



Department for Levelling Up,  
Housing & Communities

# **Previous Housing Market Downturns:**

## **A rapid review and analysis of English housing market downturns and government responses, 1970 to 2023**

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# List of Abbreviations

BoE – Bank of England

BSA – Building Societies Association

DLUHC – Department for Levelling Up, Housing and Communities

DWP – Department for Work and Pensions

ERM – Exchange Rate Mechanism

FCA – Financial Conduct Authority

GDP – Gross Domestic Product

GFC – Global Financial Crisis

GLA – Greater London Authority

HMP – Housing Market Package

HMS – Homeowner Mortgage Support Scheme

HTB – Help to Buy

IMF – International Monetary Fund

ISMI – Income Support for Mortgage Interest

LTV – Loan to Value

MHCLG – Ministry of Housing, Communities and Local Government

MIRAS – Mortgage Interest Relief at Source

MITR – Mortgage Interest Tax Relief

MoJ – Ministry of Justice

MRS – Mortgage Rescue Scheme

NAO – National Audit Office

NHPAU – National Housing and Planning Advice Unit

OBR – Office for Budget Responsibility

OECD – Organisation for Economic Co-operation and Development

ONS – Office for National Statistics

PRS – Private Rented Sector

QE – Quantitative Easing

UKAR – UK Asset Resolution Ltd

RMBS – Residential Mortgage Backed Securities

SMI – Support for Mortgage Interest

## Foreword

This report outlines the findings of a research study which the Department commissioned from Christine Whitehead (London School of Economics) and Peter Williams (University of Cambridge) in December 2022, to analyse four previous housing market downturns in the early 1970s, 1980s, 1990s, and after the 2007-08 financial crisis.

The report adopts a recession-based definition of a housing market downturn, analysing movements in key housing indicators including house prices (real and nominal), housing output, transactions, first time buyer numbers and possessions against the economic and political backdrop at the time. An evaluation of the various government responses, focusing on the specific role played by the Department, provides key policy lessons which can help to inform the Government's response to the current and any future downturns.

As this report highlights, the housing market is by nature very volatile. The booms and busts of previous downturns have varying macroeconomic drivers including inflation, incomes, interest rates and supply side shocks. The housing market has also evolved over time with increasing household formation, the changing tenure mix for both new and existing housing – most notably the rise of the private rented sector from the 1990s which now makes up around 1 in 5 households in England – and worsening affordability. This means that there are different pressures now relative to in the past. However, more stringent mortgage lending via the introduction of stress tests as well as the rise in outright ownership may have given the housing market greater resilience.

The Department has played an important role in responding to previous downturns, with schemes such as the Housing Market Package (1990s), Mortgage Rescue Scheme (2008) and Help to Buy (2013) having significant impacts on housing market outcomes and the impacts on consumers. However, as the report rightfully points out, any response from the Department is limited to the levers held within DLUHC, and the impacts of fiscal measures by other departments will also be very significant.

I would like to thank Christine, Peter and Bob Pannell for their efforts in producing this report, drawing on a huge breadth of research and their own experience and expertise. This analysis helps to build the Department's evidence base on the impacts of past

downturns, and the department will continue to develop its evidence base in this area with a view to informing future policy and improving outcomes in housing market downturns.

**Stephen Aldridge**  
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# Executive Summary

## Introduction

- This report focuses on four housing market downturns from 1970 onwards, related policy interventions and the specific role played by this government department (referred to throughout as ‘the Department’).
- There is no agreed definition of a housing market downturn, but this paper has adopted a recession defined downturn as the starting point. The housing market component of any such recession typically starts before the defined recession and continues after it.
- The key indicators of a housing market downturn include house prices (real and nominal), housing output, transactions, first time buyer numbers and possessions.
- The methodology includes a literature review, personal experience and discussion with Department for Levelling Up, Housing and Communities (DLUHC) officials.
- Most downturns are preceded by an economic upturn. All downturns vary in terms of their causation and how they evolve.

## 1973–1975 downturn

- The so called “Barber boom” led the way. The special circuit of housing finance based on the Building Societies Association’s recommended mortgage rates was ineffective in balancing the need to raise savings rates to get more money to lend and keeping the rate low to limit pressure on existing homeowners.
- The government stepped in to provide loans to the societies. Local authorities were also major lenders (25% of the market). Demand and prices surged leading to gazumping.
- After Labour won the 1974 general elections, there was pressure to get the public finances back in order, resulting in cuts in public expenditure and not least local authority mortgages.
- Higher interest rates, rising unemployment and tighter mortgage lending reduced prices.

- The housing system of the early 1970s was very different from today's market. Notably, social renting made up over 30% of all homes and included middle income households.
- The key lessons from this period are:
  1. International and macroeconomic factors generated both the upturn and the downturn.
  2. The Department could only have power over the supply of housing finance when it was ring-fenced – from the early 1980s this power lay with the Treasury and Bank of England (BoE).
  3. The Department had a significant budget to support local authority housing. Since then, the social rented sector has played a very different role.

### **1980–1982 downturn**

- This was not a sharp recession but a long period of uncertainty and weakening markets plus strikes, the Iran/Iraq war, high inflation, and controls on lending.
- The government embarked on a programme of financial deregulation alongside the introduction of Right to Buy.
- Inflated prices were put under pressure as interest rates rose, despite the cushion proved by mortgage interest tax relief.
- The key lessons from this period are:
  1. The increasingly close relationship between the housing market and wider economy, which has taken decades to be formally recognised in monetary and fiscal policy.
  2. The deregulation of financial services in the 1980s which introduced more competition and innovation into the mortgage market, but also exposed the mortgage sector and housing market to greater volatility and risk.
  3. The continued existence of mortgage interest tax relief which cushioned borrowers from interest rate rises.

### **1990–1991 downturn**

- In the early 1990s the UK had a buoyant housing market, but interest rate rises triggered by joining the Exchange Rate Mechanism (ERM) led to higher debt to



income ratios, and rising unemployment. At the time, mortgage interest relief was being phased out.

- House prices fell and possessions soared. Negative equity became commonplace.
- Government introduced a Housing Market Package (HMP) aimed at taking possessed property off the market thus curbing the downward spiral.
- For the first time government moved to protect housing supply and support housebuilders.
- Social housing providers stepped up to assist and social housing output rose for a short time.
- The key lessons from this period are:
  1. This was a downturn in which the Department played a more identifiable role. The HMP was designed to stop the downward economic spiral being amplified by a depressed housing market.
  2. We also saw a direct attempt to involve social housing providers in helping to support housebuilding, as well as an attempt to support builder balance sheets to protect supply.
  3. The mortgage rescue element and Stamp Duty measure had limited impact on the overall downturn, but did encourage lenders to improve alternatives to possession and created a temporary lift in transactions, respectively.

## **2008–2009 downturn**

- House price inflation peaked in 2007. The Global Financial Crisis (GFC) in 2008 was started by the collapse of sub-prime markets. Lenders ceased to lend to self-certified customers, those with poor credit histories, etc.
- As lending contracted and house prices fell, there was a return to negative equity.
- The BoE began a programme of rate cuts and quantitative easing, including buying in mortgage-backed securities.
- As the market was slow to rebound, the government over some years introduced a wide array of policies including a mortgage rescue scheme, a home-owner support scheme, home buy direct, pre-action possession protocols, easing Support for Mortgage Interest (SMI) restrictions, Help to Buy and more.
- The key lessons from this period are:

1. Policies aimed at boosting homeownership now need to pay much closer attention to the underlying framework of mortgage regulation.
2. Many levers exist outside direct housing policy interventions which can have significant impacts and protect homeowners.
3. Many schemes to support the housing market are introduced during times of crises, thus they have to be developed at speed which may limit their effectiveness. There may be a case for undertaking work on developing policy responses during the fallow periods of housing market cycles.
4. It would be helpful to have clear milestones agreed at the outset for schemes aimed at boosting supply, in order to ensure agreement with the housebuilders on when schemes should be closed.

### **Broad Lessons Learned**

- Three of the downturns were preceded by an upturn, highlighting the continued volatility of the housing market.
- Macro-economic drivers around inflation, incomes, and interest rates were key in triggering housing market downturns, alongside external factors such as wars and oil crises.
- Fundamental changes to the market included increasing household formation rates and the changing mix of tenure for both new and existing housing. The rise of the private rented sector (PRS) from the 1990s was particularly significant.
- Although not part of the project, the government's housing policy response to the COVID-19 pandemic was comprehensive. As in other countries it successfully headed off market downturns.
- The shift from variable to fixed rate mortgages and the introduction of stress tests and macro-prudential rules have given the housing market greater resilience, as has the rise in outright ownership.
- At the same time SMI, now a highly restricted loan, is now weaker while affordability has been stretched by ever higher house prices and slow income growth.

### **Policy and the Department**

- Given the macro-economic focus, HM Treasury is the Department with the most relevant policy levers. DLUHC's policy levers are secondary.

- Despite that, DLUHC schemes such as the HMP and mortgage rescue were important.
- Other initiatives included gap funding, Help to Buy and planning reform, have also been important DLUHC levers.
- Fiscal measures initiated by other Departments such as the Treasury's stamp duty changes, Department for Work and Pensions changes to SMI and Ministry of Justice work on protocols and possessions are also very significant. Monetary policy also plays a particularly important role.

### **Emerging Downturn?**

- Looking at what is now in place, improved mortgage regulation, stress tests and macro-prudential policies have brought new firepower to managing the housing market.
- The market is ultimately underpinned by demand, but in the context of a continuing long-term mismatch between demand and supply.
- New regulation around the Consumer Duty should further enhance the resilience of mortgage borrowers and lenders, through stronger lender forbearance policies.
- The PRS is now acting as a major "reservoir" of potential homeowners but is itself under strain and is potentially weakening would be buyers' capacity to enter ownership.

## Preface

In mid-December 2022, the Department for Levelling Up, Housing and Communities issued an invitation to tender requesting an analysis of past housing market downturns in the early 1970s, 1980s, and 1990s and after the 2008-09 financial crisis and lessons learned from them. The Department recognised that the housing market (in England/UK) was now widely forecast to be entering a housing downturn with, for example, the Office for Budget Responsibility (OBR) projecting a possible 26% fall in transactions and a 9% fall in house prices to 2024. The authors' proposal was accepted in late December with the requirement that this work be undertaken quickly to help build the evidence base, completing the report in March 2023.<sup>1</sup> Bob Pannell, a freelance economist and former UK Finance Chief Economist assisted with this work. However, any errors are the responsibility of the authors alone.

Any opinions given in this paper are the authors' own, and do not represent the views of the Department.

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<sup>1</sup> Please note that some additions were made after completion of the report in March 2023, prior to publication.

# Introduction

1. While the UK in general, and England in particular, has a volatile housing market compared to some others, e.g., Germany, it is far from being alone in facing periodic disruption to the housing system.<sup>2</sup> This is usually brought about by soaring house prices followed by steeply falling prices and all the implications that has for affordability, household movements, the output of new homes and the knock-on effects of all of this on the wider economy.
2. Perhaps surprisingly, given that background, the focused literature on housing booms and busts in the UK is rather limited. This partly reflects the reality that our view of housing problems has changed over the decades. Up until the 1970s the focus was typically on demographic trends, housing supply and housing quality and this also shaped the policy responses. It was when home ownership became the majority tenure from 1970 onwards (as a percent of total dwellings) that the issues of house prices, housing supply and cost of mortgage finance began to loom ever larger as matters to be considered along with the question of “booms and busts”.
3. By way of introduction to the issues, a recent review paper by Savills (2022) offers up a short house price focused history of the UK housing market from 1952 to 2022. This highlighted that over that period the price of an average home has risen by 365%, on an inflation adjusted basis. However, as is very clear, that has not been an unbroken path. Savills offers up a view that, since 1952, there have been 13 different phases in the housing market cycle.
4. As this extended chronology highlights, prices up or down are clearly linked to the performance of the economy, interest rates, sentiment and more – there are a wide range of factors and all are constantly in play, sometimes impacted by government policy. Moreover, as the Savills chronology notes there have been very significant real terms swings in the value of homes, albeit that, over the long run, there has been a significant uplift in their price.

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<sup>2</sup> Stephens, M (2011) *Tackling housing market volatility in the UK*, the report of the Housing Market Taskforce, Rowntree Foundation, York

## Report Structure

5. The approach to writing this report was drawn up based around initial discussions with Department for Levelling Up, Housing and Communities (DLUHC) officials on the definition of downturns and their relationship to wider macro-economic conditions. It was agreed that for reasons of simplicity the research would centre on those periods in the given timescale that were defined as recessions.
6. This was partly driven by the fact that there appears to be no single agreed definition of a downturn either in the UK literature or internationally. Related to recessions there are four economic and related housing market downturns: (i) 1973–1975 which was largely policy based, (ii) 1980–1981 which was also fundamentally triggered by deflationary policies, (iii) 1990–1991 which flowed from the excessive mortgage lending and borrowing in the late 1980s which left consumers exposed to change, and (iv) 2008–09 the Global Financial Crisis (GFC) which was most obviously internationally driven. A fifth recession related to the COVID-19 pandemic has been set aside because the factors causing that were global and less relevant in terms of lessons learned in relation to any potential housing downturn now.
7. Although the analysis is based around economic recessions, the report recognises that housing market downturns often vary from those for the economy as a whole – sometimes starting earlier and often continuing longer.<sup>3</sup> Most commentators concentrate on house prices as a key indicator, especially and as now, declines in for example, the rate of increase in house prices often happen before any defined recession is in place. Housing output in terms of both starts and completions tends to be more relevant further into the downturn and sometimes takes many years to return to pre-downturn levels.
8. The report sets out a clear statement of what happened in each downturn, its timescale, and impact. It then identifies policies used in each downturn with a focus

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<sup>3</sup> See for instance the recently published report for the Joseph Rowntree Foundation which suggest that housing market downturns are usually longer: Lloyd, T, Grayson, R and Hudson N (2023) *Reboot: Building a Housing Market that Works for All*, York, Joseph Rowntree Foundation.

on DLUHC interventions but mention is made of other Departments' and organisations' activity where relevant.

9. The research has explored all of the relevant policy responses for each downturn and what they did to help/hinder – and what legacies they left over for the next time. These are critically examined to clarify the fundamental relationships and bring out implications for the current situation.
10. Finally, the report considers why any downturn in the current economic environment might be different. It pays attention to factors such as the changing interest rate regime, the rise of outright ownership; the concomitant growth of the Bank of Mum and Dad; the shift to fixed rate mortgages and the tighter regulatory regimes now in place.

## **Methodology**

11. Given the timescale and the limited funding and resources, the research and the report are necessarily circumscribed, but works through the following;
  - a. A rapid national and international literature review alongside drawing upon the authors' experience of the situation since 1970.
  - b. Examining each downturn in terms of data and evidence, identifying their attributes and policy responses. Then searching the literature for empirical evidence on whether the policies worked.
  - c. Clarifying the current state of the housing market in 2023 and how this compares with earlier downturns – looking at both before the downturn and the potential recovery period.
  - d. Addressing the detailed questions set out in the brief which included examining the macro-economic conditions; the interventions employed, their impact in different contexts and relevance to current conditions; differences in outcomes with respect to demography, location and tenure; and examining evidence from other countries.

- e. Looking particularly at the role of housing associations; the behaviour of mortgage lenders and how the more limited backstop might affect that behaviour; the position of privately rented housing; the position of first-time buyers; and what is different in the current market.



## Brief Literature Review

12. There is no agreed definition of a housing bust (or boom) in the literature. Some analysts apply the two-quarters decline in house prices, as used with respect to output to define a recession; others opt for a wider definition with a bust being where price falls more than cancel out previous years' gains. There is a good argument for focusing upon turning points as is implied by 'downturn' in our title, although again there are always fluctuations and a turning point will always be a post facto judgement.
13. In terms of formal studies, the UK literature on housing busts and booms is modest compared to the work on housing policy or on housing problems although it is still quite significant in terms of the number of publications. Details of particular examples, including references, are provided at Appendix 2.
14. There are three main groups of relevant publications in the UK literature: descriptive, academic modelling and policy-oriented analysis.
15. The *descriptive* literature is generally made up of historical analyses covering various periods in the twentieth century (e.g. Pawley, 1978; Hamnett, 1999; Holmans, 1987 and 2005). It identifies a range of determinants of booms and busts, notably income growth which increased demand, forcing up house prices; deregulation, particularly that affecting housing finance; and macro-economic policy; as well as speculative pressures.
16. Most of the relevant academic *modelling* literature is also about booms and busts rather than specifically about downturns (e.g. Muellbauer and Murphy, 1997; Otalo-Magna and Rady, 1999). The emphasis is very much on financial liberalisation but also on demographic change, shifts in wealth effects and consumption, alongside real interest rates and income expectations as well as policy shifts. The busts are defined in the main by the reversal of all the factors present in the upturn. In some of the latest work there is a suggestion that traditional modelling approaches are inadequate for predicting the response to cyclical turning points and to large external events.

17. There is a wide range of *policy-oriented* papers. Perhaps the most relevant sets out the findings from a research project (Stephens et al., 2005) that provided an overarching analysis of the Department's housing policies between 1975 and 2000 under five main themes for which the Department had responsibility: supply, need and access; finance and affordability; housing and neighbourhood quality; widening choice; and management effectiveness and relates these to wider economic changes.
18. The work on the determinants of house price change suggests that prices are fundamentally a function of supply and demand for housing with demand being correlated with the number of households and changes in real incomes (MHCLG, 2018). One suggested that house prices were more responsive to interest rates than to the number of households, incomes or changes in housing supply, although responsive to all these factors (NHPAU, 2007). Another looked at the relationship between housing supply and prices (Gerald Eve et al., 1992). Others concentrated on the persistent volatility of house prices and the extent to which policy can modify housing cycles (Stephens, 2011). One view was that the market has become increasingly dominated by the sales of existing dwellings rather than the cost of new building, such that the housing market has some of the characteristics of an asset market where expectations, demand and supply become ever more important (Holmans, 1990).
19. Of particular relevance to this project is the recent report by Lloyd et al. (2023) for the Joseph Rowntree Foundation. The paper identifies four downturns based on housing market behaviour: 1973–1977, 1979–1982, 1989–1995 and 2007–2013, and sets out some of the most important government responses. They argue that financial factors drive booms and busts, but wider economic conditions shape their impacts – with housing conditions also affecting the economy. They conclude that reactive policy changes have less effect over the longer term than well thought through regulatory changes. The authors look at the current situation, identifying risks for recent first-time buyers, Help to Buy recipients, and shared owners. They argue that developers and mortgage providers are in a better position than in the post Global Financial Crisis (GFC) downturn and suggest that the most likely outcome is stagnation in transactions and new supply and, because of inflation,

quite significant real price reductions. Finally, they call for a strategic policy approach supporting supply; taxing short-term purchases; helping first time buyers; targeting support to vulnerable groups and reducing expectations of future house price rises by, e.g., increasing property-based taxes.

## International Perspectives

20. International comparative evaluations are mainly restricted to regular publications such as the annual statistical review by the European Mortgage Federation's Hypostat, which includes an overview of the housing and mortgage markets across Europe and articles on topics of current interest.<sup>4</sup> The OECD similarly undertakes regular reviews of each OECD country as well as overview publications such as *Housing Taxation in OECD Countries*, which covers 'Market Trends and Challenges' as well as a comparative assessment of housing policies and possible reforms.<sup>5</sup>

21. Housing finance more generally has been relatively well covered in the international comparative literature at least since the 1990s. For instance, *Housing Finance in the 1990s* (1993) describes developments in many European countries as well as the USA and Australia.<sup>6</sup> It stressed the growing internationalisation of housing finance markets and that in many countries expanding finance markets had been associated with greater housing market volatility, leading to problems of affordability, possession and lower levels of housing investment.

22. *Milestones in Housing Finance* (2016) compared the situation over a twenty five year period from 1989 to 2016 for some 20 countries and in particular discussed the relationship between mortgage debt and increases in house prices.<sup>7</sup> Of particular relevance is the chapter by Yates, which shows how financial reforms from the early 1980s to mid-1990s had a positive impact on how the Australian

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<sup>4</sup>European Mortgage Federation (2022), *EMF Hypostat 2022: An In-Depth Look At European Housing & Mortgage Markets In 2021*, Available at: <https://hypo.org/ecbc/press-release/emf-hypostat-2022-an-in-depth-look-at-european-housing-mortgage-markets-in-2021/>

<sup>5</sup> OECD (2022), *Housing Taxation in OECD Countries*. Available at: [https://www.oecd-ilibrary.org/taxation/housing-taxation-in-oecd-countries\\_03dfe007-en](https://www.oecd-ilibrary.org/taxation/housing-taxation-in-oecd-countries_03dfe007-en)

<sup>6</sup> Turner, B and Whitehead, C (eds) (1993), *Housing Finance in the 1990s*. National Swedish Institute for Building Research

<sup>7</sup> Lunde, J and Whitehead, C (eds) (2016), *Milestones in European Housing Finance*, Wiley Blackwell

system responded to the GFC in terms of stability, but negative impacts on distribution.

23. A particularly relevant article by Jorda et al. (2015) reinforces her message. The paper looks at seventeen countries over the past 140 years and demonstrated that it is leverage bubbles, involving massive increases in credit availability, that lead to deeper recessions and slower recoveries.

