approvals are phased and development agreements are channelled through the system. The panel generally acknowledged the need for reforms in the planning system to make it more simple

and flexible. However, there were concerns with the lag it would take to change planning processes. Another delegate responded by confirming that the planning system is as flexible as it needs to be and so could adapt to new market conditions.

Developer flexibility

- 4.10 Another delegate asked how flexible private sector partners were in the current climate and how far developers were considering changes to their business plan including answering shareholder demands over levels of income, profit and return. Les Brown confirmed that Countryside had already restructured its business plan to reflect longer commitments with developments. He added that Countryside would also look to put equity stakes in developments and then take it out at a later stage.

Role of local authorities

- 4.11 The panel was then asked whether local authorities were in a position to take on more significant levels of risk in leading interventions. Paul Beardmore confirmed that Rochdale Council had made significant risk management considerations when assessing interventions. Another delegate suggested that local authorities were best suited at strategic enabling a networking, securing linkages between different partners and promote housing initiatives.

Town centre flats

- 4.12 One delegate highlighted the negative reputation of town centre flats and asked the panel how these developments would be considered in a few years time. Les Brown confirmed that apartment schemes worked for developers because they make money. He added that there was a market for good quality apartments but that there maybe too many standing in the pipeline. In a regeneration context, it was added that they were an important element in an effective residential mix development.
- 4.13 The consensus was that there was a mix of quality in the apartment sector and in some cases an oversupply. Unfortunately, it was agreed that the poor quality apartments could possibly be subject to demolition in the future due to the market taking its toll.

DISCUSSION – SESSION B

- 4.14 Local authorities can act as mediator to wider organisations and work with assets they already have. If a LA is not land asset rich then they will have problems engaging with other organisations as have limited offer.

- 4.15 If they do not have land available then most effective influence is through the PRS, working with landlords and changing the way internal operations work to make the most of current situations and develop plans for the future.
- 4.16 What do you do if you have a small SH stock and limited PRS? Develop FTBI and ensure that they are widely promoted to increase awareness. This will help the housing market flow and enable people to move up the ladder. These FTBI needs to be innovative as access to mortgages will inevitably be evolving in the next few years to reflect the new economic climate.
- 4.17 Lenders are cautious of LA deposit schemes and prefer the person signing for the mortgage to have saved the deposit themselves. This demonstrates that they have the ability to save and that they are not stretching resources. It also ensures that the mortgagee is committed and has a significant stake in the house meaning that they are more unlikely to abandon payments. This also applies to Government assistance schemes.
- 4.18 Lenders do not necessarily have any knowledge of 'homebuy' or shared ownership schemes and more should be done to improve their knowledge and awareness of products available.
- 4.19 RSLs – majority of RSLs have healthy balance sheets but are not wealthy organisations – they are asset rich but rental stream is relatively marginal. RSLs operate to cover costs they are able to borrow but the amount is limited by rent controls.
- 4.20 How do you unlock the finances that could be available from smaller RSLs or partnership working in the sector?

Responsive session 2: Strategic regional

Pete Bailey, North West Housing Forum

OVERVIEW

- 5.1 Rebecca Riley's (NWDA) presentation (who unfortunately could not attend due to illness) was used to start the session by introducing the economic impact of the credit crunch. It specifically looked at the effects on North West businesses and future employment trends.
- 5.2 Pete Bailey focused more closely on the credit crunch's impact on the housing market. His presentation outlined the long-term changes, short-term responses and medium term conditions of the economic downturn while finishing on the impact for the Regional Housing Strategy.

DISCUSSION – SESSION A

Private Rented Sector (PRS)

- 5.3 Delegates regarded the potential growth of PRS as a key issue to manage. Fears were voiced that the newly formed Homes and Communities Agency may not involve itself significantly in the sector despite its growing role in the wider housing market.
- 5.4 Attendees agreed that the recent Rugg Review was a missed opportunity to provide more strategic direction on the PRS. However, it was seen as a starting point and it could act as a platform to ensure a focus on quality within the sector.
- 5.5 One delegate stated the need to raise discussion over light touch licensing which would be a useful asset to maintaining quality standards in PRS.
- 5.6 There were some calls for institutional funding for the private rented sector as it was becoming a more important aspect of stock. Comparisons were made to the continent where there was greater security in their PRS – especially in lease terms.
- 5.7 It was offered by one delegate that institutional funding has not come forward because of the low returns and risk of residential real estate. However, funding opportunities are more likely to arise with the economic downturn as other forms of investments lose value.
- 5.8 Although it was agreed that PRS was likely to grow as people were forced into renting, one delegate indicated that in Wigan there was actually lower demand and rents were falling.

Repossessions

- 5.9 Delegates agreed that repossessions would continue to increase into next year. It was added that due to securitisation of mortgages in some cases original lenders were no longer responsible for the loan.

Threats to Regeneration

- 5.10 Representatives agreed that the credit crunch posed an extensive threat to regeneration initiatives because the majority of schemes are residential led. Many delegates argued that this model could not function effectively in the current climate. It was added that many regeneration-based developers are quite thinly capitalised companies who relied on market sale to keep them going – currently they were under real pressure.
- 5.11 It was noted that a new public private partnership model needed to be developed although it was acknowledged that many regeneration companies were under threat financially. Also one delegate stressed that local authorities could not wait for long

periods while new models were devised in order to keep regeneration moving.

