Dear Clive,

Main Estimates 2014-15: Explanatory Memorandum

Please find responses to your questions on the Main Estimates Explanatory Memorandum for 2014-15 below.

1. You stated that the economic benefits of the Help to Buy equity loan scheme are expected to be £500 million to £1 billion. What are the economic benefits of the Help to Buy Equity loan scheme and what is the discounted monetary value of each benefit?

My Department’s estimates on the economic benefits of the Help to Buy equity loan scheme is based on the additional value uplift of a new home, as based on estimates provided by the Valuation Office Agency. The appraisal shared with the National Audit Office used a value of £28,000 per house, representing the net private benefit of a new home, adjusting for any loss of amenity value of land in its current use. This figure suggested £500 million to £1 billion of economic benefits, in discounted present-value terms and in 2013-14 (real) prices.

On 7 March, my Department produced updated estimates on the likely economic benefits of a new home built, increasing the value from £28,000 per home, to £52,000 per home. This provides a much higher economic benefit of £929 million to £1.858 billion - again, in discounted present-value terms and in 2013-14 (real) prices. On 26 March 2014, and in advance of the Public Accounts Committee, Sir Bob Kerslake wrote to The Rt Hon Margaret Hodge regarding this matter, which provides a fuller explanation of these changes.

I would like to add that these estimates do not include all the wider societal benefits of new homes being built – for example, the potential knock on benefits to public health, education and labour mobility. Therefore, these estimates are likely to understate the benefits of the policy in monetary terms.
Finally, these benefits are contingent on the level of “additionality” of new homes being built being between 25-50%, a matter on which I have written to you previously. As I mentioned to you then, we think that “additionality” is likely to be more than 25%, and therefore the scheme represents value for money for the taxpayer.

2. **How regularly are the assumptions underpinning the Help to Buy equity loan scheme model (to calculate the economic cost of the scheme) reviewed?**

In the first year of the programme, the model assumptions (particularly locational split of sales and average prices) were reviewed on a monthly basis. Now that there is more data on actual sales, the model assumptions are reviewed and updated bi-annually.

3. **Has the Department's estimate of the economic costs and economic benefits of the Help to Buy equity loan scheme changed since the National Audit Office's report? If so, what is the latest range of estimates of the economic cost and economic benefits of the scheme?**

I have provided the latest range of estimates on the economic benefits of the scheme in answer to your first question, which ranges from £929 million to £1.858 billion, in 2013-14 prices.

The economic costs highlighted in the National Audit Office’s report, using the Office for Budget Responsibility’s forecasts for house price inflation, suggested the likely economic costs to be between £441 million and £602 million, with a central case of £494 million. Since then, the Homes and Communities Agency has provided a revised estimate for the scheme which suggests the likely economic costs to be between £409 million and £777 million and a central case of £581 million, in 2013-14 (real) prices. This reflects the increased level of investment planned to support 74,000 homebuyers.

These figures will change and become more accurate over time to reflect actual experience of the scheme operating, but none-the-less demonstrates that the scale of the economic costs involved are likely to be much lower than the economic benefits, and therefore demonstrates the unquestionable value for money of the scheme.

4. **The Help to Buy equity loan scheme means that the Government benefits financially if there are increases in house prices. This leaves open the speculation that the Government may be slower to tackle unsustainable house price increases. How does the Department mitigate against this perceived conflict of interest?**

This Government is committed to delivering long-term economic stability and economic growth. The last Administration oversaw a housing boom and bust, and this Government has been picking up the pieces. We have a series of initiatives to boost housing supply, increase the provision of affordable housing and support a healthy private rented sector. By tackling the deficit left by the last Administration, we are helping keep down both interest rates and the number of repossessions. Whilst there have been house prices increases, particularly in London, average prices are still lower in real terms than they were in 2007 and are forecast to stay below that peak for some years to come.
Ensuring financial stability is the primary goal of the Bank of England's Financial Policy Committee. The Bank has already acted with the Treasury to refocus the Funding for Lending Scheme away from mortgages towards small business lending. Recently, the Chancellor announced the intention to legislate in order to give the Bank direct powers to put in place limits on mortgage lending. In the meantime, in its recent Financial Stability Report, the Bank has already moved to put in place measures which will act to mitigate any move to unsustainable house price increases accompanied by increases in household indebtedness.