24. Finally, *Global Housing Markets Crises Policies and Institutions (2012)* covers the causes and consequences of the sub-prime crisis and the GFC across the USA, Western Europe, Transition Countries and Asia – plus four countries, Australia, Brazil, Canada and Israel, which showed various levels of immunity to the contagion effects of the GFC.<sup>8</sup> Lessons included: regulatory structures when enforced made a difference; global linkages played a role; quick decisive public sector responses helped (with Australia, which reduced interest rates and incentivised first time buyers, especially with respect new build, as the main example).

## **Defining Downturns**

25. As noted earlier, the definition starts from the broader concept of recession and includes all those where peak to trough runs for two quarters or more. There are five such periods since 1965, in four of which the housing market also suffered downturns measured in terms of real house price falls.

26. What is clear from Chart 1 below is that, while the pattern is generally similar, the point at which real house prices (dark blue line) start to fall sometimes occurs slightly before the peak from which the recession is measured. Also, in the 1990 recession real house prices hardly rise and indeed fall again, only becoming positive in 1996. After the 2008 recession there is a somewhat similar pattern –

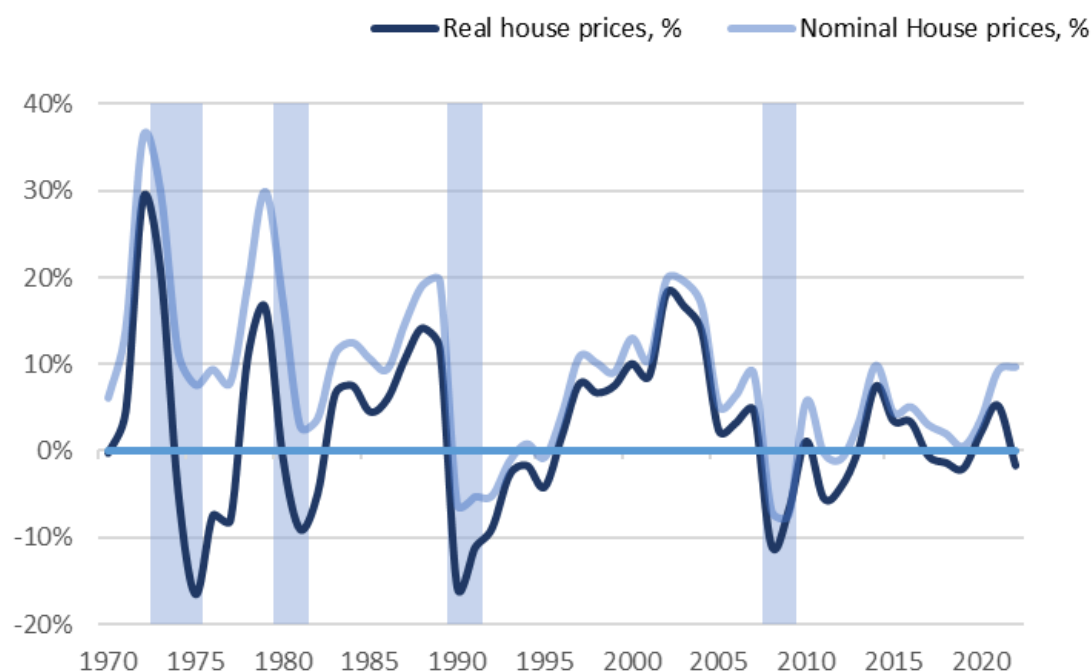
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<sup>8</sup> Bardhan A et al (2012) *Global Housing Markets: Crises Policies and Institutions*, Wiley. The chapter by Scanlon and Whitehead covers the UK and other selective bubbles in Europe.

falling back almost immediately and remaining negative for at least three further years.

27. A second issue with respect to housing market downturns is whether real house prices is the most relevant measure. It is likely to be the lead indicator, followed by transactions. On the other hand, from the point of view of policy timing, it might be useful also to take account of the earlier peaks which reflect the rate of price increases starting to fall. In other words, when the strength is going out of the boom.

**Chart 1. Changes in House Prices, 1970–2021**



Source: Chart 1, Appendix 1: House prices real and nominal

28. There are also a range of variables that make up a housing market downturn which did not all adjust directly in line with one another – including not just real house prices but also nominal house prices (light blue line), i.e., not adjusted for inflation; numbers of transactions; housebuilding and indeed first time buyer numbers. How they relate to each other is another relevant issue for determining policy (see charts 2-7 in Appendix 1).

29. The emphasis on downturns (especially as narrowly defined here) may also not be the most appropriate period for analysis. Understanding the period prior to the downturn, which in all the four cases discussed include significant booms as well

as more general volatility, almost certainly impacts on the depth and length of the downturn. Equally, especially if the objective is to bring investment back to pre-downturn levels, understanding the recovery period is just as important. More fundamentally, the housing market is clearly more volatile than the economy as a whole, and as it is much easier to adjust housing investment downwards than to get the system working again, this has significant longer term negative implications.

30. It is worth noting that, in real price terms, the extent of both peaks and troughs have declined over the forty year study period, with both the peaks and troughs becoming less extreme, making the total peak to trough fall in house prices smaller. One can only speculate that this may be related to a better understanding of fundamentals or possibly also to the greater openness of the financial system. Importantly, lower rates of general price inflation may mean that more of the housing adjustment falls on investment activity rather than prices, as reflected in the longer periods before output levels return to earlier levels.
31. Overall, there is a good argument for focusing upon turning points as well as just downturns even though the former cannot readily be predicted. However, this paper sticks with the agreed recession-based definition. This will aid comparison and discussion.

## **Past Housing Downturns: A chronological account and assessment**

32. This section sets out a clear statement of what happened in each downturn, its timescale, and impact. It includes and discusses data on the downturn in the housing market and on macro-economic variables, and identifies policies used in each downturn by the Department for Levelling Up, Housing and Communities (DLUHC) and other departments. It briefly discusses other policies, including regulatory changes with respect to mortgages, and considers the interaction between the different policies. Finally, it analyses the relevant policy responses for each downturn and what they did to help/hinder – and what legacies they left over for the next time.

### **Housing Downturns**

33. A series of charts are provided in Appendix 1 including all the key housing market indicators such as house prices, supply, first time buyers, arrears and possessions and then key wider economic indicators such interest rates, inflation, GDP, and unemployment covering all four downturns under review. An additional useful resource is the BuiltPlace website, which as part of its Digging Deeper section, has pages devoted to downturn data (see <https://builtplace.com/subscribers/digging-deeper/housing-downturns/>).

34. It is necessary to discuss the earlier upturns as well the downturns as they provide the context, including relevant government interventions. The first four downturns were, as might have been expected, immediately preceded by periods in which there had been sustained house price inflation. The 2008 downturn was however rather different, as its direct cause was the Global Financial Crisis (GFC) starting in the USA. In the UK, it had been preceded by a long period of housing market growth until 2005, and then a further short upturn before the crisis.

## **1: The Downturn 1973–1975**

### **The preceding upturn**

35. Before the downturn the housing market was the strongest in living memory according to Holmans (1990), with nominal prices more than doubling in three years. Pawley (1978) notes that the average price of a new dwelling on which a mortgage was granted in England and Wales rose from £5,020 at the end of 1970 to £10,690 at the end of 1973 – a gross increase of £5,670 or 112%. Little wonder that the term “gazumping”, came into daily parlance as even accepted offers were quickly trumped by new and higher bids as prices spiralled.
36. As can be seen from Chart 1 this was the strongest price upturn in the four cycles examined here in both nominal and real terms, as well as being one of the strongest downturns in real terms.
37. The upturn was built on the back of the Heath government’s expansionist economic policies, the so called “dash for growth” (and the “Barber Boom”, named after Anthony Barber, the Chancellor of the Exchequer’s budget in 1972). A wage/price spiral ensued along with high inflation and an expansion in the supply of mortgages. The government recognised the problems that were being generated in the housing market and through the National Economic Development Office issued details of a proposed new low start mortgage. The Chancellor of the Exchequer also then reduced Stamp Duty so that some 90% of homes escaped it altogether – encouraging transactions. A wave of property speculation by both individuals and corporate entities unfolded which included exploiting government provided home improvement grants to boost the value of acquisitions of older existing homes and sell on.
38. At this time local authorities issued up to 25% of home loans, usually at fixed rates and notably on pre-1919 properties where building societies, the dominant funders of house purchase, were reluctant to lend. The latter’s mortgages were priced using a recommended rate set by their representative body, the Building Societies Association (BSA). This rate was often not market clearing, so mortgage queues were common. Keeping rates low fuelled demand but it also meant that savings rates were low with the result that the inflows were sometimes well below that demanded by building societies. As a consequence, the government was often under pressure to support this so called “special circuit of housing finance” by



making a variety of interventions to ensure the flow of and cost of funds were maintained at an acceptable level.

### **The Downturn: late 1973–1975**

39. The oil crisis of late 1973 was the most immediate source of problems in the wider economy. As a result of the crisis, output was declining and the pound was under pressure with the Bank of England (BoE) trying to manage the situation. The special housing finance circuit was an element that had to be managed formally by the Department.
40. As Pawley (1978) notes, in 1973 the government made a loan to the building societies (£15 million) to keep mortgage funds flowing. However as both inflation and interest rates rose in 1973 (the BoE minimum lending rate as it was called rose from 9% on 23 July to 13% on 13 November) so house prices slowed and new housebuilding fell back sharply. The government loan had limited impact and the building societies' net receipts were at £1.5 billion while mortgage outflows were £3.5 billion – little wonder the societies began talking about much higher loan rates, perhaps up to 14%.
41. The government then tried a new tack, signing a *Memorandum of Agreement* with the BSA to help maintain the flow of mortgages and support housebuilding, along with efforts to stabilise house prices and support home ownership. This evolved into an attempt at mortgage rationing around a priority list of borrowers via a Joint Advisory Committee backed by a technical sub-committee that provided insights into the housing and mortgage markets.<sup>9</sup>
42. In 1974 the Conservatives lost power with the recession firmly underway. They were replaced first by a minority Labour government and then after a further election in the same year Labour secured a small majority. The new administration made a further agreement with the societies. Inflation and unemployment continued to rise, as did mortgage possessions – from 1,060 in 1973 to a peak of 4,300 in 1976 (see Chart 11, Appendix 1). By 1976 Britain faced a financial crisis,

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<sup>9</sup> DoE (1980) *The Guideline System, a report by the Technical Sub-committee of the joint Advisory Committee on Building Society Mortgage Finance*. See also BSA (1981) *The Determination and Control of House Prices*, and BSA (1978) *Cooperation between building societies and local authorities*, BSA, London.

with the government being forced to apply to the International Monetary Fund (IMF) for a £4 billion loan. This was granted on the condition that there were deep cuts in public expenditure (which included cutting local authority mortgages). House prices declined in real terms between 1974 and 1977 and starts fell back sharply (see Chart 4, Appendix 1).

43. The Labour government initiated a series of housing related reforms as well as putting in place a comprehensive *Housing Policy Review*.<sup>10</sup> The reforms proposed included modifying the structure of housing subsidies for local authorities, new rent setting rules in both public and private sectors, a shift to area-based improvement and away from clearance and much more – although some of this never got to the statute book in part because the Labour government lost power in 1979.

44. With the cutback in local authority mortgages, the government initiated a support lending scheme with the building societies offering mortgages on pre-1919 properties via the local authorities who could also provide mortgage guarantees. Take up improved over time but the scheme had limited success in terms of maintaining the flow of funds to this market.

## **Assessment**

45. The housing system of the early 1970s was very different from today's market, which makes it more difficult to take messages from that downturn. Notably, the tenure mix was roughly 50% owner-occupiers, almost 30% social tenants and 20% private tenants. Housing associations played only a minor role in provision.<sup>11</sup>

46. Departmental policies concentrated on direct subsidies to local authorities to build new homes; setting rents in the social sector – which moved from a cost-based approach to what were called “fair rents” (although reform was delayed by the downturn) – and managing flows of funds from building societies.

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<sup>10</sup> Published as *Housing Policy, A consultative document* in 1977 (Cmnd 6851) along with three technical volumes which even today offer up some of the most in-depth analyses of housing ever undertaken.

<sup>11</sup> See Chapter 1 Trends in Tenure, English Housing Survey: Households 2013-14

47. In terms of housing finance, building society loans were not available to a whole range of people including singles, women and those who had not saved in the building society usually could not obtain a mortgage. Over 70% of loans came from building societies with around 25% from local authorities. As noted earlier there were substantial swings in the intake of funds by building societies and hence in the amount of funds available for lending. In this period the result was a “mortgage famine”, which in turn helped generate a housing market slump – the number of private sector dwellings started halved between 1973 and 1974. The swing from (comparative) plenty to famine in the supply of mortgage loans and from “boom to bust” in the housing market put stabilisation of mortgage finance high on the Department’s future agenda.
48. Under the Guideline system the government provided loans to building societies at £100 million a month for five months from April 1974 to help maintain the flow of finance for house purchase loans. By the end of the scheme interest rates had fallen back to a point where building societies were able to take in sufficient funds from investors, both to maintain an adequate level of lending and to repay these loans.
49. More generally, when the inflow of funds was more than sufficient to maintain the required amount of lending the excess would be added to liquid assets; and when the inflow was falling short, liquid assets would be drawn on to finance the guideline level of lending. Clearly this type of approach could not survive in a more market-oriented finance system and the system was suspended in 1979.

### **Lessons to be learned?**

50. Perhaps the most important lessons from this period are:
- a. It was clearly international and macro-economic factors which generated both the upturn and the downturn. Housing demand simply responded to that volatility and the Department then had to manage financial flows for mortgages.
  - b. The Department could only have power over the supply of housing finance when it was a ring-fenced system. From the early 1980s those powers effectively lay with the Treasury and the Bank of England, both of which had

wider objectives. In the downturn the short support lending scheme had some merit and it did help encourage building societies into the pre-1919 housing market. Today that distinction no longer exists.

- c. The Department had a significant budget to support local authority housing which could in principle be used to help manage the downturn. Importantly the mix of households in that sector overlapped with those in owner-occupation, a situation that only changed with the introduction of Right to Buy in 1980. Since then, the social rented sector has played a very different role (albeit social housing providers also offer shared ownership schemes with the first national scheme introduced in 1980).

## **2: The Downturn 1980–1982**

51. This housing market downturn, unlike the other three identified downturns, can be seen as more the result of a long period of economic uncertainty which was particularly difficult because of both high inflation and high unemployment.<sup>12</sup>

### **The preceding upturn**

52. In 1977 the house price to income ratio was moving back into some kind of equilibrium and the stage was set for a second surge in prices which began in 1978 as real incomes rose for a short period but, more importantly, as inflation took off (see Chart 1). The economy was very unstable with the so called “winter of discontent” – mass strikes and labour unrest and political uncertainties around the election in 1979. Inflation was partly caused by the Iran-Iraq war, which led to a second oil crisis.

53. The housing market was less affected than might have been expected, given the wider uncertainties in the economy. Nominal house prices rose 7% between 1975 and 1977, 17% in 1978, 29% in 1979 and 15.5% in 1980. But because inflation was rising as well, real house prices rose more slowly, becoming negative for the last two years of the decade.

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<sup>12</sup> Merrett, Stephen, and Fred Gray (1982) *Owner Occupation in Britain*. RKP, London

## The Downturn: 1980–1982

54. The most important structural change was from the highly regulated housing finance system described earlier to a completely restructured and much more competitive market, which also enabled the banks to become major competitors in the market. In the 1970s, the supplementary special deposits scheme (the 'corset') restricted banks' ability to raise funds for lending with penalties if their deposits grew faster than set limits (it was last activated in June 1978 to June 1980 and was abolished in the mid-1980s).<sup>13</sup> The uncertainties in the more general economy made the mortgage market attractive to banks. Initially their focus was on up-market lending but over time there was a growth in higher Loan to Value (LTV) mortgages, i.e. beyond the typical 70% LTV loan, along with increased competition for savings.<sup>14</sup> This was now a fully open housing finance market with mortgage volumes and rates driven by forces in the wider economy and notably by the Bank of England. Local authority mortgages largely ceased to exist as an option and indeed over the coming years the local authorities sold their loan books to mortgage lenders.
55. However, as Hamnett (1999) notes, the Bank of England interest rate, having fallen back in 1977, began to rise in 1978 and kept climbing, reaching 17% in November 1979 as the authorities sought to control inflation. Nominal house prices fell back in 1981, rising by just 2.1% in that year and 3% in 1982 (in real terms -9% in 1981). Possession cases more than doubled from 2,910 in 1979 to 8,400 in 1983.
56. The policy interventions over this period were not directly related to the observed short downturn but were rather about restructuring the housing market and housing provision in line with the Conservative government's objectives of expanding owner occupation together with market deregulation across the economy.

## Assessment

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<sup>13</sup> Bank of England (1982), The supplementary special deposits scheme <https://www.bankofengland.co.uk/-/media/boe/files/quarterly-bulletin/1982/the-supplementary-special-deposits-scheme.pdf>

<sup>14</sup> Bank of England (1990), *The development of the building societies sector in the 1980s*, Bank of England Quarterly Bulletin: November 1990, Available at: <https://www.bankofengland.co.uk/-/media/boe/files/quarterly-bulletin/1990/the-development-of-the-building-societies-sector-in-the-1980s.pdf>

57. The most fundamental change following the election of the Conservative government was the deregulation of the housing finance market. In 1980, not only was the corset on banks removed, but building societies were permitted to provide non-mortgage products and so compete more directly with banks in other areas. Then, in 1986, the Building Society Act allowed societies to 'demutualise' and become banks, leading to significant restructuring and further competition. This in turn stimulated the housing market by producing fiercer competition amongst mortgage lenders and helped generate an increasingly rapid upturn that only ended in 1990. Importantly, efforts to limit mortgage tax relief, strongly supported by economists, were rejected on political grounds. The continuation of tax relief in an inflationary economy encouraged continued indebtedness, benefited mortgagors and supported housing demand and prices.
58. The immediate cause of the short downturn was the rapid rise in inflation and the associated increases in interest rates needed to try to stabilise the economy. Private housing starts fell to just below 100,000 in 1980 (see Chart 5 in Appendix 1), a decline which was not matched until 2009 and 2010, but then recovered. But overall starts continued to decline until 1985, as a result of cutbacks in social housing investment – an outcome of policy decisions.
59. Politically, the biggest policy change was the introduction of the *Right to Buy* in 1980. In the first three years nearly 400,000 homes were sold boosting annual transactions by around 10% per annum. Over a million homes were sold in the first seven years, significantly changing the nature of the lower part of the housing market with, at least initially, little increase in mortgage risk. The policy continued with varying less generous discounts over the following decades.
60. The cuts in public expenditure in 1980 had an immediate impact upon the supply of publicly funded housing, with starts falling from 77,000 in 1978 to 35,000 in 1980. Local authority rents increased, rising in real terms by 44% between 1980 and 1982. Public funding for local authority mortgages was reduced even further.
61. Taxpayers were entitled to offset their mortgage interest costs against their tax liabilities. It was originally partially offset by Schedule A tax – a charge based on the imputed rental income of the home – but this was abolished in 1963. Tax relief

was continued. In 1983 Mortgage Interest Relief at Source, or *MIRAS*, was introduced to help the large numbers not making annual tax returns by which the relief had been reclaimed. In the 1983 Budget the Chancellor, Geoffrey Howe, also raised the tax threshold allowance for a mortgage loan from a maximum loan size of £25,000 to £30,000.

### **Lessons to be learned?**

62. The downturn was triggered by pressures in the macro-economy and not least by rising interest rates. Housing supply slumped and mortgage borrowers came under strain. In terms of lessons learned the most obvious are;

- a. The close relationship between the housing market and the wider economy. It has taken some decades for this to be more formally recognised in the working of monetary and fiscal policy.
- b. The deregulation of financial services in the early 1980s had long-lasting impacts. It introduced more competition and innovation around the mortgage market but it has also exposed both the mortgage sector and the housing market to greater volatility and risk.
- c. The continued existence of mortgage interest tax relief (*MITR*) and the subsequent *MIRAS* scheme cushioned borrowers from interest rate rises. *MIRAS* was slowly reduced in the 1990s and finally abolished in 2000. That cushion is no longer in being and borrowers and others now face full market rates and volatilities.

## **3: The Downturn 1990–1991**

### **The preceding upturn**

63. Property transactions had reached a high of 2.15 million in 1988 (see Chart 3, Appendix 1) partly caused by the Chancellor giving four months' notice of the removal of the double mortgage interest tax relief in the April budget.

64. Deregulation had increased the opportunities for individuals to borrow money and the ratio of household debt to income reached 100% in 1987 and climbed to 114% by 1990. Unemployment also rose from 1.8 million in 1990 to over 3 million in 1992 (see Chart 15, Appendix 1). Given house price inflation, *MIRAS* was defraying ever less of the mortgage interest bill (in the mid-1970s around 40% of total mortgage interest was covered by tax relief) and thus owner occupiers were more exposed to the costs of rising interest rates (although those with a few years of ownership had of course enjoyed considerable house price uplift).

### **The Downturn: 1990–1991**

65. In 1990 the UK joined the European Exchange Rate Mechanism (ERM). The UK had had to raise its interest rates to protect the unrealistically high three deutschmarks to the pound. This impacted upon the UK's housing market, competitiveness and economic growth as the economy was facing high inflation and interest rates and the pound was weak. Mortgage interest rates rose from around 9.5% in May 1988 to a peak of 15.4% in February 1990 before falling back slightly in late 1990 and dropping to 11.5% in September 1991.

66. Transactions fell back to 1.6 million in 1989, 1.4 million in 1990 and 1.14 million in 1992. The fall in transactions was largely concentrated in the four southern regions of England where the upturn had been most marked (reflecting both the concentrations of two earner households and the price pressures).