- 5.12 One delegate proposed a model which used stock transfer funding because it provided a long-term alternative which had previously seen more enthusiastic lending from banks. This model could be adapted for specific regeneration initiatives that could secure 30-40 year funding which would get through market fluctuations.
- 5.13 The panel suggested that developers may be greater swayed by reassurances of sufficient demand rather than grant funding possibilities.
- 5.14 Another delegate highlighted an example of a regeneration project in Hanover whereby 50-year funding had been committed to by banks. This long-term commitment was called for to ensure regeneration schemes deliver.
- 5.15 Community-based models were also offered as alternatives to traditional residential-led regeneration. In particular, Community Land Trusts were identified as a government backed initiative that could be further explored.

Sharing experience

- 5.16 It was put to the session whether housing professionals were doing enough to share experience and best practice and whether there was a system needed to capture networking efforts.
- 5.17 It was suggested that Housing Northwest was in the best position to take on this role. Additionally, all organisations were called on to increase publicity about the independent services available to assist first-time buyers and other relevant households. Central government were already funding advice services which councils need to tap into.
- 5.18 One delegate highlighted an innovative method of engaging households – through speaking to the courts and asking them to send an advice letter out with the first court correspondence regarding repossession.

Shared Ownership

- 5.19 Contrary to much of this disfavour shed on shared ownership, one delegate from Bury Council highlighted that shared ownership was particularly popular and that other affordable housing schemes were in high demand due to relative falls in house prices. It was confirmed that the product needs to be easy to understand and the transaction needs to take place quickly – in these conditions activity could be sustained.

DISCUSSION – SESSION B

Worklessness

- 5.20 There is a real possibility that in the current economic climate the worklessness agenda may lose momentum and when the economy turns we will be in an even more difficult position. How can this be kept on the agenda when there are more immediate and emerging priorities?
- 5.21 The current housing market may also mean that a large number of people effected by worklessness will live in the PRS, how do you reach these tenants and provide advice and support? Instability in the PRS in areas such as Pennine Lancashire where there is a significant reliance on the sector - how can this be co-ordinated on a SR level.
- 5.22 NW local authority LAAs demonstrate that existing commitments to worklessness is not diminishing and people are still working to linking this to the wider agenda (DWP and Jobcentre plus).

Delays with Government and other Stakeholder Data

- 5.23 Delegates highlighted that significant delays to data becoming available in the public domain is causing real problems as the information needs to be audited. Delays very often mean that the data is out of date and no longer reflects the current situation in local areas and it is therefore hard to take immediate and decisive action to make early intervention.
- 5.24 This should be raised as a significant area for improvement.

Student Housing:

- 5.25 Is there potential for students to use empty, repossessed flats or fund developers to finish half completed developments.
- 5.26 In Liverpool and Manchester students are increasingly moving into city centre accommodation. This means that there is an increase in number of family sized dwellings available in the PRS; however issues of landlords who have not worked in this area previously and support may be needed during the transition period.
- 5.27 Concerns have been raised around the potential problems of students moving away from traditional areas to city centre flats. Traditionally students develop a connection with the areas they live in whilst at university and this encourages them to stay once they have graduated. The city centre may not provide this kind of settled environment and they may be less rooted and less integrated into the community and more likely to move on.

Local Housing Need:

- 5.28 Lancashire delegates felt that the RHS does not currently reflect the diverse nature of the sub region and that more work needs to be done to reflect the bespoke working arrangements currently in place. 80% of the current Lancashire housing market is owner occupier and if this falls to the regional average (around 66%) then there will be huge increase in demand for social housing to buy/rent and the PRS. How will this be addressed?
- 5.29 Cumbria delegates stated that if owner occupiers do suffer in the current economic climate then the SR would struggle to provide alternative accommodation. The PRS is not vast and there is a limited supply of existing vacant dwellings that could be purchased by BTL investors.
- 5.30 RHS needs to take account of all SR housing market conditions and variations. It is debatable whether this is the role of the RHS and whether it would be more appropriate to providing advise for the SR who are developing the their strategies to deliver growth.

What if we don't 'bounce' back from the current down turn to the same economic environment?

- 5.31 Regeneration activity in the major cities is based on increasing property prices and developers making inflated profits – how will the current situation affect the regeneration agenda?
- 5.32 If the recession does take place the labour market will inevitably restructure – it is pointless planning for it to return to previous state and consideration of how to move forward should be made.
- 5.33 Should the RHS provide details of how we got into this situation and guidance on how to avoid this again?
- 5.34 Mortgages need to be addressed not the owner occupied market – vast majority of people do not own their homes outright. More range and flexibility is needed in the mortgage market to meet the needs of people at different times in life.
- 5.35 Joint Economic Commission – what should we be telling or asking them? Rethink the perception of homeownership
- 5.36 Look at global housing market and examine examples of best practice of how they operate housing finance models. The PRS in European countries is much more tenant focused with longer and more secure tenancies on offer with more variety of housing available.

The Private Rented Sector:

- 5.37 Wirral has made significant improvements in recent years by introducing a landlord accreditation system and there is a wide spread confidence in the sector – from tenant to LA officer.
- 5.38 How do you enable the PRS to bridge the gap between Social Housing and the owner occupied market? Need to make the PRS an accepted and reliable form of accommodation. Reward landlords

who perform well and tenants need more protection and more open support.