5. Does the Department have a role in monitoring and mitigating sharp increases in house prices?

The Department does not set price controls for market housing but does monitor activity in the housing market in order to better understand market outcomes and the impact of policy interventions. In the long run market outcomes are determined by the balance between housing supply and housing demand. The Department aims to help people to have a home of their own by getting Britain building again. In order to do this we have a suite of measures in place to tackle a market which had become characterised by low levels of activity. These are complemented by significant investments in the supply of new affordable housing and in the development of a new market that provides purpose built and professionally managed private rental homes. New housing starts reached their highest annual total since 2007 in 2013, whilst starts in the first quarter of 2014 were also up 31 per cent on the same quarter in 2013.

6. How concerned is the Department about the rate of house price increases, especially in London and the South East?

The Department would like to see a sustainable market much less characterised by price fluctuations. Such a market would give more certainty and confidence to builders, buyers and lenders. Recent price rises in many areas of the country may be helpful to market activity, especially in markets where prices are still nominally lower than they were before the financial crisis. And in real terms house prices across the country are lower than 2007 levels and forecast to stay below that peak for some years to come.

However, we are concerned about the level of house price inflation that has been seen in London, where high demand is outstripping supply in the market, both in terms of second hand property and new build. A further sustained period of price rises at these levels would suggest a market being driven less by fundamentals and more by expectations. But the most recent surveys tentatively suggest the market in London may be slowing, whilst mortgage approvals and transaction levels do not currently indicate a market bubble. The National House Building Council reported that 60 per cent more new homes were registered in London in 2013 compared to 2012 (note – these are not National Statistics).

7. Which Help to Buy transactions will be recorded in Annually Managed Expenditure? How much of the £125 million budget does the Department expect to utilise in 2014-15?

The Help to Buy equity loan scheme offers buyers a 20 per cent equity loan that can be used towards the cost of buying a new build home. This budget reflects fluctuations in the value of the equity loans. It does not involve the movement of cash. The Department does not currently expect to utilise much of this budget, and will amend the budget at the Supplementary Estimates 2014 to reflect the latest estimates.
8. **What transactions will be scored against the new £60 million Annually Managed Expenditure budget for the Homes and Communities Agency Housing Supply?**

The £60 million Annually Managed Expenditure budget for the Homes and Communities Agency Housing Supply is to cover any impairments arising from loans and equity investments under Get Britain Building, Build to Rent, Local Infrastructure Fund, Custom Build and Service Plots. This does not involve the movement of cash.

9. **How much funding has been allocated to Round 1 Build to Rent bids?**

There are 10 Round 1 Build to Rent projects in contract, worth £134 million and delivering approximately 1,800 new homes for private rent. The Homes and Communities Agency currently anticipates that 13 Round 1 projects will be in contract by summer 2014, worth £186.5 million and delivering approximately 2,300 new homes for private rent. The remainder of the £1 billion Fund will be allocated via a strong and competitive Round 2 shortlist.

10. **Have there been any delays or set-backs in the Build to Rent programme?**

All Round 1 projects are scheduled to be in contract by summer 2014. Build to Rent is a market-led programme and there have been some projects that have required restructuring by bidders prior to contracting. Contracting is the conclusion to a thorough process of negotiation between the Homes and Communities Agency and bidders to maximise value for money for the taxpayer.

11. **Is the Build to Rent on track to support the development of 10,000 homes for rent by 2015?**

Yes. The Build to Rent Fund is on track to have contracts in place by March 2015 to deliver up to 10,000 new homes for private rent.