67. Hamnett (1999) argues that this downturn was different in a number of ways, most notably in terms of the size of the fall in both real and nominal prices and the resultant rise of negative equity – estimated to have impacted 2 million households at the peak. This itself then helped trigger rising arrears and possessions. Confidence plummeted, and with nominal price falls, there was a real sense of a loss of wealth. Although 1990-91 were the most difficult years the reality is that the housing market downturn really dragged on until at least 1995. The downturn was also notable for its duration in housing output terms. The upturn in private sector starts, although it began in the very early 1990s, never returning to its peak of around 220,000 in 1988. Housing Association starts (see Chart 6, Appendix 1) did rise rapidly for a short period during the downturn, reflecting increased funding,



and reached a peak of over 40,000 units (again never, as yet, exceeded) but was followed by a rapid fall until nearly the turn of the century.

68. The housing market recession in the early 1990s, following the upturn in the late 1980s, showed that deregulation had added to housing market instability with greater risks for individuals and institutions. It also greatly strengthened the link between the housing market and the wider economy by making housing wealth more liquid (so, for example, facilitating equity withdrawal). Although instability predates deregulation, it has clearly contributed to the amplitude of the cycle. As such it was indirectly responsible for the rise in arrears and possession in the early 1990s.
69. There was a surge in mortgage possessions, up from 15,800 in 1990 to 43,900 in 1991 and peaking at 75,500 in 1992 (see Chart 19, Appendix 1). At the end of 1992 over 200,000 households were in mortgage arrears of more than 6 months. With large numbers of possessed properties on the market (around 1 in 4 transactions involved a property that had been taken into possession) this “overhang” was seen to be depressing prices and forestalling a general recovery. Almost inevitably this resulted in lower house prices in both money and real terms and reduced mortgage advances until the middle of the decade.
70. The policy response was inherently intertwined with macro-economic conditions. The Major Government was under considerable pressure on all fronts. The UK left the ERM in September 1992, on so-called “Black Wednesday”. This was almost inevitable as, already noted, the UK had entered the ERM at too high an exchange rate.
71. On exit, the government and the Bank of England settled on inflation targeting as a way of anchoring the pound. In 1992, the UK government issued a mandate for price stability. This stated that the target retail prices index excluding mortgage payments was to be 1–4% and that inflation should be in the lower half of the range by 1997. The target has changed a few times since 1997 and is currently set at 2%. Bank independence was not immediately adopted in the UK, but from 1992 there were checks on the ability of the government to base interest rate decisions on political rather than economic reasons. This highlights that the strength of

macro-economic factors impacting on the UK housing market is clearly still the case.

72. More specifically, the Government needed to stem the flow of possessions and especially the flow of possessed property on to the market. In addition, builders were sitting on large stocks of unsold homes which were putting pressure on their balance sheets and resulting in even lower output of new homes.

73. In November 1991 the government responded to the severe housing market downturn by announcing a special *Housing Market Package (HMP)* of around £600 million to be invested in housing associations buying up unsold private sector homes. As the Housing Corporation evaluation shows, of the 18,430 homes bought under the scheme only 7% were mortgage possession cases, 50% were from developers and some 41% were purchases of existing homes in the market.<sup>15</sup> The review report offered no evidence that it helped restore confidence in the market but did suggest it had helped create longer chains of sales, although this is hard to confirm. A secondary objective of helping a small number of those in need obtain affordable homes was achieved.

74. The report also reflected on some of the downsides – purchases were scattered rather than concentrated, the timescales for acquisition were lengthy, and, of course, there were political tensions around the outcome which mixed private and social homes.

75. On 19 December 1991, the Chancellor of the Exchequer announced that in the light of evidence put forward by lenders that money was often diverted to other uses by borrowers, *Income Support for Mortgage Interest (ISMI)* would in future be paid direct to the lender rather than via the recipient.<sup>16</sup> This was introduced in April 1992 with lenders agreeing that where recipients were not in arrears with respect to mortgage interest, they would not take possession of the home. Where *ISMI* was not payable, the largest lenders agreed that they were prepared in case of need to provide funding on concessional terms to help borrowers to remain in their homes.

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<sup>15</sup> Housing Corporation (1995) *the Housing Corporation's implementation of the housing market package (HMP)*, Housing Management and Research Division, Report no 5, Housing Corporation, London

<sup>16</sup> Parliament UK (1991), *Housing Repossessions*, Available at:  
<https://publications.parliament.uk/pa/cm199192/cmhansrd/1991-12-19/Debate-1.html>

In such cases, the homes would either be sold to housing associations or taken into ownership by the lender.

76. These moves assisted in reducing the number of mortgage possessions to 49,210 in 1995, down from 75,540 in 1992. The number of borrowers with long term arrears (6-12 months) also fell from 164,600 at the end of 1993 to 133,700 at the end of 1994 and 73,800 in 1997 (see Charts 18 & 19, Appendix 1).

77. The Chancellor also reduced stamp duty for a period of eight months. It was normally charged at 1% on the full price of land and buildings costing more than £30,000. He raised the threshold to £250,000 until 19 August 1992, after which it would revert to £30,000. This meant that no stamp duty was payable on 90% of private home purchases. The cost to the Exchequer was about £110 million in the 1991-92 financial year and about £310 million in 1992-93. In 1993 the tax threshold was doubled from £30,000 to £60,000, though the impact was blunted by a cut in mortgage interest tax relief to 15%.

## **Assessment**

78. It was widely recognised that the lenders “mortgage rescue” scheme reduced the likelihood of default and loss on the mortgage but of course the household still lost their home and, usually, became a tenant. Lenders tailored their own solutions for people in difficulty, including loan restructuring and forbearance – schemes they promised to maintain and are in principle still applied today. In a small number of cases, notably the Bradford and Bingley Building Society, the lender relet the possessed homes back to the families that previously occupied them if they so wished. The Society built up a portfolio of around 1,700 homes as a rental subsidiary (this was ultimately sold out to the managers of the scheme who were supported by a loan from the Halifax Building Society). That entity remains in operation today.

79. The *HMP* did bring benefits, not least to housebuilders’ cash flow and to housing associations. Its direct impact on lender possessions was more limited but it stimulated the industry to do more and, of course, the *ISM* adjustment brought major lenders into an agreement with government.

80. A slow recovery in prices began in southern England in 1993, although not in the north until 1996. This was aided by a rise in real incomes and therefore a sharp fall in house price to income ratios. The policy responses taken together helped restore confidence in the market and return it to a more normal state, albeit not until the mid/late 1990s. Private sector starts rose slowly but to nowhere near to the levels achieved in the earlier peak. Housing association starts, on the other hand, fell rapidly from their peak in 1993.

81. The costs of the downturn were considerable. For example, lenders write-offs on irrecoverable losses rose from £18 million in 1990 to £1.03 billion for the two years 1992 and 1993 with provisions of £2.3 billion. Similarly, insurance companies saw their related losses rise from £48 million in 1990 to £1.37 billion in 1991.

### **Lessons to be learned?**

82. This was a downturn in which the Department played a more identifiable role, albeit in conjunction with HM Treasury. The housing market did not trigger the downturn, but it quickly became a centre of attention both politically and economically.

- a. The move to create the *HMP* drew directly on the skills and capability of the Department, bringing together its funding capacity with actions designed to stop the downward economic spiral being amplified by a depressed housing market.
- b. There was a direct attempt to involve social housing providers in helping to underpin the private housing market and to support housebuilders.
- c. The mortgage rescue element was less directly successful, but it did encourage lenders to improve their alternatives to possession and eviction.
- d. The stamp duty measure had limited impact, although as Chart 3, Appendix 1 shows, there was a temporary lift in transactions in 1993 and 1994 before falling back in 1995 – suggesting activity had been brought forward – which also brought forward demand for products associated with moving house.

- e. This was the first downturn where there was an attempt to help support builder balance sheets and thus protect supply capacity.

## 4: The Downturn 2008–2009

### The preceding upturn

83. From the early 2000s commentators were becoming ever more concerned about the rate of house price inflation – 16.2% in 2002, 15.7% in 2003 and 11.9% in 2004 then slowing to 5.5% in 2005 before rising again to nearly 11% in 2007 (see Chart 1). The UK was not alone in seeing prices surging, but the OECD argued that in the UK, Spain and Ireland there was increasing evidence of over-valuation.<sup>17</sup> Interest rate cuts over the period 2000–2003 had fuelled a spirit of optimism (before they started to rise again in 2007). There was record borrowing and both new products and lenders emerged to reflect this – notably with significant reliance upon the mortgage securitization process.<sup>18</sup>

84. House price inflation peaked in mid-2007 (depending upon the index used and the region in question) when the sub-prime crisis in the USA first became newsworthy. Mortgage lenders had been making loans to borrowers who had weak credit histories and capacity. The loans were inadequately priced to reflect those risks. Questions started to be raised about the value of such mortgage assets which had, via the securitization market, been placed with investors around the world. Northern Rock, a long-established UK mortgage lender, had made significant use of the securitization market to fund its expansion and was the first to be identified as exposed (it was provided with emergency funding by the Bank of England and was then nationalised in February 2008). Efforts to cover this via higher interest-bearing retail deposits were problematic in that this also meant mortgage rates had to go up. Contagion spread across the market, with all quoted lenders coming under pressure – rights issues followed with varying degrees of success and the

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<sup>17</sup> OECD (2005) *Recent role of house price developments: the role of fundamentals*, Chapter 3, OECD Economic Outlook, 78, OECD, Paris

<sup>18</sup> Wilcox, S and Williams, P (2010) *The emerging New Order?* Contemporary Issues 4, UK Housing Review 2009/10, Chartered Institute of Housing, Coventry. See also *Private Housing* in the same issue, Chapter 3

regulator became ever more involved. Mergers and takeovers became necessary to prevent collapse and the Bank of England brought in liquidity facilities to help buy up mortgage assets.<sup>19</sup>

85. As captured in the title often applied – the sub-prime crisis – mortgage lenders in the USA and the UK had been tempted to embark on very expansionary lending, giving access to home ownership to groups who had previously found it more difficult to borrow, e.g., the self-employed, people with a damaged credit histories and those with low deposits. This expansion in higher Loan to Value (LTV) lending as well as the use of interest only loans, alongside allowing self-certification of earnings proved to be very damaging. This was all rolled back in the downturn and through the subsequent regulator-led mortgage market review before being enshrined in new regulatory rules which effectively banned certain products and behaviours.

### **The Downturn: 2008–2009**

86. Prices and transactions slumped with a speed that exceeded the 1990-91 downturn as the market retreated. Possession cases began to rise, up 54% from 25,900 in 2007 to 40,000 in 2008. They peaked at 48,900 in 2009 (see Chart 19, Appendix 1). Negative equity returned albeit on a much lower scale than in the previous downturn (impacting around 1% of households compared to 15% then) but Standard and Poor forecast that by 2009 some 1.7 million borrowers could be in this position.<sup>20</sup> This prediction did not eventuate with an estimated 700,000 in Q1 2009 because of a substantial and wide-ranging programme of interventions by the Bank of England and by government.<sup>21 22</sup>

87. In brief this report notes the following actions:

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<sup>19</sup> Williams, P (2010) *Home Ownership – where now?* In Malpass, P and Rowlands, R, eds, *Housing, Markets and Policy*, Routledge, London

<sup>20</sup> Standard & Poor's RatingsDirect (2008) Risk Of Negative Equity For U.K. Mortgage Borrowers Returns, 30 July S&P

<sup>21</sup> Hellebrandt, Tomas, Kwar, Sandhya and Waldron, Matt (2009), *The economics and estimation of negative equity*, Available at: <https://www.bankofengland.co.uk/-/media/boe/files/quarterly-bulletin/2009/the-economics-and-estimation-of-negative-equity.pdf>

<sup>22</sup> Edmonds, T et al (2011), *The economic crisis -policy responses*, Standard Note SN/BT4968, 3<sup>rd</sup> June, House of Commons Library, London

- a. The Bank of England cut the base rate from 5.75% in July 2007 to 2% in December 2008 and by March 2009 it was at 0.5% (where it remained until 2016 when it dropped to 0.25%). It also introduced Quantitative Easing (QE), buying in bonds (including Residential Mortgage Backed Securities (RMBS)) from the market in line with similar interventions elsewhere. The QE programme was subsequently expanded significantly and it was only in 2022 that it began to be unwound. The impact of these rate cuts was significant in helping homeowners cope with the downturn.
- b. The government stepped forward with a substantial set of responses announced in the November 2008 Pre-Budget Report (HM Treasury, 2008). This included a commitment to supporting householders facing financial difficulties based on:
  - i) a new Lending Panel to improve monitoring of lending to households and businesses as well as to drive up best practice across the mortgage market and promote awareness of initiatives to support households against possession;
  - ii) help through a mortgage rescue scheme (*MRS*) and *Support for Mortgage Interest (SMI)* scheme for eligible homeowners in difficulty;
  - iii) a commitment from major mortgage lenders on the Panel not to initiate possession action within at least three months of an owner-occupier going into arrears; and
  - iv) free and impartial debt advice supported by increased Government funding.
- c. In addition, on 3 December 2008 a new *Homeowner Mortgage Support Scheme (HMS)* was announced to begin in early 2009 with detail provided in a Treasury Press Release on 10 December.<sup>23</sup> The scheme incentivised lenders to offer greater forbearance for longer periods to borrowers who faced temporary

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<sup>23</sup> HM Treasury (2008), *The Homeowner Mortgage Support Scheme*, National Archives, Available at: [https://webarchive.nationalarchives.gov.uk/ukgwa/20100202125457/http://www.hm-treasury.gov.uk/press\\_135\\_08.htm](https://webarchive.nationalarchives.gov.uk/ukgwa/20100202125457/http://www.hm-treasury.gov.uk/press_135_08.htm)

income difficulties and were not eligible for Support for Mortgage Interest. Payments could be reduced to 30% as a minimum and if in the end there was still default and possession the government guaranteed the lender 80% of the deferred interest losses.

88. To support new buyers *HomeBuy Direct* was introduced in January 2009. This was an up to 30% equity loan product on new build units co-funded by government and the developer. It was intended to support up to 10,000 lower income households over two years; in part by helping people obtain shared ownership mortgages; as well as to help developers. It was replaced by *First Buy* and ultimately by *Help to Buy*. It was part of a suite of policies including *Social Homebuy* which aimed to support shared ownership in different ways.

89. The government re-scheduled the *Affordable Housing Development Programme* to 2009 to enable new build to be brought forward. This had some limited short-term effect on housing association development, but the expected additional funding did not materialise under the new government, so output declined again after 2010.

90. There was considerable discussion about the role that housing associations might be able to play, as partners to developers or as developers themselves, in increasing housing output – notably in discussion between their trade body, the National Housing Federation and the Government. A significant number of associations saw this as an opportunity to cross-subsidise affordable housing provision from the profits to be made on market sale housing. While of little immediate impact, from around 2014 this new model helped support the expansion in housing association starts that occurred thereafter (though of course also making them more pro-cyclical).

## **Assessment**

91. The 2008-09 downturn was part of a Global Financial Crisis (GFC) with a coordinated response from governments and central banks around the world.

92. There were very substantial interventions in the finance market albeit with varying degrees of impact. In reality the most significant were the interest rate cuts by the



Bank of England and the financial support to the banks. In relation to the Department's initiatives it is worth highlighting the following:

1) *Homeowner Mortgage Support Scheme (HMS)*

93. *HMS* was devised by the Treasury but administered through UK Asset Resolution Ltd (UKAR as it is known, is owned by HM Treasury and is the vehicle into which nationalised mortgage assets were placed). In the end only 47 cases were admitted (and only in 1 case was there a claim on the guarantee).<sup>24</sup> An evaluation of the scheme conducted in 2010 observed that support for *HMS* remained muted amongst lenders and advisors as it was seen as overly burdensome. However, as the 2010 evaluation report noted it had wider benefits by prompting borrowers and lenders to find ways to avoid possession with over 30,000 borrowers entering into lenders' own concessionary schemes in the early years.<sup>25</sup> *HMS* itself closed at the end of 2010-11.

2) *Mortgage Rescue Scheme (MRS)*

94. This Departmental scheme became operational in early 2009 drawing upon the earlier 1990s rescue scheme. It was part of a £2 billion housing package announced by the Labour government in early September 2008. The two year scheme was funded to the tune of £205 million from the *National Affordable Homes Programme* with the aim of helping around 6,000 households. A further £80 million was added in April 2009 from the same budget and the Department allocated an additional £221 million in October 2010 to allow the scheme to run to spring 2013.

95. Eligible homeowners were offered one of three products, following assessment by their local authority:

- a. shared equity to help householders who have experienced payment shocks and needed some help in paying their mortgage;

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<sup>24</sup> Cromarty, H et al (2021) *Mortgage arrears and repossessions (England)*, House of Commons Library Report 04769, House of Commons, London

<sup>25</sup> Wilcox, S et al (2010) *Evaluation of the Mortgage Rescue Scheme and Homeowners Mortgage Support*, Interim Report, Communities and Local Government, London

- b. shared ownership to help those with a bigger financial gap but still able to make a contribution to monthly payments;
- c. sale and rent back (mortgage to rent) to help the most vulnerable on low incomes with little chance of sustaining a mortgage.

96. Eight lenders agreed to take part in the scheme: HBOS, Nationwide, Abbey, Lloyds TSB, Northern Rock, Barclays, RBS, and HSBC, while over 60 councils fast tracked its development so it was ready for 2009. Further provision was made to cover households' additional borrowing and homes in negative equity. A variety of complex legal issues were resolved including whether households were regarded as intentionally homeless by defaulting on payments.

97. As the interim evaluation makes clear the take-up of the shared equity option was very low – only 16 households being accepted in the first 15 months, compared to 613 becoming housing association tenants.

98. The National Audit Office's (NAO) full evaluation of the scheme in 2011 confirmed that total rescues were 2,600 – roughly half of the number planned – and 98.5% of these were mortgage to rent.<sup>26</sup> There were no shared ownership rescues and few shared equity ones, possibly suggesting that households simply did not have enough financial capacity to opt into them. Despite the lower take-up, the NAO report suggested that the scheme reduced the numbers of people presenting as homeless as a consequence of mortgage arrears and that some 16,000 households who contacted their local authority received various forms of aid and advice.

99. The NAO set out a range of lessons to be learned including drawing more thoroughly on existing evidence and data wherever possible and piloting schemes fully prior to implementation. If the latter was not possible due to time constraints, as was the case with *MRS*, it was suggested that the Department should identify the gaps in their knowledge, research specific target groups to test key

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<sup>26</sup> NAO (2011) *Department for Communities and Local Government: The Mortgage Rescue Scheme*, NAO, London

assumptions, subject its business cases, projects and programmes to independent scrutiny, and undertake sensitivity analyses in key business case submissions.

100. The Government also strengthened financial advice available to mortgagors, announcing a series of measures in May 2008. These included £9 million made available as additional funding for debt advice by third sector partners and a commitment to expand access to free legal representation at county courts throughout England for households at risk of possession; along with strengthening the National Housing Advice Service to provide a new comprehensive debt advice service. In addition, more specialist training was provided for Citizen Advice staff and local authorities on debt advice.
101. A Pre-Action Protocol on possessions was agreed with lenders and announced in late 2008. This set out clear standards that judges could expect lenders to meet in bringing possessions cases to the courts. It made clear that possessions should be a last resort and where possible lenders were expected to try to discuss and agree with borrowers an alternative to possession. Where the case came to court, lenders had to be able to set out how they had complied with the protocol. The then Financial Services Authority set out its requirements to ensure that borrowers in arrears and facing possession were treated fairly.
102. The Government also announced reforms to the system of financial support for mortgagors aimed at more accurately reflecting the value of people's property and reducing the waiting time before help from *Support for Mortgage Interest (SMI)* kicked in. The announcement stated that, as a temporary measure, the 39 week waiting period before help towards a mortgage is paid, would be cut to 13 weeks for all new claims from those receiving working age benefits. The measure came into effect from January 2009. In addition, also as a temporary measure from January 2009, the capital limit on loans upon which *SMI* is based was increased from £100,000 to £200,000 for the same groups. The reductions in the standard rate of interest used in *SMI* calculations and which were derived from market trends, were also deferred.
103. Again, what can be observed was action across a range of government departments in conjunction with mortgage lenders, regulators and the court

service. This spread of activity was powerful and in total quite effective. The upshot was that mortgage possessions fell away – although direct attribution to the specific initiatives is not always easy. From the peak of 48,900 in 2009 they dropped to 38,500 in the following year, then 37,300 in 2011 and 28,900 in 2013 before falling more rapidly over the next few years to 2,250 in 2021. It is also worth noting that over the period 2008 to 2013 some 227,500 households lost their homes via possession so, despite the interventions, numbers were still considerable.

### **Lessons to be learned?**

104. These are probably many and varied as might be expected given this was a financial market crash first and foremost, albeit crucially linked to the housing market and real estate assets. It raised major issues about the recognition and pricing of risk and the underlying financial strength of lenders' balance sheets and their capacity to cope with downturns. It has resulted in a complete reworking of financial regulation and oversight as well as in the structuring and management of lenders. Flowing from it there has been financial stress tests imposed on household borrowing capacity and the imposition of macro-prudential rules that put in place various lending limits. Taken together all of these have resulted in tighter controls over access to the mortgage market, which in turn has reduced access to home ownership.
105. In terms of the Department specifically there are a number of possible lessons;
- a. Policies aimed at boosting home ownership should now pay much closer attention to the underlying framework of mortgage regulation as this sets bounds around what can be done.
  - b. The suite of policies put into place in this downturn gives a real sense of how many levers exist outside direct housing policy interventions, e.g. the pre-action protocols mobilised through the court service had a significant impact, not just on those cases proceeding through the system but also on the practices and procedures of lenders with respect to borrowers in distress. The lesson here for the Department is to log these interventions and capture as far as possible their costs and benefits in order to ensure there is a government wide memory of these assessments. In terms of specific DLUHC schemes, the evaluations of

these suggests that the understandable desire to ensure the schemes were suitably structured and avoided unjustified subsidy and support resulted in them being administratively complex and burdensome which in turn may have limited take up.

- c. Given that the need for such schemes arises in the context of some form of crisis thus requiring development at speed, there may be a case for undertaking work on framing and developing potential responses in the “fallow” periods in the cycle. This report is a starting point for that process. However, the range of interventions across a wide spectrum of departments has meant it has not been possible here to do full justice to this matter. The NAO report referenced earlier provides important insights from which to learn.
- d. *Help to Buy* was very much built on the back of this downturn and with a number of objectives, including helping boost housing supply and builder capacity as well as helping households access home ownership. The Department sponsored two evaluations of the scheme and both recommended its closure – the first in 2017 – not because it was failing, but rather because it had done its job. The market had returned to some kind of normality and builders were capable of standing on their own feet. However, closing the scheme down has proved difficult in the face of pressures from participants to keep it going.<sup>27 28</sup> It therefore may have been helpful to have an agreed set of milestones, which when met would have triggered closure, agreed with the housebuilders from the outset. There may also be affordability concerns for some customers as they face higher than expected mortgage rates when their interest free loans run out.

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<sup>27</sup> HBF (2017). *HBR REPORT: STEPPING UP! An analysis of the Help to Buy Scheme to date*

<sup>28</sup> HBR (2018). *HBF REPORT – HtB 5 years on.*

## Broad lessons learned from previous downturns

### Comparing the downturns: a summary

106. Having explored lessons learned at the end of each downturn, this section now looks at these in the round. It is clear that each of the four downturns identified had different attributes and occurred in different economic environments, meaning causality has also been different. It is therefore important to examine the period before the downturn in each case as this helps to understand what factors changed to generate the downturn and enables us to ask what might have needed to change to reduce the negative impacts.
107. Three of the downturns are preceded by periods of boom in terms of house prices and levels of activity in the housing market. Falls in activity and indeed prices were therefore occurring from a level which was out of line with general trends. The exception is the downturn 1980–1982 which appears to be one element in a more general period of economic change and uncertainty.
108. It is reasonable to argue that the core causal factors at national level are to do with the macro-economy and specifically with respect to inflation, income growth and the associated interest rate changes. It is also true that because supply is inelastic, when demand changes the impact is concentrated on price. As such it is not surprising that most of the policy emphasis is on what the Treasury and the Bank of England have done in response to the boom and the downturn rather than on departmentally specific policies. The fundamentals of housing also mean that demand can adjust immediately while supply can adjust downwards quite quickly but it takes a long time to return to trend levels of output. Volatility thus results in supply being reduced into the longer term.
109. All four of the downturns were impacted by external factors. In the early 1970s the main external factor was the oil crisis; in the early 1980s there was a further oil crisis followed by both the Iran/Iraq and the Falklands wars; the 1990 downturn was at the time of the Kuwait war; while the source of the 2008 downturn lay in the Global Financial Crisis (GFC). The early 1990s downturn was particularly affected by the UK joining and then leaving the Exchange Rate Mechanism (ERM), with extremely negative impacts on our financial system as a whole and housing in

particular because of the high debt levels that had become more normal in the late 1980s. Deregulated housing systems were also at the core of many problems at the time of the GFC when again both large numbers of households were overindebted while lenders were overcommitted.

110. In terms of the UK political environment, the downturn in the early 1970s was associated with a change in government and significant changes in government policy with respect to restructuring the financing of social housing and mortgage lending. The downturn in the early 1980s took place at a time of significant change as the Thatcher government implemented both financial deregulation and tenure restructuring towards owner-occupation and away from local authority housing. The downturn in the early 1990s came after a period of over-rapid growth in demand, and adjustments to interest rates to join the ERM, which caused soaring mortgage rates, falling house prices and rises in negative equity, arrears and possessions. There was then the financial crisis caused by withdrawing from it ('Black Wednesday')– together with a government much weakened by these events. Finally, while the 2008 global financial crisis originated in the USA, the UK economy, its financial system and its housing market were all heavily impacted.

111. Overall, although the immediate reasons for each downturn differ from one another, the resultant changes in interest rates play the most obvious core role in both downturns and upturns and are also indicative of other problems. Housing itself is not generally a major cause of change, although it may be contributory (e.g. in the early 1990s when housing policy was one immediate determinant). It follows that the effects on housing are often not at the forefront of the policy measures introduced to tackle the more general downturn.

## **The Changing Housing Environment**

112. Over the fifty year period during which these downturns occurred the UK housing system has changed enormously. In the early 1970s the numbers of dwellings finally exceeded the number of households in all local authority areas and the household formation rate was seen as relatively constant. As a result, it was assumed that the housing shortage was under control – with consequently less emphasis on housing investment. Thereafter, however, particularly as

incomes grew and immigration rose, household formation increased and exceeded projections until well into the twenty first century – raising major concerns about inadequate housing output levels. Only in the last decade has the household formation rate declined, in part as a result of house price increases and the lack of housing supply, alongside very slow income growth. Current ONS household projections are very different from earlier decades and based more on migration than reductions in the size of households as fewer people chose to live separately.

113. Another factor which has been relevant to both demand and supply has been the growth in the higher and, to a lesser extent, further education system. This flowed from the Robbins Review in 1963 but was further expanded in the 1992 Act. The tradition of leaving home to attend university led to an expansion in purpose-built student housing provision generating a different strand of new build demand and a different investor led funding system – possibly helping to stabilise investment over the cycle.
114. A further change which impacts on the nature of housing market downturns has been in the mix of tenure in new homes being built. In the early 1970s it was roughly 50% social rented housing, 50% owner-occupation and near zero private renting. The housing associations began to be more relevant in the 1970s but had little impact until after 1988 when private finance was introduced. After the GFC, housing associations – with their potential to increase output levels and cross-subsidise social sector house building by developing market housing were seen as important ways out of any downturn in housing investment. It is much less clear that they have the potential to repeat that level of involvement now because they are far more indebted and have an increasing number of commitments to address related mainly to the existing stock, including with respect to net zero.
115. A core change in mix has been the growth in the private rented sector (PRS), starting from the introduction of Assured Shorthold Tenancies in 1978. This, together with the introduction of Buy to Let mortgages in the late 1990s helped better off households (usually existing owner-occupiers) to invest in privately rented accommodation. Buy to Let now makes up over 10% of gross annual mortgage lending and it has proved to be a stable and secure mortgage market up to now. On the other hand, the growth of housing as a readily marketable asset



has increased levels of debt and with it the possibility of strong systemic risks as international finance markets come under pressure.

116. From being a residual sector in decline prior to 1978 the PRS now houses not far short of one in five households in England – and nearer 30% in London – with the proportion of those living in the privately rented sector more than doubling since the turn of the century. Importantly large numbers of Right to Buy properties are also now located in the sector.<sup>29</sup> The recovery in demand for private rented housing together with readily available finance has led to the development of a significant and growing Build to Rent market mainly serving middle/higher income households. This segment of the market may be affected by different pressures than those affecting development for owner-occupation.

117. There is already some limited evidence that growth in private renting may be slowing or declining, with the proportion of households in the PRS falling from 20% in 2016-17 to 19% for the past five years. Concerns have been raised by landlords around the changes in taxation which make investment in the PRS less tax efficient for individual owners, itself a consequence of the government wishing to rebalance the market in favour of first-time buyers<sup>30</sup>. There are current suggestions that the expansion of the Buy to Let market may have peaked and that there is now a shortage of rental properties coming on the market, in turn leading to rapid rent rises, while house prices stabilise or fall<sup>31</sup>. At the present time the number of individual landlords is thought to be declining, while the numbers of company landlords is showing quite rapid growth. It is probable that, at least in part, the first group are selling to the second or buying additional units as companies, so the net effect is, as yet, unclear.

118. Moreover, it is worth noting how Buy to Let investment decisions are linked to wider issues of other asset values and investment in general. Weaker stock markets and lower savings rates made decisions to invest in property fairly

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<sup>29</sup> Murie, A (2022), *Right to Buy: the long view of a key aspect of UK housing Policy*, UK Housing Review, Chartered Institute of Housing, Coventry

<sup>30</sup> Scanlon, K Whitehead, C and Blanc, F (2021a). *Private Landlords and Taxation*, LSE London, London.

<sup>31</sup> Savills and LSE (2023) Supply of Private Rented Sector Accommodation in London, London Councils, London.

straightforward, not least given their historically strongly favourable tax treatment. As that context has changed and the tax treatment has been modified to make it less attractive, the view on Buy to Let has shifted. Interest only mortgages which are typically used are particularly costly in the current rising rate environment. Taken together with the ageing of that population of baby boomers who are now seeking to reduce or liquidate assets it is little wonder some re-adjustment is underway. At the same time some new younger households have been stepping into this market reflecting how young singles have bought flats which may be retained as a Buy to Let home as they move up the housing ladder. Importantly there is a lack of adequate data to understand the current dynamics of this market.

### **Changing Financial Regulation**

119. In the 1970s the mortgage market was very restricted, as reflected in the queues and rationing that were in place. Single people and particularly women were typically unable to obtain mortgages. Because the building societies requirements were strict there was less evidence of mortgagor problems as a result of a downturn. Over the years the availability of mortgages improved and became more market driven at the same time as the lenders' assessment of risk became more "liberal". The risks of potential negative impacts in a downturn therefore increased, resulting in stretched affordability and sometimes worsening arrears and possessions. This was observable to a limited degree in the 1980s but especially in the early 1990s when large numbers of households having entered the market fell quickly into negative equity. Arrears and possessions followed basically the same pattern in the downturns suggesting that intervention aimed at limiting possessions, was not as successful as was expected. The more comprehensive arrangements used during the GFC and COVID-19 pandemic appeared to work better – even if at some significantly greater cost. Whether they can be further improved in any prospective downturn is an important issue.

120. The other major change has been the shift away from variable to fixed rate mortgages which helps protect existing mortgagors from rising rates for the life of the fix. However, these are generally for short periods by international standards. Moreover, the capacity to borrow more and add to indebtedness has increased

over the years so exposure to risk can last much longer. If house prices were to fall significantly in money terms, negative equity might also re-emerge.

121. After the 2008 crisis the ensuing financial problems were managed both by government intervention and an agreement from mortgage providers to address the problems faced by their borrowers directly – which, with insurance, was intended to remain in place into the longer term. However, the attempts to expand mortgage protection insurance had little impact and the government's backstop support for mortgage interest has been significantly reduced. In the context of rising rates of interest and possibly falling capacity to service debt there may be concerns about the ability of some mortgagors to maintain repayments.

122. On the one hand there are far higher proportions of borrowers than in the earlier downturns who are long established existing owners and are protected by past house prices rises and shrinking debt. Taking this together with the limitations on interest only mortgages post the GFC, there may be fewer households at risk suggesting that the system itself may be more resilient than in earlier downturns. On the other hand, because we are starting from very low interest rates, the impact on repayments of even a 1% increase is significantly more than in the past.

123. The rise of outright ownership is also important here. The ONS estimates for England in 2020 are instructive. There were 15.6 million owner occupied homes. Of these 8.8 million were owned outright – some 56% compared to 6.8 million with a mortgage (44%). With lower entry rates into home ownership and increased longevity in the population this trend will continue and further evaluation may be needed not just with respect to potential downturns but also in terms of its impact upon the mix of tenures and the overall functioning of the housing market.

### **Affordability**

124. As already noted, in the 1970s and given the controlled flow of mortgages, most households purchasing their homes had secure incomes which allowed them to cope with changing interest rates so there were very few arrears and defaults until the 1980s. Thereafter indebtedness has grown and the potential for arrears and possessions is significantly greater.

125. Affordability measured by the ratio of house prices to incomes remained relatively stable through the 1970s, 1980s and 1990s except for short term over-valuations in the run up to the 1973 and 1990 recessions and a period of under-valuations as the housing market recovered from the 1990 crisis (see Meen and Whitehead (2020), Table 2.2). However, since 2000 the ratio has been significantly above the trend especially after the 2008-09 crisis. This is mainly an outcome of the very low interest rate environment which has allowed higher borrowing and in turn has been capitalised into house prices. The affordability ratio can be expected to reverse in the face of higher interest rates, but probably not enough to solve the affordability problems which have worsened particularly during and after the pandemic.
126. It is worth noting that the trend of reduced affordability has been observed in many OECD countries although not universally. The USA, Germany and Japan have all experienced long-term declines since the 1980s.

## **Housing Output**

127. In the first three recessions detailed here private housing starts fell from their peak before the economy went into recession and in the first two started to rise again even before the recession was fully in place. In each upturn from 1980 private starts reached a lower output level before they started to fall again. Starts still had not recovered to 2007 levels in 2021 after a further downturn in 2015 – and are now falling again.
128. Local authority starts fell before the early 1970s recession but rose during the recession itself before falling consistently until the 1990s. Housing association starts also rose from very low levels during the early 1970s recession but fell immediately afterwards. From 1988 when private finance was brought in, housing association output rose rapidly until the end of the 1990s recession and then fell until the turn of the century. Thereafter they rose again until 2008 then stabilised and, after a fall at the beginning of the 2010s, rose again.
129. Overall, there are few signs of any strong social housing countercyclical behaviour after the early 1970s although the *Housing Market Package* in the early 1990s did see housing association output double to around 41,600 starts in 1993

for a short time. What is clear is that once output levels start to fall the time taken to get back to something like normality is slow and extended as compared to the movement of house prices, while the capacity of the social housing sector to offset housing market declines has generally been limited.

# Policy Approaches

## Departmental Policies

130. It was only in the 1970s that the Department had direct powers to intervene in the housing finance market enabling them to manage the flow of funds to some degree, including at one point the capacity to supplement building society funds for a short period. Since the mortgage market was opened up in the 1980s the Department has had no direct policy involvement. They can and do of course interact with both the Treasury and the Bank of England clarifying the costs and benefits to housing of proposed wider policy changes. However, it is always clear that housing issues cannot drive such policy but must rather respond to macro-economic pressures.
131. Similarly, it was only in the 1970s that the Department had control around rent rebates and allowances. These were introduced in the early 1970s first for social housing and then for the private rented sector. One important objective of the introduction of income related benefits was to shift the emphasis from bricks and mortar subsidies to demand side subsidies where policy is generally determined by the Department for Work and Pensions within the budget set by Treasury.
132. The Department's own housing policy levers relate mainly to planning, affordable housing, improvement of new and existing stock (including increasingly energy efficiency), and regeneration. These powers are generally about the allocation between geographical areas and between types of activity. As was noted in the *Evaluation of Housing Policy 1975 – 2000*, these policy areas have not generally been seen as mechanisms for counter cyclical investment. There have been some counter cyclical measures including the *Housing Market Package* in 1990-91 which provided help to developers by buying up unsold properties. In 2008-09 funding under the National Affordable Housing Programme was moved forward so that output might be enhanced but this did not generate significant increases in output because additional funds were not made available as expected. Indeed, there was significant decline in output as funds were cut back. The overall availability of subsidy is anyway determined by the Treasury.

133. As already noted, initiated in 2013 *Help to Buy (HTB)* was a massive extension of the ideas tried under the previous *Homebuy Direct* and *Key Worker* schemes. It involved an equity loan which, while free in the short term, involved both paying interest after five years and returning to government the relevant proportion of the capital gains derived from the property. *HTB* has been generating a good rate of return for the government (a rate well above 10%) although this could change if prices fall significantly. There are also concerns that purchasers may run into financial difficulties as they begin to pay higher than expected interest rates on their equity loan. There is continuing uncertainty about the impact of *HTB* on new build although the evaluations sponsored by the Department showed considerable additionality. The scheme finished in March this year (except for self-build and armed forces *HTB*). An alternative approach may need to be considered.
134. As part of the *HTB* suite the government also launched a mortgage guarantee scheme in response to the decline in the availability of high Loan to Value (LTV) products, following the 2008 financial crisis. It ran from 2013 to 2016 and the scheme was a success in that the number of products available at 95% LTV increased from October 2013 to June 2017 from 43 to 2,611. The scheme also directly helped over 100,000 households to buy their own home across the United Kingdom.<sup>32</sup> The scheme was relaunched in 2021 as a mirror of the earlier scheme with the aim of invigorating the higher LTV market post the COVID-19 pandemic. It has recently been extended to 2025. The earlier scheme had to charge lenders a fee to participate, to avoid EU state aid rules. That pressure is no longer there but a fee continues to be charge. Unfortunately, there continue to be major difficulties around the capital relief which might be enjoyed by lenders who participate in such guarantee schemes. In almost all cases participation in the guarantee scheme has not given lenders any relief from the capital weighting rules under Basel III despite the offset in risk – something which may need considering if guarantee schemes are to become a feature of the lending landscape.

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<sup>32</sup> HM Treasury (2021), *The mortgage guarantee scheme: outline*, Available at: [https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment\\_data/file/965665/210301\\_Budget\\_Supplementary\\_Doc\\_-\\_mortgage\\_guarantee\\_scheme.pdf](https://assets.publishing.service.gov.uk/government/uploads/system/uploads/attachment_data/file/965665/210301_Budget_Supplementary_Doc_-_mortgage_guarantee_scheme.pdf)

135. *Gap Funding* was also a policy available to the Department for about 20 years before the turn of the century and appears to have been helpful to developers and to housing output during the second two downturns.<sup>33</sup> It was ruled out of court by the EU at the turn of the century but replaced by a less generous scheme in 2007. It appears not to have been popular with the private sector, perhaps because they thought it was too targeted. If appropriate gaps can be identified, it could be of use in the current environment.
136. The introduction of S106 in 1990 which enabled local authorities to negotiate a proportion of affordable housing in larger developments and, later, the Community Infrastructure Levy brought significant funding into the housing system mainly for additional affordable housing both rented and owned. However, the available funding is directly related to levels of private sector building rates and so, if anything, reinforces market cycles.
137. The Department's direct involvement in housing supply currently comes in the form of the *Affordable Homes Programme 2021–2026* which aimed to produce 180,000 new homes managed through Homes England and the Greater London Authority (GLA). Much of this core element of the programme involving strategic partners has already been put in place. However, there must be major concerns about the capacity to deliver, given interest rate and construction cost increases and the many other pressures facing housing associations and local authorities. It would need considerable additional government funding to generate significant counter-cyclical investment were a full-scale downturn to eventuate.
138. Another area of concern lies with the planning system reforms and the extent that this may slow down permissions and delivery. Early this year it has become clear that many local authorities, mainly in the South East, have withdrawn their local plans with the intention of reducing planned numbers based on local conditions now that the local housing targets are only advisory.

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<sup>33</sup> Parliament (2000), *The Implications of the European Commission Ruling on Gap Funding Schemes for Urban Regeneration in England*. Available at, Available at <https://publications.parliament.uk/pa/cm199900/cmselect/cmenvtra/714/71406.htm>



139. Again, some 40 (maybe more) local authorities have been warned by Natural England about 'nutrient neutrality' requirements which if not met means that planning permissions cannot be built out.

### **Government Policy more generally**

140. Financial policy is mainly within the remit of the Treasury and is at the centre of measures to respond to any downturn. This may involve funding which is allocated to the Department to support housing initiatives as well as tax changes such as Stamp Duty. The Department does of course advise on relevant matters. However, it also means that the Department's financial powers are generally limited to the allocation of their own budget mainly for housing investment, which may include additional funding allocated to them by Treasury in response to each crisis.

141. *Help to Buy* introduced in 2013 aimed to address the slow recovery of new build activity (and builder balance sheets) and the housing market in general by providing a subsidised equity loan to both first time buyers and existing owners. It was restricted to first time buyers from 2021 and is to be phased out in March 2023. Two evaluations were undertaken for the Department.<sup>34</sup> The first suggested that it had had a significant positive impact on housing output in the early years, but that support was probably unnecessary after 2016. A more econometric based analysis suggested that *Help to Buy* had put significant pressures on house prices, particularly near London.<sup>35</sup> The House of Lords Select Committee Report in November 2022 reinforced that view.<sup>36</sup> However, individual transactions data show that price rises were not concentrated in the *Help to Buy* units themselves but often further up the price range.

142. One reason for introducing *Help to Buy* was that major developers needed to borrow to build. Since then, the major builders have been able to increase their equity significantly, so are not dependent on borrowing. As such, an equivalent

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<sup>34</sup> Finlay, S et al (2016) *Evaluation of the Help to Buy Equity Loan scheme*; Whitehead, C. et al. (2018) *Evaluation of the Help to Buy Equity Loan scheme*, Ministry of Housing Communities and Local Government.

<sup>35</sup> Carozzi, F Hilber, C. and Yu, X (2020) *On the Economic Impacts of Mortgage Credit Expansion Policies: Evidence from Help to Buy*, CEP Discussion Paper No 1681

<sup>36</sup> House of Lords Built Environment Committee (2022) *Meeting Housing Demand*, First report of Session 2021-22, Parliament

scheme purely aimed at increasing developer cash flows as well as demand may not be as immediately relevant in the current context.