12. **The New Homes Bonus budget for 2014-15 is being reduced by £133 million for previous plans suggesting that there have been fewer new housing completions that the Government originally anticipated. What assessment has the Department made of the reasons for the lower than expected level of new homes construction?**

This amendment is owing to how the New Homes Bonus operates, rather than changes in the expected delivery levels of new homes construction- the premise of the question is therefore incorrect. The New Homes Bonus is made up each year of £250 million from the Department’s Main Departmental Expenditure Limit, with the remainder being redistributed from the Local Government Finance Settlement (Local Government Departmental Expenditure Limit). A provisional figure is included in the Local Government Finance Settlement for the amount that may need to be redistributed. This figure is a deliberately conservative estimate, necessary to ensure that the Bonus can be fully funded. It is made clear to authorities that any funding not used for the Bonus is returned in line with their Start Up Funding Assessments. So the reduction in the New Homes Bonus held back funding is not an indicator of housing completions versus expectations.

13. **Does this indicate that the New Homes Bonus does not provide sufficient incentives for local authorities to grant planning consent for new homes?**
No. For example, the District Councils Network has recently commented: “New Homes Bonus has been effective at incentivising growth and housing delivery and this should continue. Districts have used this to support communities, invest in regeneration and keep council tax low.”

14. How does the Department estimate the number of additional new homes built as a result of the New Homes Bonus incentive?

The National Audit Office in their study of the Bonus stated (paragraph 1.25) “Establishing causality for policies in a complex environment such as housing supply is difficult. We agree with the Department’s assessment that it is not possible to separate the impact of the Bonus from other policies and wider factors affecting housebuilding. Neither is it possible to robustly assess what the housing supply would have been without the Bonus.”

The Bonus is one element of a package of measures introduced by this Government aimed at unlocking both supply and demand; to boost both sectors, freehold and rented, and to make the best use of redundant land and empty properties. That is why starts on new homes in past year were up by 31 per cent on the previous year, the highest since 2007-08. Significantly in respect of the Bonus, 230,000 new homes were given planning permission in in the last 12 months, showing that our locally-led planning reforms are working.

15. In October 2013, Sir Bob Kerslake said that “our review of the New Homes Bonus is underway and the groundwork will be completed by Easter 2014”. Has the groundwork for the review of the New Homes Bonus been completed? When will the findings of the review be published?

The groundwork for the evaluation has been completed. Currently the findings are being brought together in a synthesis report, with the assistance of an independent technical advisory group. The findings of the evaluation will be published in due course.

16. The Main Estimate 2014-15 shows Revenue Support Grant of £12,527 million whereas the final local government finance settlement 2014-15 states that the total Revenue Support Grant for 2014-15 is £12,675 million. Could you explain how the two reconcile?

The Revenue Support Grant total for 2014-15 set out in the 2014-15 Local Government Finance Report includes year 2 payments for the 2013-14 round of Council Tax Freeze Grant (£173.963 million) which rolls into Revenue Support Grant from 2014-15. In line with the 2013 Spending Round Settlement letter, Treasury will provide budget cover for the full amount from the Reserve at the Supplementary Estimate. The remaining difference from the figure you quote in your letter (£25.980 million) is the annual budget for Specified Bodies which is also paid from the Revenue Support Grant budget. This figure is included in the amount of Revenue Support Grant determined in Section 3.1 of the 2014-15 Local Government Finance Report.

17. The budget for Research and Data (p13 of Memorandum) has increased by 44% when compared to 2013-14. What will be the main outcomes from the additional £19.8 million expenditure?

The £19.8 million increase relates to European Regional Development Fund losses and write-offs. The increase this year is mainly due to:
• Potential foreign exchange movements as we progress and finally close the remaining 2000-06 European Regional Development Fund programmes,
• Liabilities on both the 2000-06 and 2007-13 programmes arising during and after the Programming period. Some of the 2000-06 debts are quite old and the Department is now considering writing off such debts.

The budget will be revised to reflect latest estimates at the Supplementary Estimates. In May 2010, this Government inherited £236 million in potential liabilities for the 2000-06 European Regional Development Fund. By the end of March 2014, the Department had reduced this to £24.3 million.