143. Since the removal of *MIRAS* mortgagors pay market rates without general subsidy. It may be appropriate to assess whether there are particular groups (such as first time buyers and shared owners) who could usefully benefit from some limited assistance.

144. One tax directed at housing transactions is *Stamp Duty Land Tax*. The first major stamp duty holiday was between December 1991 and August 1992 when the Chancellor increased the threshold from £30,000 to £250,000 in light of the economic recession. Since the turn of the century adjustments to stamp duty have become a more frequently used policy tool as opposed to simply a means of raising money. In 2008 the threshold was raised from £125,000 to £175,000 to support transactions in the face of the Global Financial Crisis (GFC) and in 2010 three rates replaced the single rate making transactions more expensive for dwellings sold for over £1m. The big structural change from slab to slice was introduced in 2014, making it more consistent with other forms of progressive taxation and in 2016 an additional 3% was added to the duty on second home transactions. To offset some negative effects, a higher threshold for first time buyers was put in place in 2017. The biggest changes came in 2020 in response to the COVID-19 pandemic with the threshold raised to £500,000 for nine months, extended to a year in July 2020. This may have led to additional purchases and boosted the economy in general but as before it also fed into significantly increased house prices. The reality of stamp duty holidays is that the benefits are ultimately capitalised into prices which over time negate the value of the intervention.<sup>37</sup> <sup>38</sup> <sup>39</sup> The gainers are the early purchasers plus all existing owners.

145. Another area where the Department has little direct say is with respect to monetary policy and financial regulation. It is the Bank of England that determines both interest rates and, via the Prudential Regulation Authority and the Financial Conduct Authority (FCA), the rules that are applied to mortgage lenders and

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<sup>37</sup> Centre for Cities (2020). *Who will be affected by cuts to stamp duty?*

<sup>38</sup> Ball (2021). COVID stamp duty holiday reveals big problems in the housing market.

<sup>39</sup> Scanlon et al (2021). *Lessons from the stamp duty holiday*.

borrowers. Interest rate changes have been a – possibly the – major factor in all four upturns and downturns but, while the impact on housing is recognised, wider macro-economic objectives inevitably dominate, as is enshrined in the Bank’s objectives. The introduction of stress tests for both providers and borrowers in the low interest environment of the last few years was intended to ensure that both are not too overstretched in the face of rising interest rates and have been a valuable tool in restricting over-borrowing. However, they have been diluted to some degree over the last couple of years. Up to now the regulatory policy put in place post the GFC has not been fully tested but it will be of growing importance as fixed interest loans fall due for renegotiation in a rising interest rate environment.

146. The Department for Work and Pensions (DWP) also has a significant role to play with respect to *Support for Mortgage Interest (SMI)* as it is only accessible for households eligible for certain welfare benefits. As it is now a loan, any household looking to claim *SMI* must take account of the need to pay it back with interest. Again, this policy may, as in the past, be more useful because people who apply receive advice not least about how to approach the mortgage lender regarding forbearance. Given it is now a loan, there should be room for more flexibility as to when it might be called upon. Indeed, it has often been suggested that it could be used as a more direct way of stimulating home ownership, though of course DWP would find this more difficult to support. More generally the freezing of Local Housing Allowance is putting additional pressure on lower income tenants and their landlords and putting off their capacity to service Buy to Let mortgages.

147. The Ministry of Justice’s potential role has been clearly evidenced with respect to the 2008-09 downturn and during the COVID-19 pandemic. The use of protocols and the courts embargo on evictions was quite powerful in stopping the flow of cases – and forced lenders and many landlords into serious forbearance albeit in a low interest rate environment. The approach seems to have been generally accepted as a short-term necessity, although the unintended consequences of increased backlogs are only now being addressed.

148. The make-up of a downturn, with transactions and prices falling rapidly; fewer first time buyers; followed more slowly by declines in housing output; and recovery especially with respect to housing investment taking much longer than the

downturn itself are well understood. In addition, it is now recognised that the negative impact of general cost of living pressures are being made worse by increases in mortgage costs and continuing rent increases. There is potential for negative housing outcomes including arrears, possessions and negative equity to become more common because of the greater openness of the housing finance system. There is also a growing problem of homelessness as tenants find it more difficult to pay their increasing rents.

149. However, possessions have been better managed during the last two downturns and the imposition of financial stress tests on both lenders and borrowers and lessons learned about forbearance should hopefully partially offset the impact of the reduction in the formal safety net. In the rental sector however regular government statistics show evictions and homelessness rising in London in the face of worsening affordability with concerns growing across local authorities. Given the depth of the cost of living crisis and frozen Local Housing Allowances, without intervention evictions and homelessness may become more likely.

## **The Emerging Downturn: why it might be different and what might be done about it?**

150. The emerging economic downturn does not yet technically meet the criteria for a recession although it is possibly still expected to do so this year. Quarterly growth was negative in November but marginally positive in December and higher in January. The housing market according to the Nationwide House Price Index has seen a seven month fall in monthly house prices from their peak in August 2022, before stabilising in April with a 0.5% monthly increase. Annual house price growth is now negative. The latest projections from the Office for Budget Responsibility in March suggest a 10% peak to trough fall (2022-2024), but with house prices rising again by 2025.
151. Housing starts dropped by 19% in the third quarter of 2022, but this was partly offsetting the rise in starts in the previous quarter which were made to avoid upcoming Building Regulatory change in energy efficiency requirements coming into force in June 2022. Private sector forecasts made after the mini budget in late September 2022 suggested that housing output might fall by 40% in 2023 although these projections are now seen to be overly pessimistic.
152. As previously discussed, it is important to look at the period before the downturn which shows that housing starts peaked in 2018 and were thus falling before the COVID-19 pandemic started. However, against predictions (across the world), by 2022 prices were higher than in 2018, suggesting the pandemic had in housing terms been a relatively short-term event with costs borne more by government than individual households. On the whole, these and other data now available suggest that the market was relatively buoyant prior to the mini budget in September 2022.
153. The major concerns expressed over the last few months have been mainly around interest rate rises and the resultant increases in the cost of mortgages. These will impact on repayment capacity and therefore reduce demand from new entrants and those who might have been looking to trade-up. They are also likely to generate growing arrears both because of the worsening cost of living and the large numbers of households and landlords whose fixed interest rate mortgage have already or will shortly have to be renegotiated (1.4 million loans in 2023).

154. Looking at the four earlier downturns, all saw significant house price falls in real terms. There seems very little reason to doubt that there will be real term falls in house prices in 2023, especially as there have already been two such falls since 2011 and house prices have been falling in real terms over the last year.
155. The early 1990s recession led to major changes in the mortgage market, integrating it more fully into the wider finance system. Changes included the use and development of mortgage securitisation and disintermediation via the growth of mortgage intermediaries. The *Buy to Let* mortgage product, introduced in 1996 also changed lenders portfolios and boosted residential property investment as an asset class.
156. A 'golden decade' (10 years plus) running up to the Global Financial Crisis (GFC) saw fresh innovation and competition in the mortgage market with housing and mortgage markets far more exposed to risk and thus less able to withstand the effects of the GFC. It also saw more international finance come into the market something which expanded greatly after the GFC under Quantitative Easing (QE) as housing was treated more as a tradable asset.
157. Post GFC the introduction of QE slashed interest rates and by late 2009 house prices were once again increasing. Although there has been some volatility, even during the COVID-19 pandemic they have continued on an upward trend.
158. Post GFC, as noted above, a host of regulatory measures were introduced to ensure more prudent mortgage lending, mandate forbearance, etc. In principle, this should mean that the fall-out from any economic bad news should be limited. The possible downturn over the next couple of years will impact mainly on households who face higher variable and fixed rate mortgage charges and/or have increased mortgage debt. Some potential purchasers, notably would-be first time buyers, will be unable to enter the market. Others will put off buying (and selling) because of uncertainties. As in other downturns, transactions will decline and only pick up slowly as the economy improves.
159. What appears very different from earlier downturns however is that there is less likely to be an unemployment crisis, although there will be significant declines in

real incomes (at least for some time). Forbearance policies are therefore of particular importance.

160. While some forecasts have pointed to the possibility of large falls in house prices both nominal and real, most of the more formal projections suggest more limited reductions of around 10% in nominal terms in part because of people holding off from the market. So, although some negative equity is forecast it can be expected to be relatively limited. Declines in house prices could, in principle, also make housing more affordable to some of those who have previously been excluded from the market.
161. One big concern in comparison to the last two downturns as already noted is that the borrower safety net is now in the form of a loan and limited to those who are out of work or of State Pension age and get income support through income-based Jobseeker's Allowance or income-related Employment and Support Allowance. Mortgage lenders forbearance policies are now enshrined in regulations and recently strengthened by the new Consumer Duty being put in place by the Financial Conduct Authority. But while lenders have significantly strengthened their risk managements processes and procedures they are likely to have reduced their Arrears and Possessions teams. This could become an important issue if the recession gathers momentum and drives up the case load.
162. The state of the privately rented sector is an increasing area of concern. Rents have been rising significantly lately especially in London but, despite this, there has been some evidence of landlords leaving the market.<sup>40</sup> Some landlords will undoubtedly face financial difficulties as will many tenants.
163. The other big concern at the present time is the effect on new build levels, exacerbated by the shortage of skills and the massively increasing costs of construction materials. This may also be made worse by changes proposed in the National Planning Policy Framework reforms, which are making targets advisory and the delays that inevitably follow from the many changes envisaged. While major developers have more of their own equity available than in earlier downturns, especially compared to 2008/09, they may well be more risk averse given the more

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<sup>40</sup> Cabot (2023). *Why are landlords leaving the rental market?*

negative economic environment around construction. In addition, they are being required to use their funding to address issues such as cladding and fire safety so, like housing associations, they may be less able to finance new development. Smaller developers are particularly impacted by rising costs of funding and it is now suggested that they, as well as larger developers will also have to pay for cladding removal. Leasehold issues add to the risks. The *Deposit Unlock* scheme, the builder led replacement for *Help to Buy (HTB)*, introduced in 2021, is making progress though so far has clearly less impact than its HTB predecessor.

164. Looking to the potential upturn, the most obvious concern is that this is the first period since before the GFC that interest rates have been increasing and may well continue to do so. It is not yet known how generations who have grown up with only falling rates of interest will respond to both rising rates and much higher rates than they were used to. Rising mortgage costs and falling real wages along with the worsening cost of living and possible tax rises looks a tough ask for households and there is bound to be some adjustment. These concerns point to a very slow recovery both in terms of the housing market overall and new supply in particular. But when the recovery comes, as always, the most likely outcome is that demand will increase more rapidly than supply, leading to upward pressure on prices, despite the higher mortgage rates. Uncertainty is also likely to generate continuing volatility in prices and supply, further slowing investment.

### **What Might be Done About It?**

165. The Bank of England now gives more attention to the impact of their decisions on sectors such as housing. But it will always be the case that ultimately macro-economic concerns dominate.
166. While the evidence suggests that supporting additional housing investment in downturns, notably in affordable housing, would be highly desirable, new initiatives need to be carefully designed to ensure that the effect on house prices and other factors is limited.
167. Both lenders and large developers are better capitalised than in earlier downturns so they should be in a better position to respond to any increase in demand.



168. While short-term interventions in the housing market may be needed to respond to immediate challenges, typically they are not the answer in the housing market. For example, reducing stamp duty has short-term demand boosting effects but ultimately any benefits must be measured against the cost in terms of foregone tax revenue and pushing up prices over the longer term (Scanlon et al, 2021). A more coherent and forward-looking approach to policy is required, built around an understanding of what levers are most effective in both the short and long term and in relation to specified problems.

### **Possible initiatives**

169. More thought needs to be given to how market segments interact, e.g., home ownership and private renting, first time buyers and last time sellers. Taking a more coherent view of the market and thinking about how a policy might have more than a single outcome is important as the Department already knows and practices. The issue here is extending that thinking into the upturn and the downturn scenarios.

170. The same applies to having a more segmented analysis of policy around different household groups, e.g., single people, families, young professionals, as well as a fuller grasp of changing contexts, e.g., the bank of Mum and Dad has supported up to 50% of first time buyer purchases – that capacity might reduce during any downturn as donor households limit their use of assets and finance. Exploring how offsetting such loans against inheritance tax liabilities could be one way of giving this market renewed capacity. The reality is that with increasing levels of outright ownership, there may be the option for that accumulated wealth to be more fully exploited.

171. One possible route for Government to help stimulate market activity and maintain liquidity would be to facilitate trading down by older households, especially if this can be sold as a Net Zero initiative rather than simply giving more handouts to older homeowners. Helping older households adjust their housing consumption could help ensure a better use of the existing housing stock and take some pressure off new housing supply.

172. A politically difficult initiative would be to reform council tax so that it better reflects actual house values. This would provide an incentive to downsize within

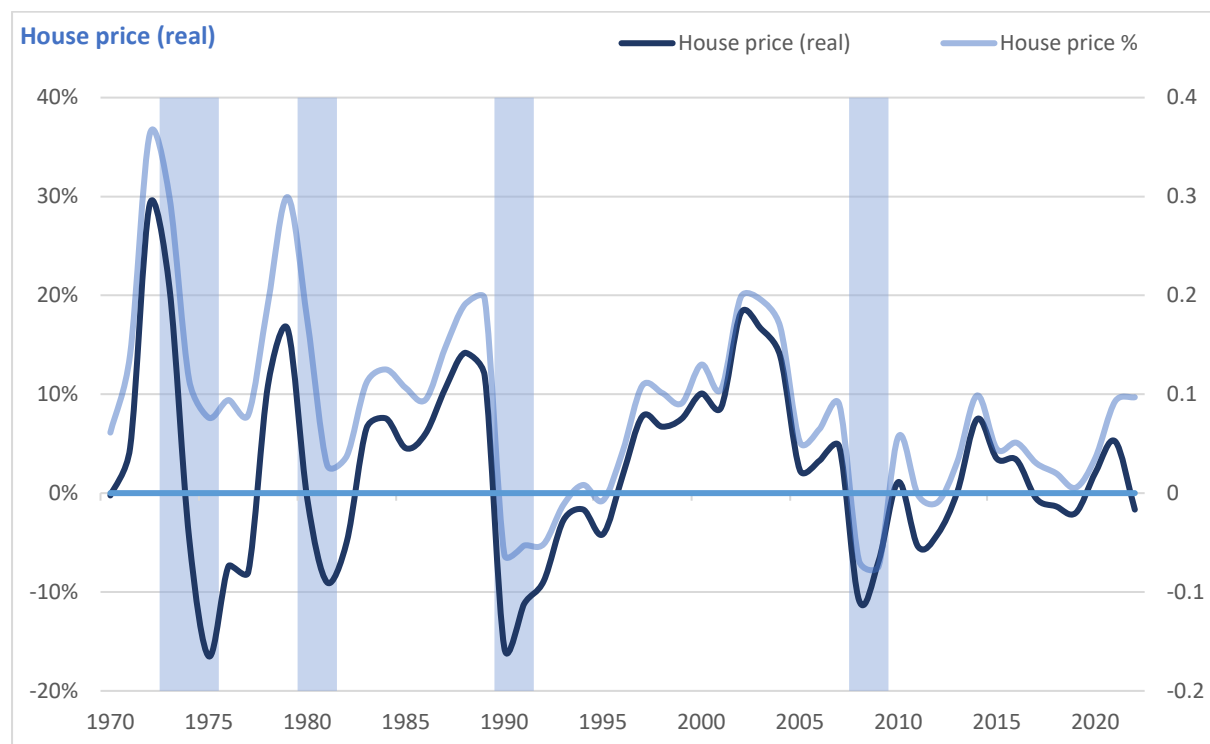
the existing housing market; slower rises or even falls in house prices, increased affordability as well as providing necessary funding to local authorities e.g. to support affordable housing.

173. Planning ahead for market cycles and notably both market upturns and subsequent downturns would be sensible. More consideration should be given on how to dampen volatility in the market in both directions. Increasing supply as a solution to house price volatility is dependent on the housebuilders increasing build out, and the levels of supply that would be needed to dampen price volatility is high.
174. Building a “playlist” of possible remedial moves in the event of a downturn could be held as a standard protocol in the Department, rehearsed periodically with other departments and relevant entities outside Whitehall.
175. This would require periodic “look aheads” on the economic cycle and reflection of the potential capacity constraints/possibilities for market players whether as providers of homes or finance or more. The Department for Levelling Up, Housing and Communities should probably be part of the Bank of England Residential Property forum if it is not already. There is also a case for the Department to set up its own periodic roundtables to review key indicators and possible actions. Such entities have existed in the past and been terminated but that action has been taken without the stronger sense of “eyes” through the cycle that is set out here.
176. It would also be desirable to undertake more formal independent research on the relationship between the different elements of the housing finance system (which has been through so many changes) and their impact on housing investment and demand. Current evaluations are often over-mechanistic rather than addressing interactions.
177. Part of the task of the government is to give confidence to investors with long time horizons who are without doubt keen to invest in residential real estate. These investors bring extra capacity to the market and potentially reduce the need for government grant in downturns. As has been seen in the last few years, pension funds and other long-term investors have begun to consider investing in social housing in general and shared ownership in particular. Without doubt this market

will expand but the Department might wish to consider how it could help frame that expansion by engaging in a dialogue with potential investors and borrowers.

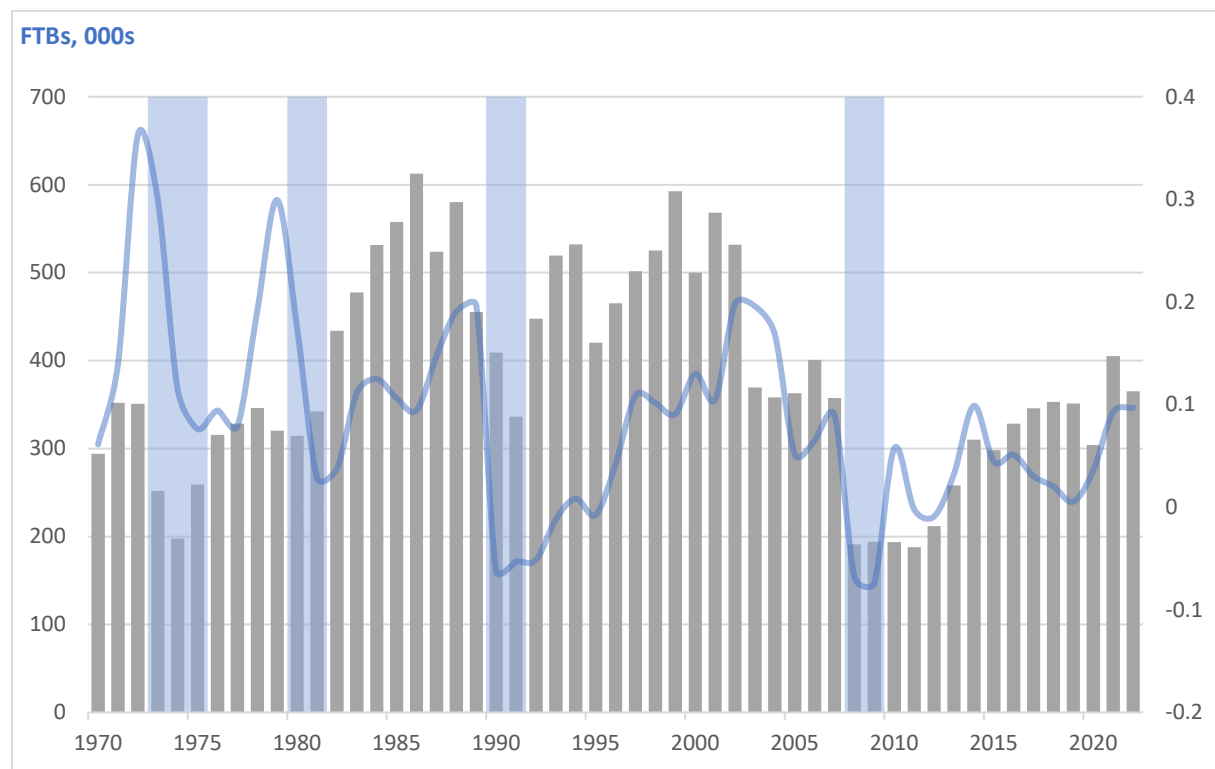
## Appendix 1: Housing market and wider economy charts

Chart 1: House prices real and nominal



Source: UK house prices since 1952, Nationwide Building Society. Author estimate based on House price % change less RPI % change.

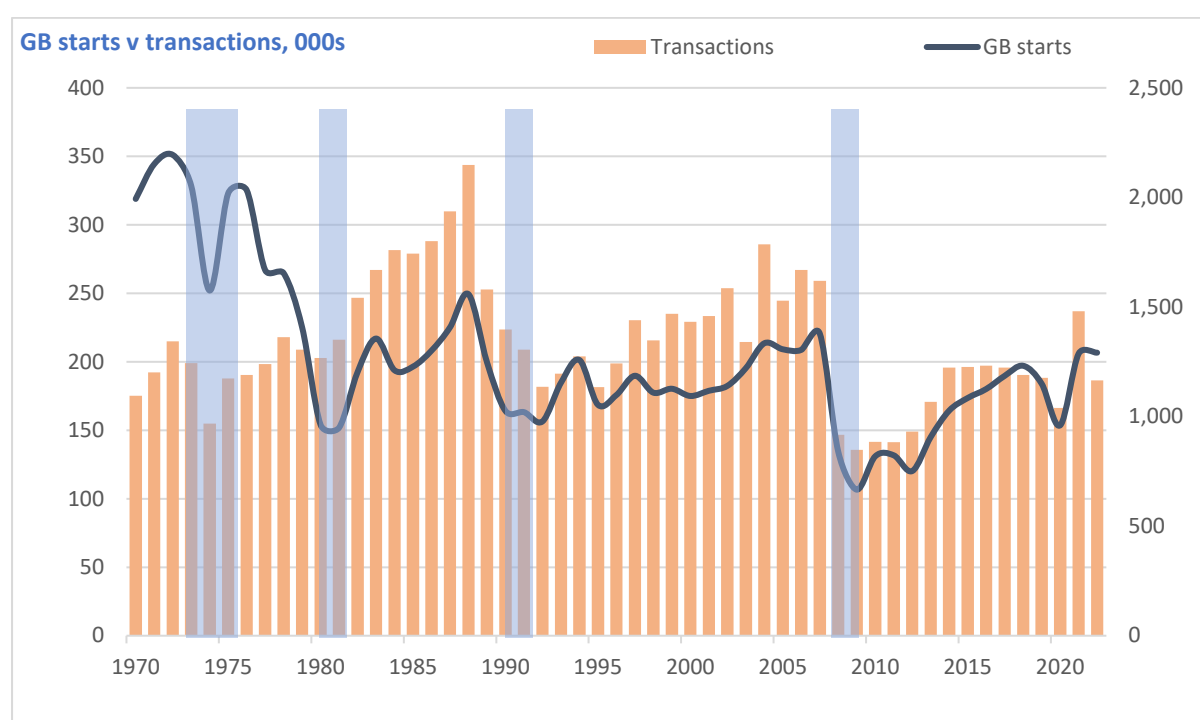
**Chart 2: First time buyers**



Source: UK Finance/Council of Mortgage Lenders. Author estimates for 1970-1973 and for 1978, based on figures from Table D3 of the Compendium of Housing Finance Statistics (CML). 2022 figures are estimates based on data to Q3.

UK house prices since 1952, Nationwide Building Society.

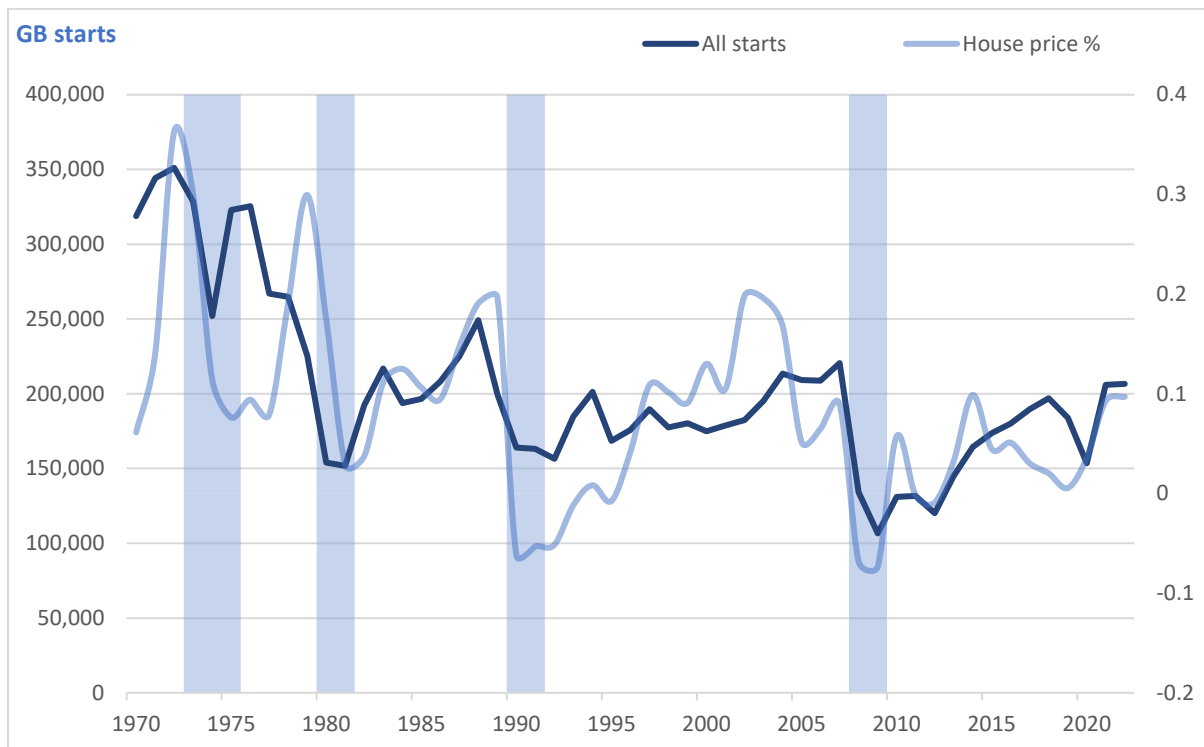
**Chart 3: GB starts v Property Transactions**



Source: Table A2 of the Compendium of Housing Finance Statistics (CML) (1970-77), Office for National Statistics (1978 onwards). Figures relate to GB in all cases. For Wales, author estimates made to derive breakdown of starts by sector from 2011 onwards and total quarterly starts Q2 2020 - Q1 2022 inclusive. For Scotland, author estimates to derive private starts and completions for Q2 2022. Figures for 2022 relate to year ended mid-2022.

Board of Inland Revenue (to 1995); HMRC (1996 onwards). Author estimate, based on particulars delivered (PD) figures from Table B1 of the Compendium of Housing Finance Statistics (CML) and Table 39a of the UK Housing Review 2018, spliced with HMRC property transactions data for more recent periods. Although the PDs data relates to England & Wales, it also included non-residential transactions and was historically used as a proxy for UK residential activity.

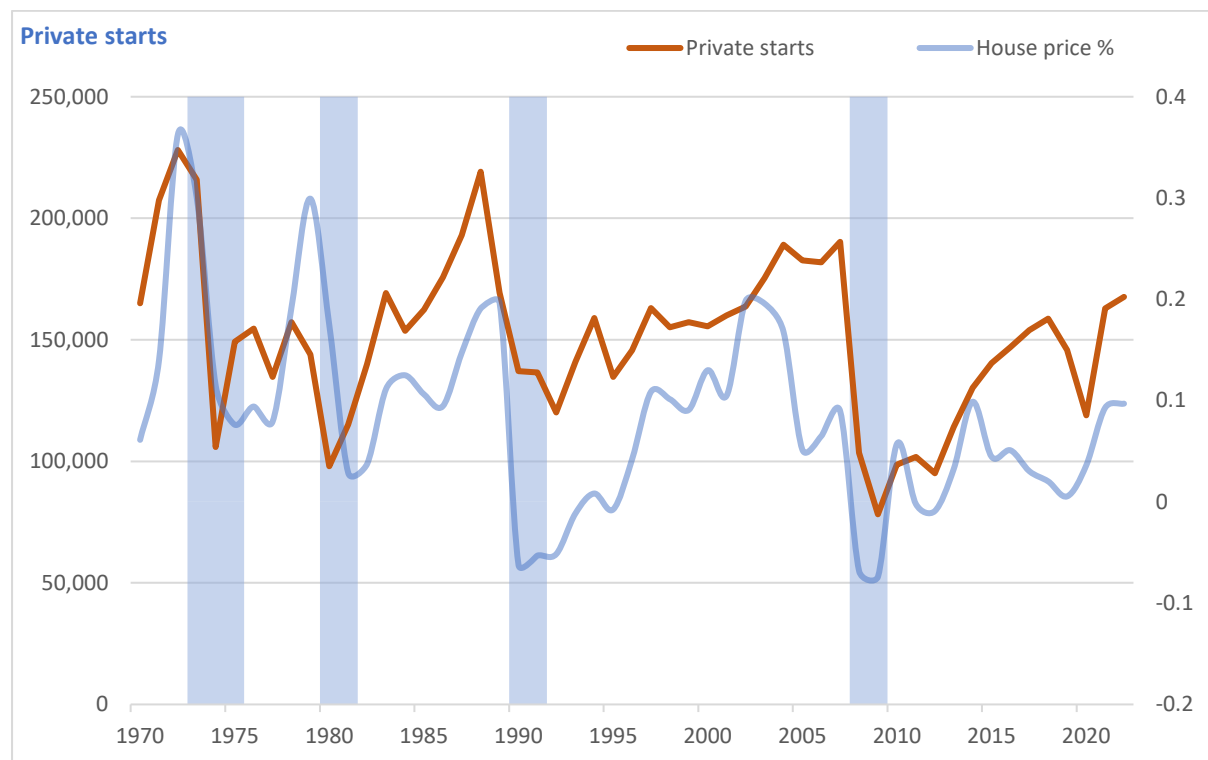
**Chart 4: GB Starts**



Source: Table A2 of the Compendium of Housing Finance Statistics (CML) (1970-77), Office for National Statistics (1978 onwards). Figures relate to GB in all cases. For Wales, author estimates made to derive breakdown of starts by sector from 2011 onwards and total quarterly starts Q2 2020 - Q1 2022 inclusive. For Scotland, author estimates to derive private starts and completions for Q2 2022. Figures for 2022 relate to year ended mid-2022.

UK house prices since 1952, Nationwide Building Society.

**Chart 5: Private starts**

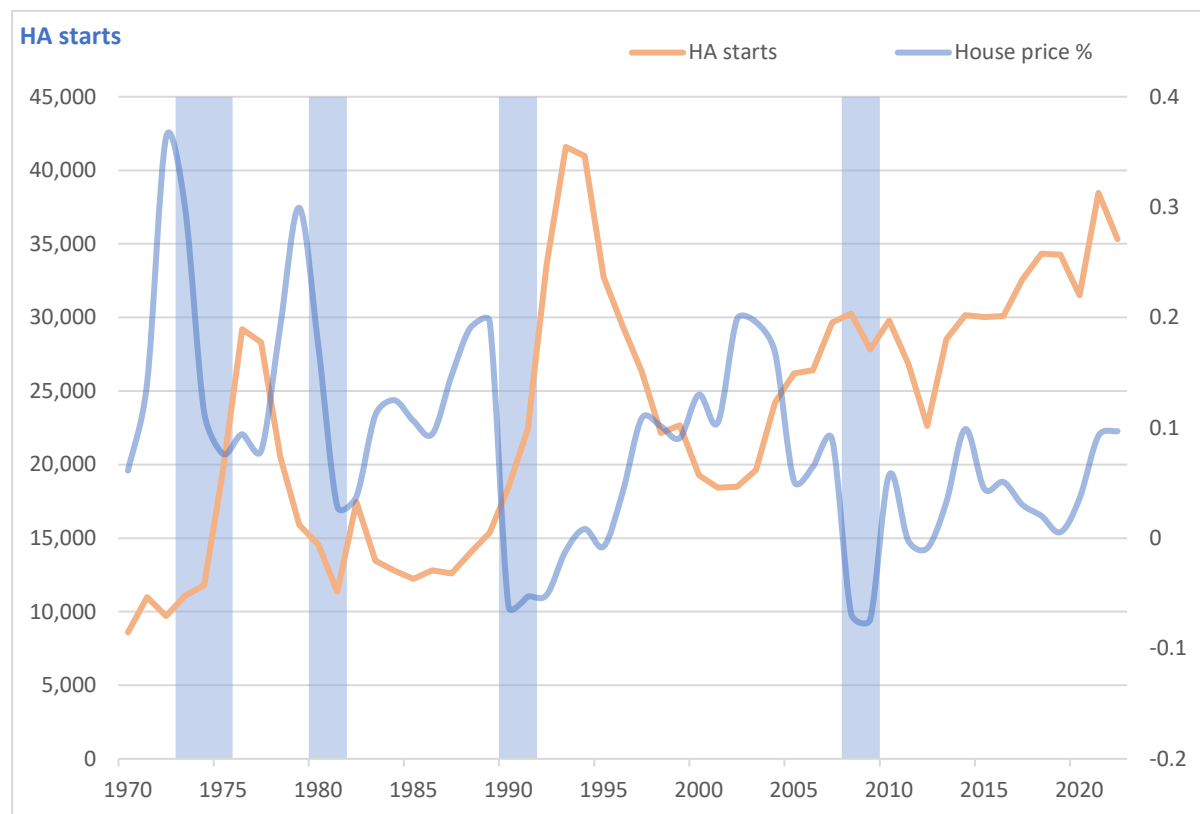


Source: Table A2 of the Compendium of Housing Finance Statistics (CML) (1970-77), Office for National Statistics (1978 onwards). Figures relate to GB in all cases. For Wales, author estimates made to derive breakdown of starts by sector from 2011 onwards and total quarterly starts Q2 2020 - Q1 2022 inclusive. For Scotland, author estimates to derive private starts and completions for Q2 2022. Figures for 2022 relate to year ended mid-2022.

UK house prices since 1952, Nationwide Building Society.



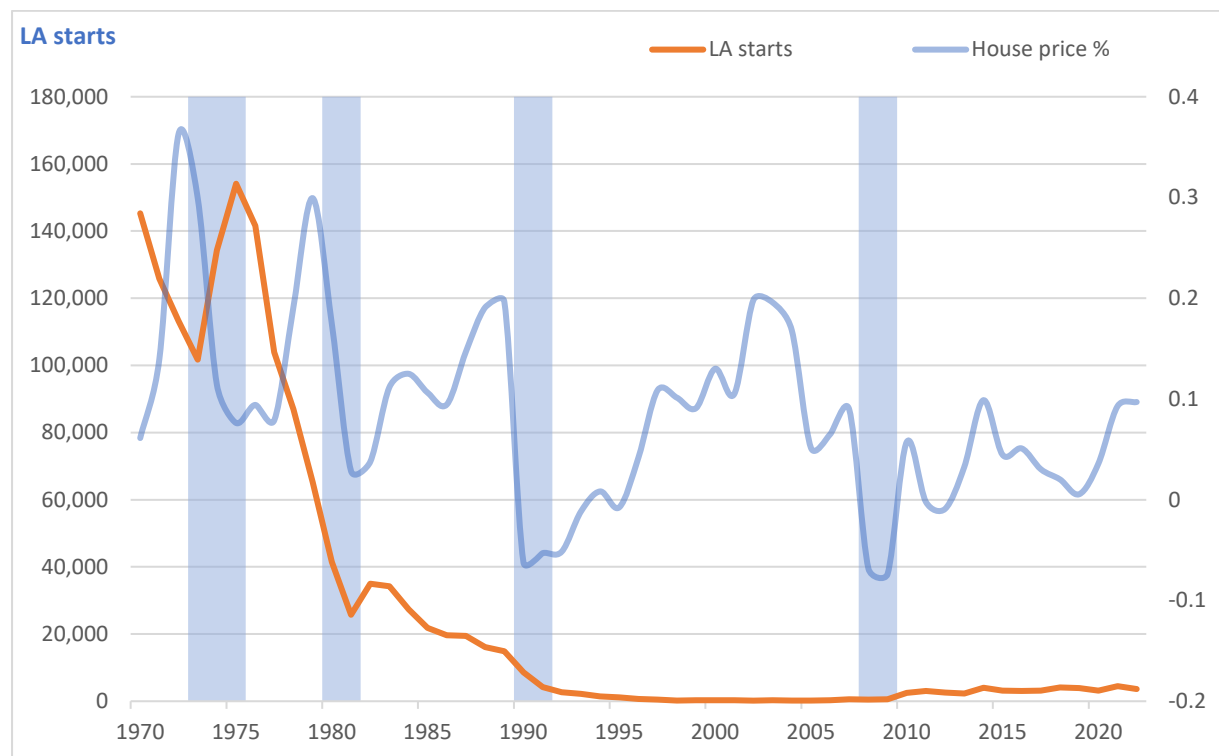
**Chart 6: Housing association starts**



Source: Table A2 of the Compendium of Housing Finance Statistics (CML) (1970-77), Office for National Statistics (1978 onwards). Figures relate to GB in all cases. For Wales, author estimates made to derive breakdown of starts by sector from 2011 onwards and total quarterly starts Q2 2020 - Q1 2022 inclusive. For Scotland, author estimates to derive private starts and completions for Q2 2022. Figures for 2022 relate to year ended mid-2022.

UK house prices since 1952, Nationwide Building Society.

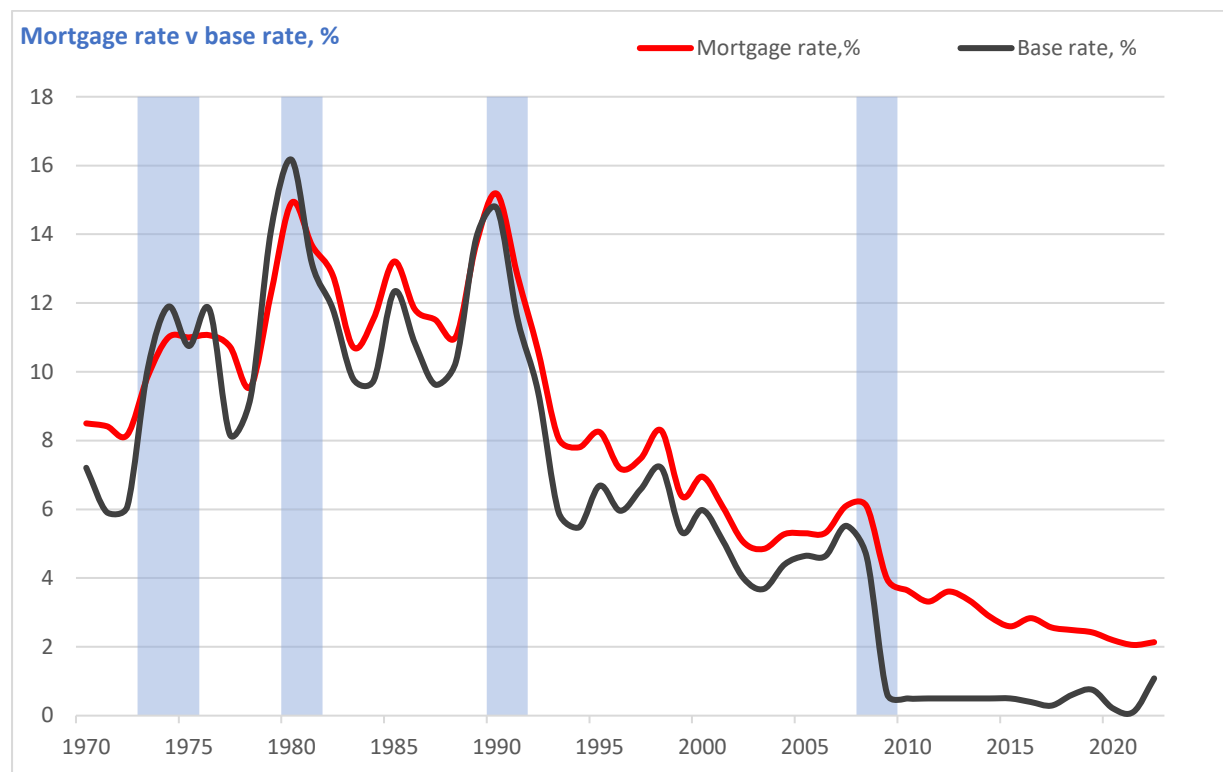
**Chart 7: Local authority starts**



Source: Table A2 of the Compendium of Housing Finance Statistics (CML) (1970-77), Office for National Statistics (1978 onwards). Figures relate to GB in all cases. For Wales, author estimates made to derive breakdown of starts by sector from 2011 onwards and total quarterly starts Q2 2020 - Q1 2022 inclusive. For Scotland, author estimates to derive private starts and completions for Q2 2022. Figures for 2022 relate to year ended mid-2022.

UK house prices since 1952, Nationwide Building Society.

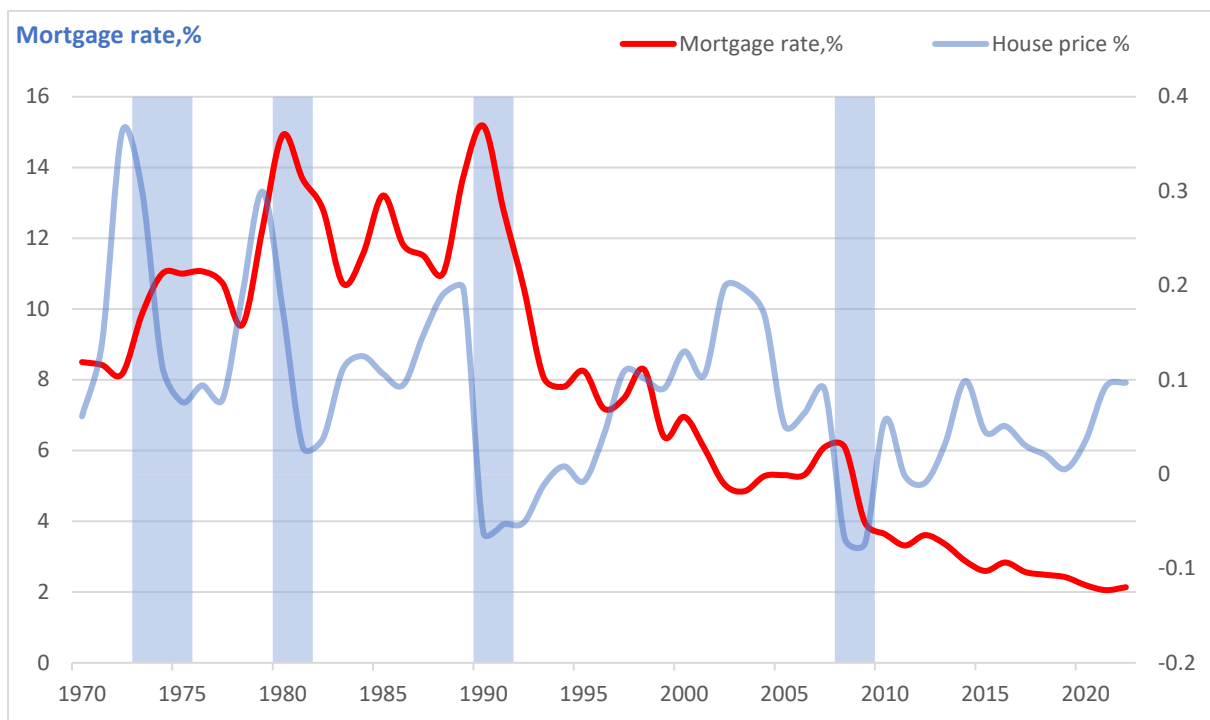
**Chart 8: Mortgage rate v Bank base rate**



Source: All figures provided by Bank of England. Author estimate, based on splicing variable mortgage rate data shown in Three centuries of data – version 2.3 (to 2015) with Effective interest rate on secured loans to individuals - CFMZ6K6 - (2016 onwards).

Bank of England.

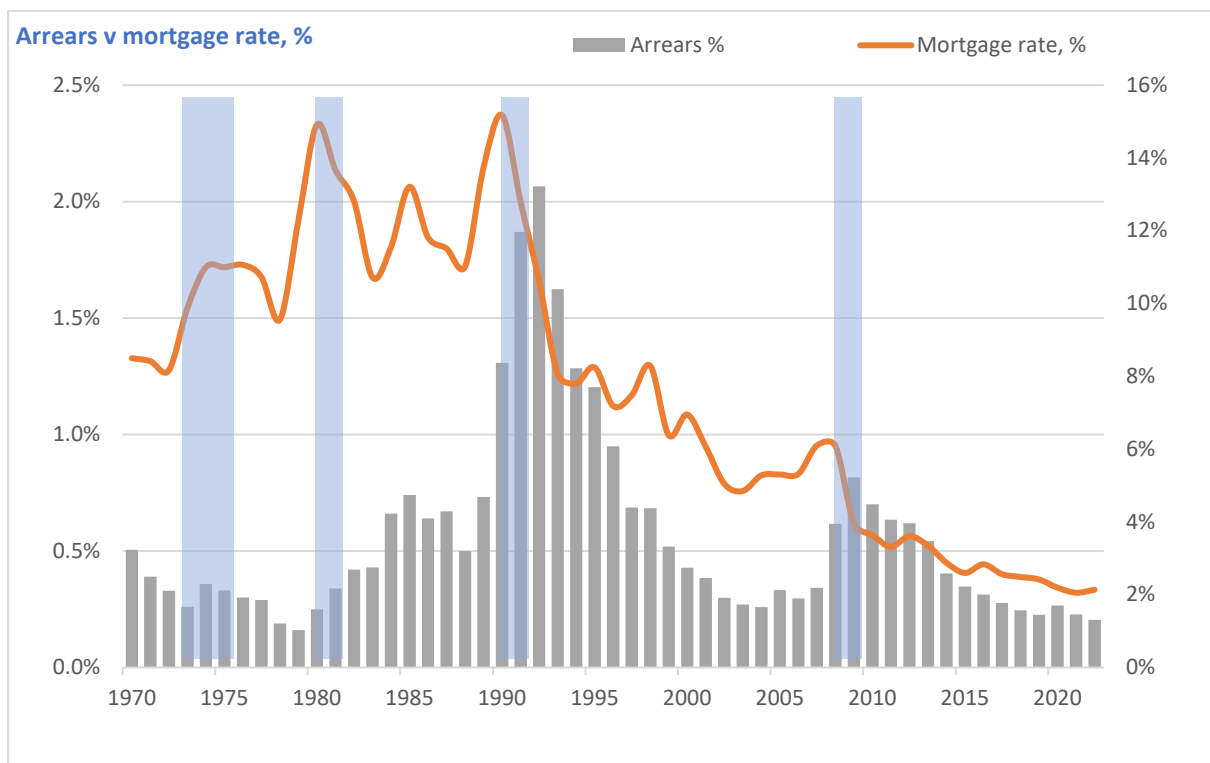
**Chart 9: Mortgage rate**



Source: All figures provided by Bank of England. Author estimate, based on splicing variable mortgage rate data shown in Three centuries of data – version 2.3 (to 2015) with Effective interest rate on secured loans to individuals - CFMZ6K6 - (2016 onwards).

UK house prices since 1952, Nationwide Building Society.

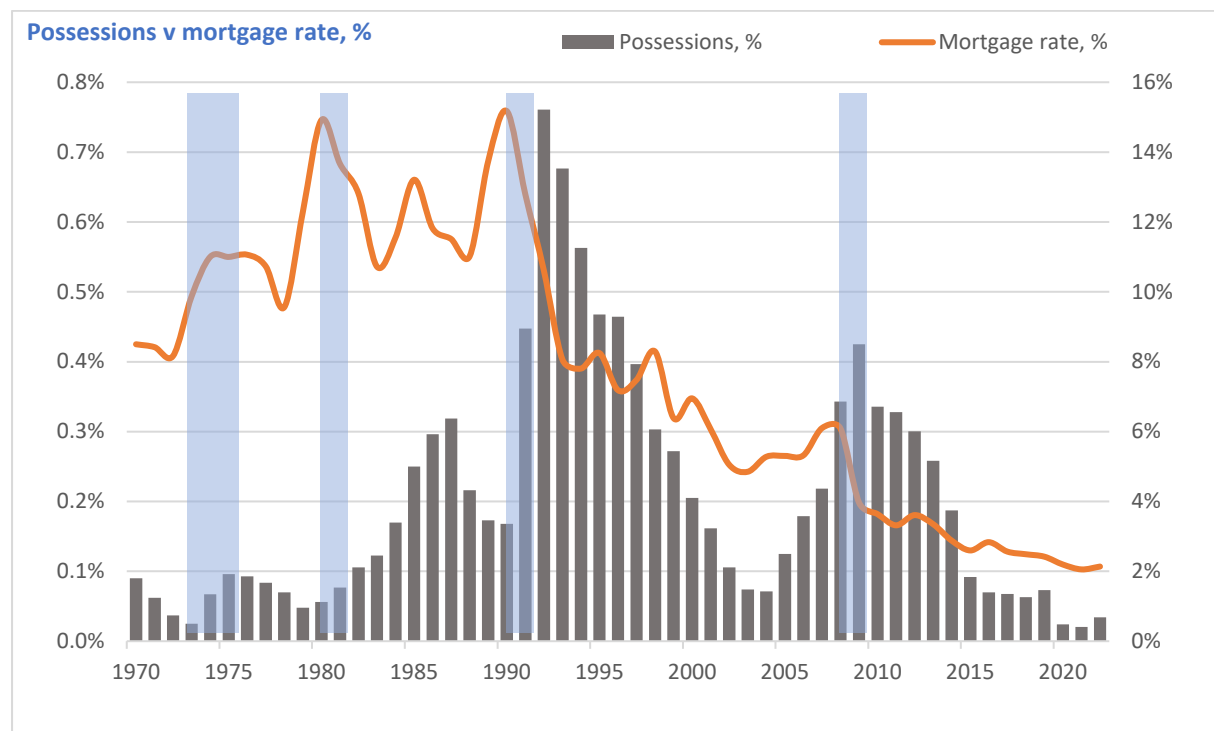
**Chart 10: Arrears v Mortgage Rate**



Source: UK Finance/Council of Mortgage Lenders. Figures show total number of residential mortgage borrowers including BTL. Arrears figures show loans >6-12 months in arrears. 2022 figures are estimates based on data to Q3.

All figures provided by Bank of England. Author estimate, based on splicing variable mortgage rate data shown in Three centuries of data – version 2.3 (to 2015) with Effective interest rate on secured loans to individuals - CFMZ6K6 - (2016 onwards).

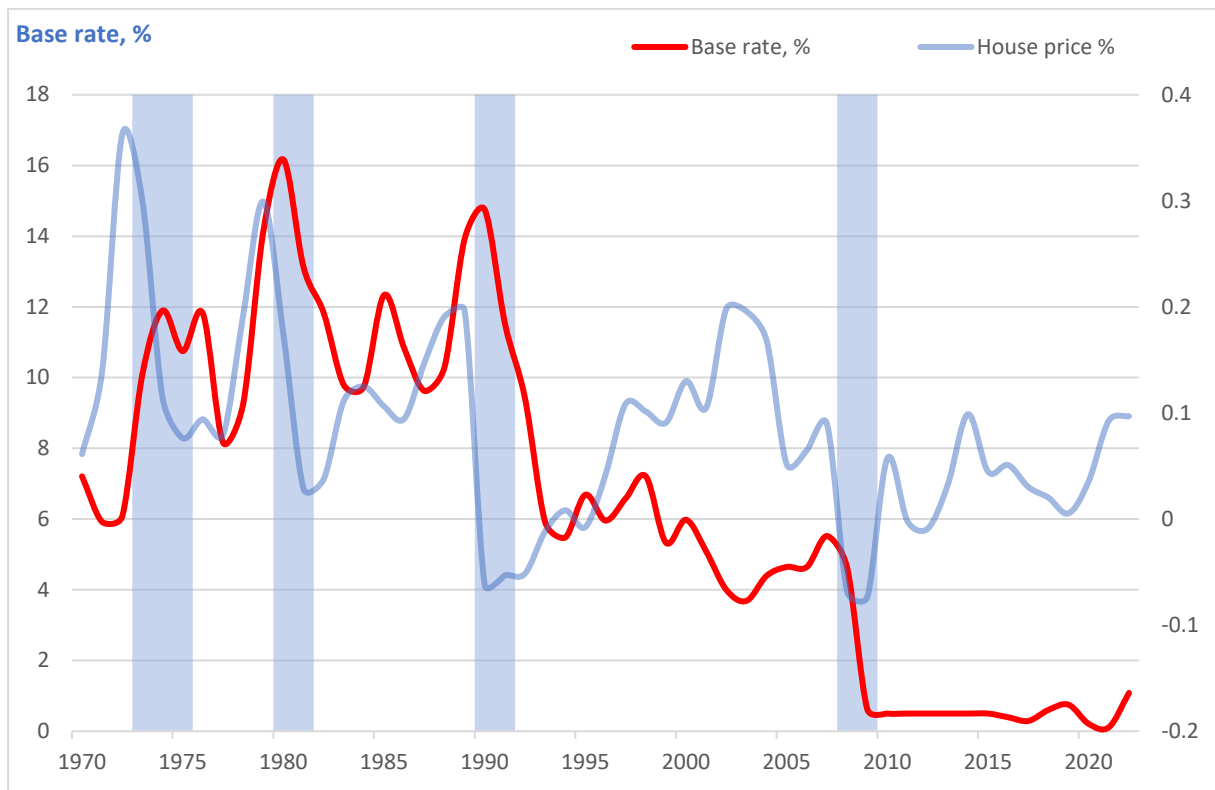
**Chart 11: Possessions v Mortgage rate**



Source: UK Finance/Council of Mortgage Lenders. Figures show total number of residential mortgage borrowers including BTL. 2022 figures are estimates based on data to Q3.

All figures provided by Bank of England. Author estimate, based on splicing variable mortgage rate data shown in Three centuries of data – version 2.3 (to 2015) with Effective interest rate on secured loans to individuals - CFMZ6K6 - (2016 onwards).

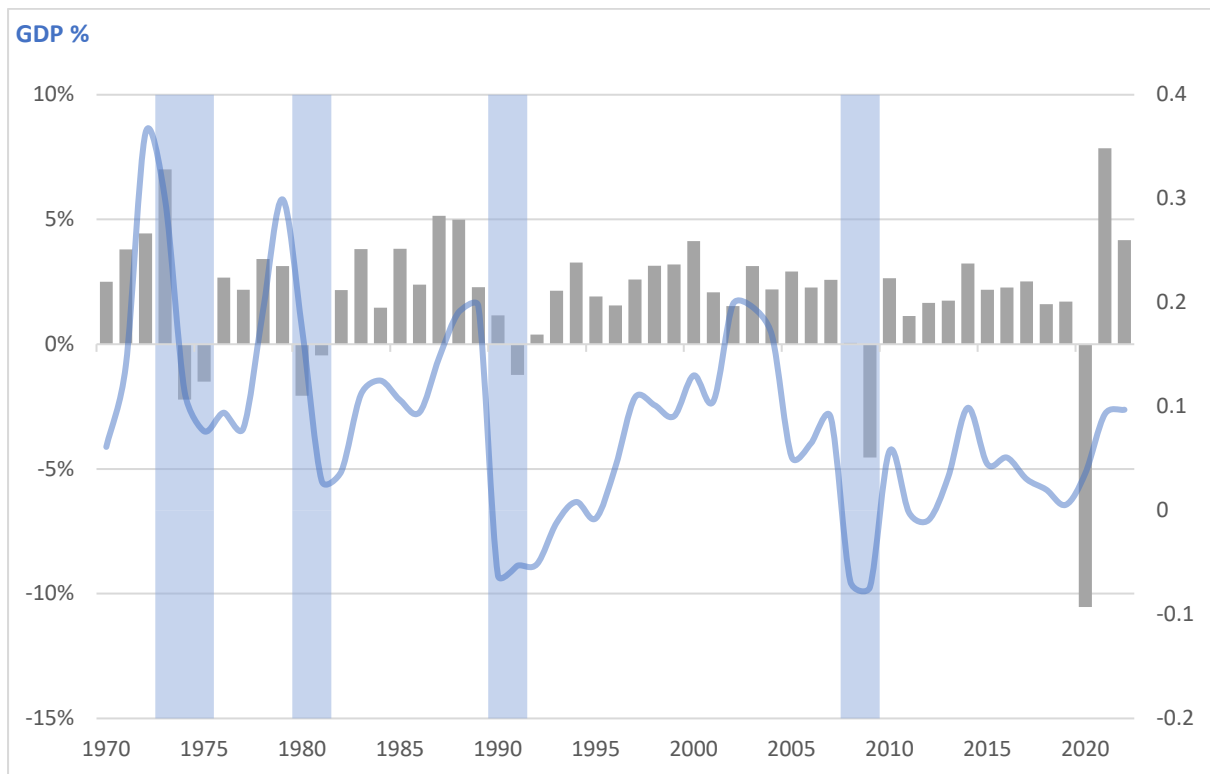
**Chart 12: Bank Base rate**



Source: Bank of England.

UK house prices since 1952, Nationwide Building Society.

**Chart 13: GDP**



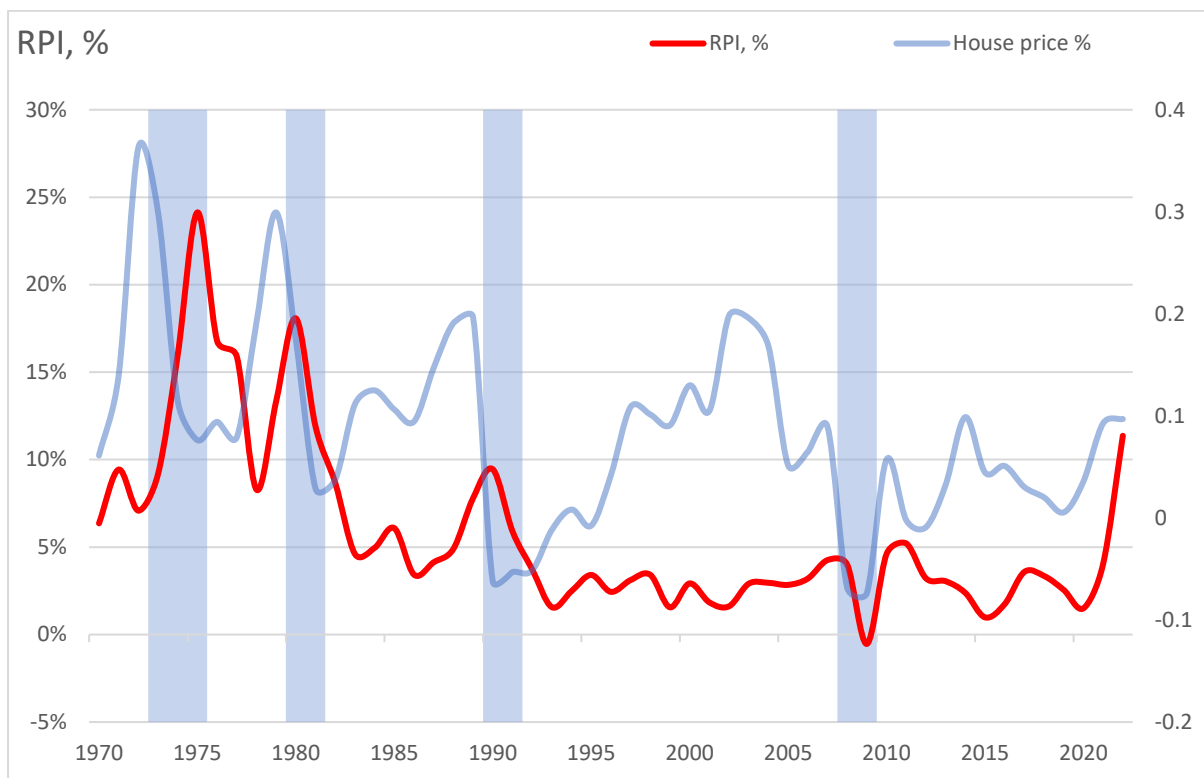
Source: Office for National Statistics. Gross value added at basic prices:CVM:Index:SA. Author averaged quarterly index figures to obtain annual averages. 2022 figures are estimates based on Q1-Q3 2022.

<https://www.ons.gov.uk/file?uri=/economy/grossdomesticproductgdp/datasets/uksecondestimateofgdp/datatables/quarter3julytosept2022quarterlynationalaccounts/quarterlynationalaccounts/datatables.xlsx>

UK house prices since 1952, Nationwide Building Society.



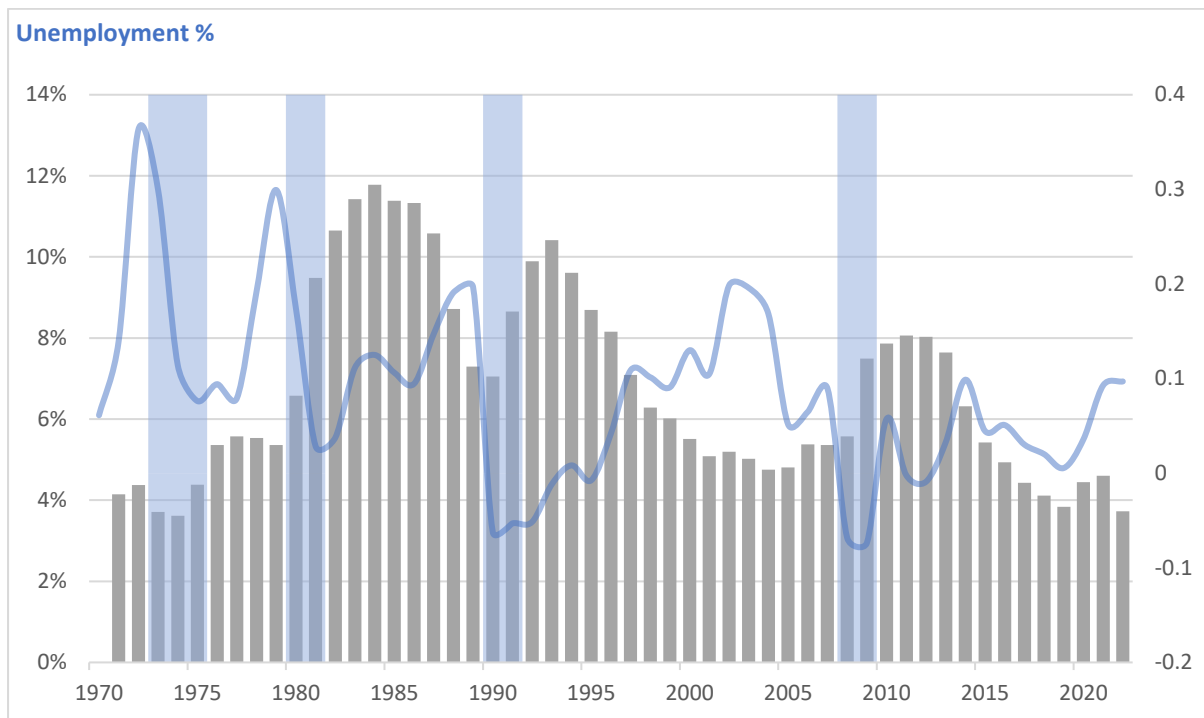
**Chart 14: RPI**



Source: Office for National Statistics. Retail Prices Index: Long run series: 1947 to 2021. Author estimates based on simple averages of monthly RPI % change figures. 2002 figure is estimate based on January - November figures.

UK house prices since 1952, Nationwide Building Society.

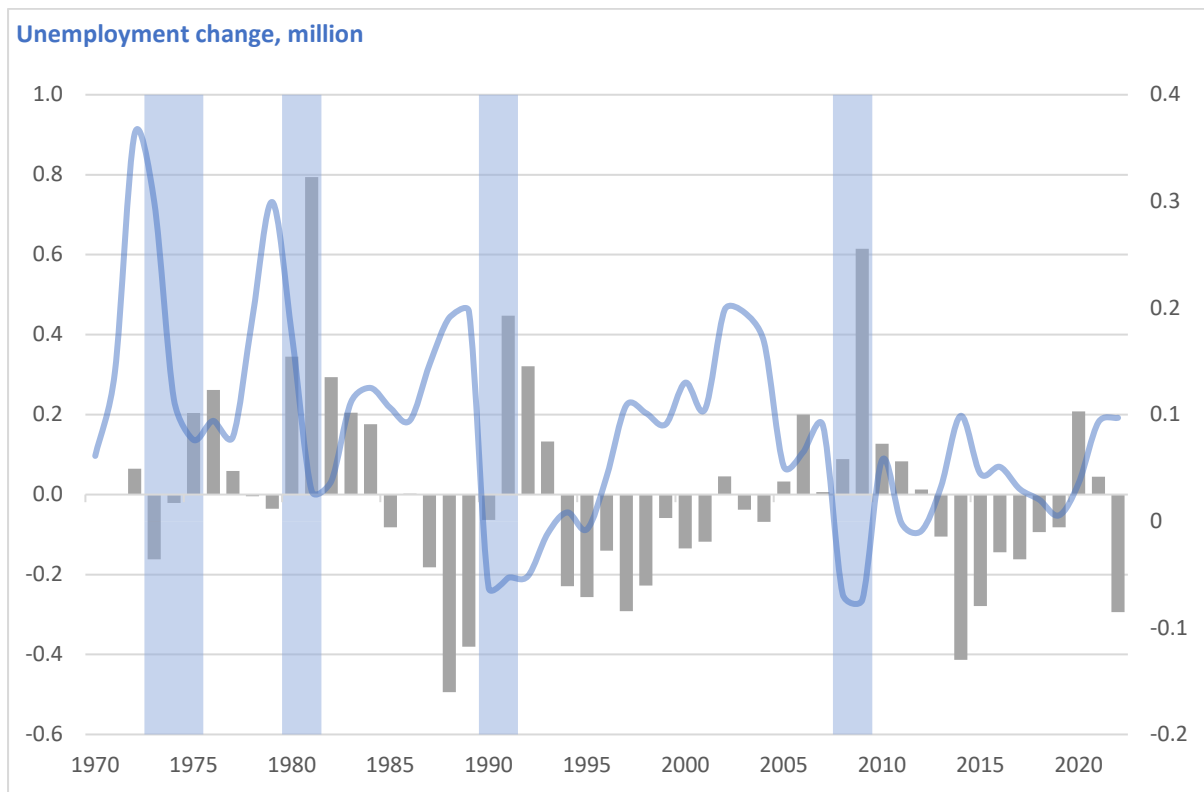
**Chart 15: Unemployment**



Source: Office for National Statistics, Labour market statistics. 2022 figures are estimates based on January - October figures.

UK house prices since 1952, Nationwide Building Society.

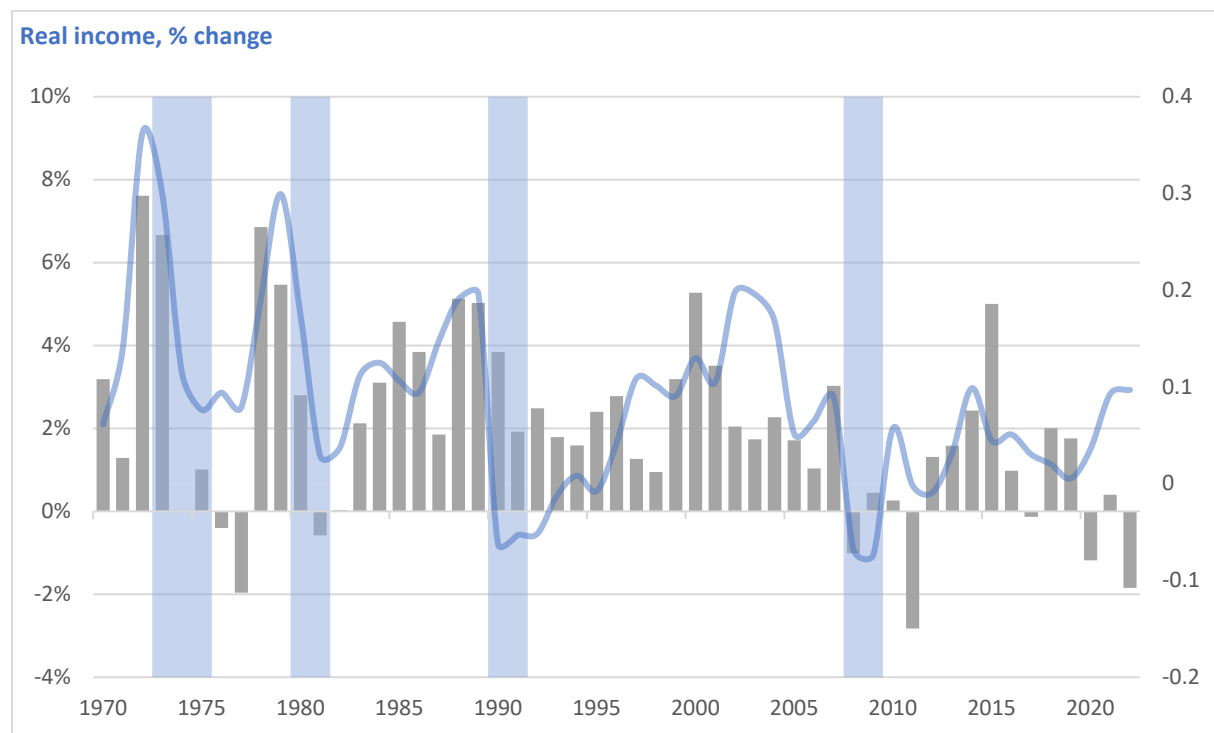
**Chart 16: Unemployment change**



Source: Office for National Statistics, Labour market statistics. 2022 figures are estimates based on January - October figures.

UK house prices since 1952, Nationwide Building Society.

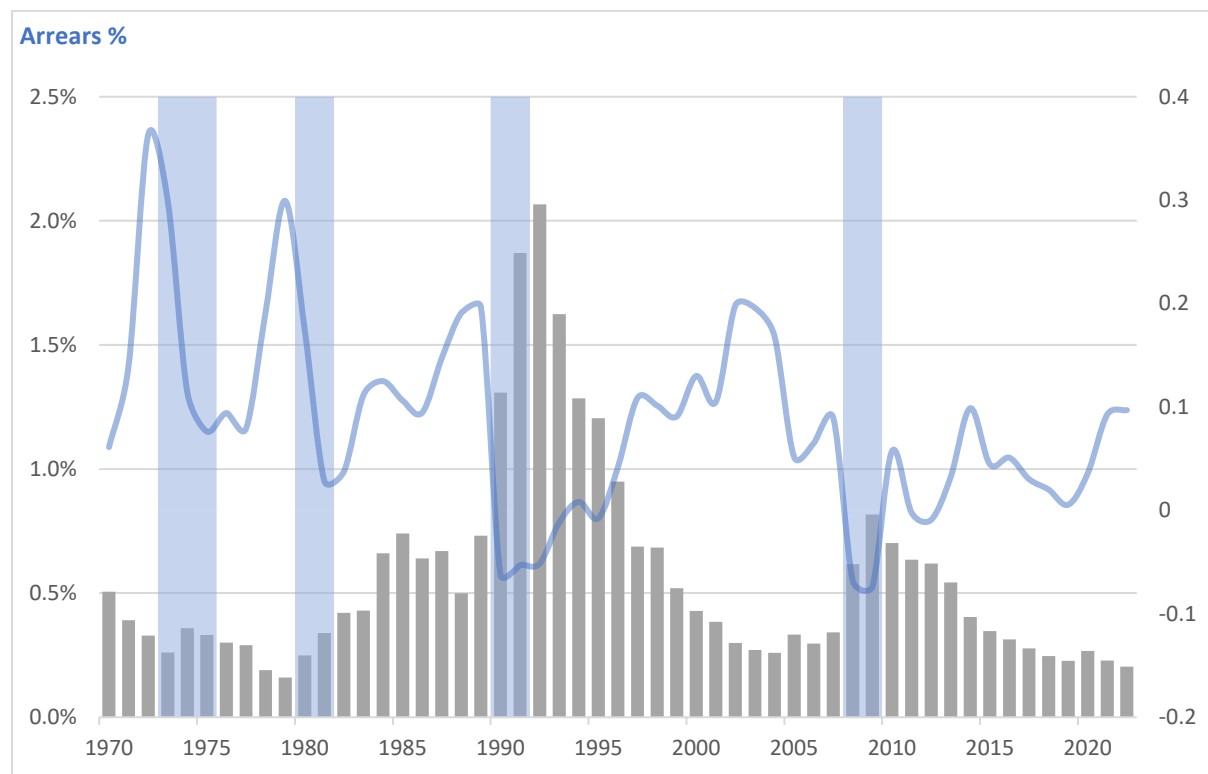
**Chart 17: Real Income change**



Source: Office for National Statistics. Households: Real disposable Income, per head: Quarter on Quarter-1 growth %: Chained volume measure £: Seasonally adjusted. Author estimates. 2022 figure represents first three quarters of year.

UK house prices since 1952, Nationwide Building Society.

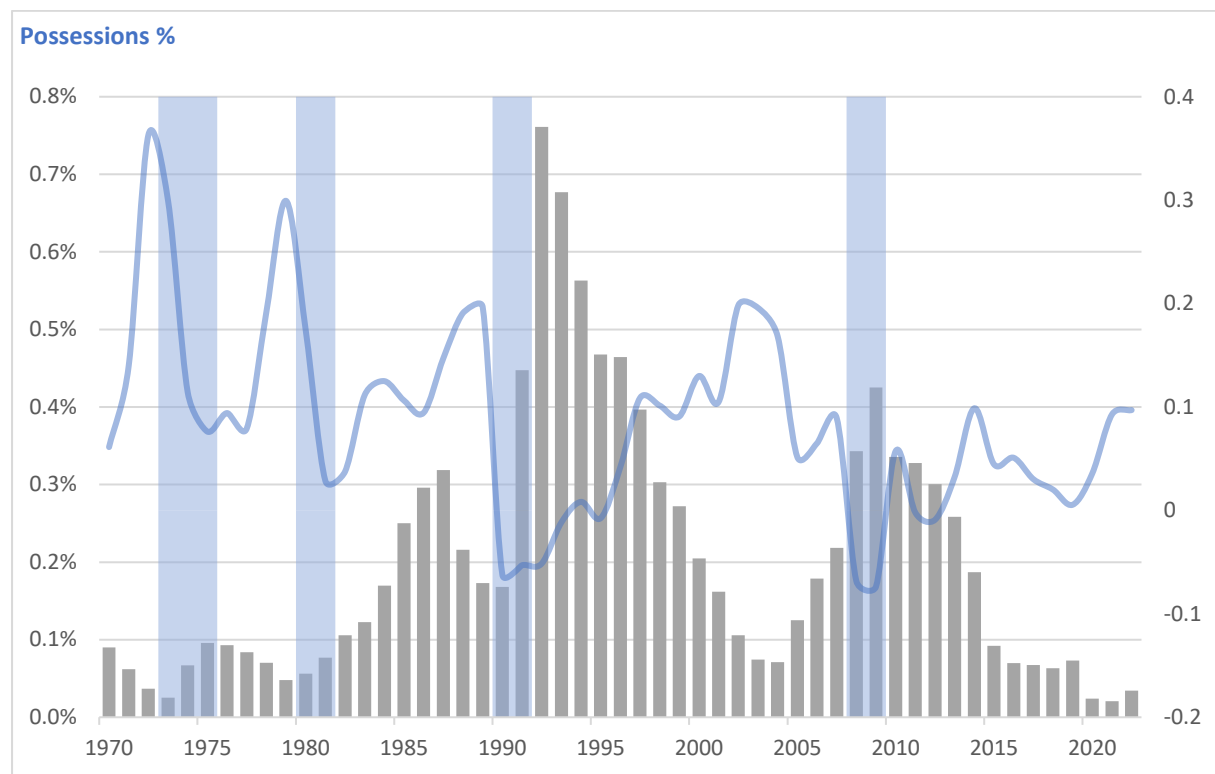
**Chart 18: Mortgage arrears**



Source: UK Finance/Council of Mortgage Lenders. Figures show total number of residential mortgage borrowers including BTL. Arrears figures show loans >6-12 months in arrears. 2022 figures are estimates based on data to Q3.

UK house prices since 1952, Nationwide Building Society.

**Chart 19: Mortgage Possessions**



Source: UK Finance/Council of Mortgage Lenders. Figures show total number of residential mortgage borrowers including BTL. 2022 figures are estimates based on data to Q3.

UK house prices since 1952, Nationwide Building Society.

## Appendix 2: A Short Literature Review: Some Examples

### ***Descriptive Studies***

1. Most such studies are fairly general. Monnery's *Safe as HOUSES: A historical analysis of property prices* (2011) is a rare more tightly focussed contribution.<sup>41</sup> It examines price trends in 10 or more countries including the UK (from 1900) rather than the drivers of prices and the consequences of the cycle. However, based on his review of this range of markets he would list as drivers of a boom (and a bust) as flowing from demographic changes, economic shocks, the supply of new homes, construction costs, mortgage availability, costs of finance as well as expectations, taxation/incentives and alternative housing – all factors which should be recognised as significant.
2. Hamnett's *Winners and Losers: Home Ownership in Modern Britain* (1999) gives explicit attention to booms and busts as he tries to capture who has won or lost in the process.<sup>42</sup> His book covers the post war period up to the late 1990s with a particular focus on the crash of 1990/91. He highlights the significant role of rising incomes relative to house prices at the start of the boom with the house price income ratio at or below its long-term norms. As the volume of sales rises, the stock of unsold homes dries up and prices begin to rise quite sharply. Prices move ahead of incomes and ratios become unsustainable to the point where prices begin to stabilise or fall. He also notes that the three booms (early and late 1970s and the 1980s) were all significantly conditioned by changes in monetary policy and financial liberalisation.
3. Pawley's *Home Ownership* (1978) focusses on the operation of that market.<sup>43</sup> In part three of his book *Life in the Fast Lane* he highlights the rise of property speculation in the 1970s, gazumping and the rapid growth in the supply of mortgage credit. The early 1970s boom triggered extensive debates about the role of housing supply and mortgage credit along with a variety of government interventions not least around low start mortgages and efforts to control the supply of mortgages.

### ***Modelling studies***

4. Most of the relevant academic modelling literature is also about booms and busts rather than specifically about downturns. Francois Ortalo-Magna and Sven Rady for instance published an article in the *European Economic Review* in 1999 which showed that the

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<sup>41</sup> Monnery, N (2011) *Safe as HOUSES? A historical analysis of property prices*, London Publishing company, London

<sup>42</sup> Hamnett, C (1999) *Winners and Losers: Home Ownership in Modern Britain*, UCL Press, London

<sup>43</sup> Pawley, M (1978) *Home Ownership*, Architectural Press, London

co-movement of owner-occupation and house prices was an equilibrium response to income and credit market shocks by examining the causes of the boom bust period from the mid-1980s to the mid-1990s.<sup>44</sup> They concluded that financial liberalisation had been the main cause of the growth of owner-occupation and first time buyers.

5. John Muellbauer has long focussed on the economics of the housing market and periods of boom and bust.<sup>45</sup> He has explored a number of relationships including the links between the market and the economy and between possessions and house prices. In an important article with Anthony Murphy on *Booms and Busts in the UK housing market* (1997) they explore the rises and falls in UK house prices over the period 1957 to 1994 via an annual econometric model.<sup>46</sup> They pay particular attention to financial liberalisation, shifts in wealth effects and consumption alongside real interest rates and income expectations (as well as transaction costs and spill over effects from the private rented sector). They offer up two measures of booms and busts based around house price to income ratios and investment returns to housing.
6. The authors find that the most significant factors include positive income growth, demographics, low real interest rates and what they call “announcement” effects (policy shifts – in this case the introduction of the so called “poll tax and the ending of double mortgage interest tax relief). The authors highlight certain contextual effects for the late 1980s boom – low debt levels, low real house prices, financial liberalisation, favourable demographics and relatively low housing supply. The busts were defined in the main by the reversal of all of the factors present in the upturn – rising real interest rates, weaker income growth, reversing demographics, high debt levels and real house prices and tightened mortgage lending.
7. Geoff Meen has examined the issues of housing market booms and busts in the context of his modelling of the housing market over the last decades. Some of the findings can be found in Meen and Whitehead, *Understanding Affordability* (2020).<sup>47</sup> His latest work which looks at the effectiveness of modelling in predicting outcomes in the housing market and is, as yet, unpublished, suggests that the usual models (including his own) are adequate for understanding housing prices and activity except at cyclical turning

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<sup>44</sup> Ortalo-Magna F and Rady S. (1999) Boom In, Bust Out : Young Households and the housing price cycle, *European Economic Review*, Volume 43 (4-6), 755-766

<sup>45</sup> Aron, J and Muellbauer, J (2011) Modelling and forecasting with county court data: Regional mortgage possession claims and orders in England and Wales, SERC discussion Paper 70, Spatial Economics Research Centre, Oxford

<sup>46</sup> Muellbauer, J., & Murphy, A. (1997). Booms and Busts in the UK Housing Market. *The Economic Journal*, 107(445), 1701–1727. <http://www.jstor.org/stable/2957902>

<sup>47</sup> Meen, G. and Whitehead, C (2020) *Understanding Affordability*, Bristol University Press, Bristol



points or in response to large external events – clearly the periods of most interest to forecasters and policy analysis including the study of downturns.

### ***Policy Oriented Analyses***

8. A study sponsored by the Rowntree Foundation and reported on by Stephens in *Tackling housing market volatility in the UK* (2011) focussed on the persistent volatility of the UK housing market since 1970 (identifying four major booms and busts) and the impacts these housing cycles had on housing choices, possessions, housing supply and wealth inequality.<sup>48</sup>
9. In terms of solutions the report argues that although improving housing supply is the key to reducing the risks of market volatility in the longer term it cannot remove it altogether. Credit controls were also highlighted as a corrective measure alongside reformed Council Tax and Stamp Duty in the short term. The system of safety nets for homeowners was flagged up as inadequate with proposals set out for a new structure. While private renting provided a flexible alternative to ownership for many younger and more mobile households, it was deemed an unsuitable alternative for households requiring longer-term secure and affordable homes. The report highlighted the importance of maintaining an affordable social rented sector as a part of the UK's mainstream housing system.
10. Stephens et al *Evaluation of English Housing Policy* (2005) comprehensively evaluated the full range of Departmental housing policies individually over the period 1975 – 2000.<sup>49</sup> It also provided a more overarching analysis of the individual policies under five main themes for which the Department had responsibility: supply, need and access; finance and affordability; housing and neighbourhood quality; widening choice; and management effectiveness.
11. Of particular interest to this report are the two papers contributed by Alan Holmans, who by then had retired from his role in the Department as Chief Economist: '*Housing and housing policy in England 1975 – 2000, Chronology and commentary*' and '*The Context for housing policy since 1975*' (both 2005).<sup>50</sup> The first sets out the range of policies and their objectives by tenure and notes that the major trend throughout much

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<sup>48</sup> Stephens, M (2011) *Tackling housing market volatility in the UK*, the report of the Housing Market Taskforce, Rowntree Foundation, York

<sup>49</sup> Stephens, M et al, (2005) *Evaluation of English Housing Policy 1975 – 2000, Lessons from the past, challenges for the future*, Office of the Deputy Prime Minister, London

<sup>50</sup> Holmans, A (2005) '*Housing and housing policy in England 1975 – 2000*', '*Chronology and commentary*' and '*The Context for housing policy since 1975*' in Holmans, A. E (1987). *Housing Policy in Britain: A History*. <https://doi.org/10.4324/9781003134756>.

of the period was a decline in state activity. He also noted that by the late 1970s the shortage of housing had been overcome and concern did not reappear until the mid-1990s. The second analyses the associated time series data. In 2005 Holmans also published *Historical Statistics of Housing in Britain* supported by the Economic and Social Research Council.<sup>51</sup> This brought together very long time series data for most major housing variables.

12. The Department in its various guises has made many contributions in this broad area over a long period of time, for example, publishing reports on the relationship between house prices and land supply (1992) and looking at house prices over time at different levels (1990).<sup>52</sup> <sup>53</sup> In the latter, Holmans makes the point that over the decades (primarily focussing on the post second world war period) the market has become increasingly dominated by the sales of existing dwellings rather than the cost of new building. He therefore suggests that the housing market has some of the characteristics of an asset market where expectations, demand and supply become ever more important. In 2004 the Department also published an evaluation of five high level housing policy themes of which two were on Supply, Need and Access and on Finance and Affordability.<sup>54</sup>
13. In 2018 the Department published an analysis of the determinants of house price changes arguing that prices were fundamentally a function of the supply of and demand for housing with demand being correlated with the number of households and changes in real incomes.<sup>55</sup> In part the paper was published in order to qualify the conclusions of an earlier National Housing and Planning Advice Unit (NHPAU) report on affordability and to provide updated estimates of the real impact on house prices over 25 years.<sup>56</sup>
14. This NHPAU report had estimated that, all things being equal, in relation to house prices and affordability the following relationships would hold:

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<sup>51</sup> Holmans, A. E. (2005), *Historical Statistics of Housing in Britain*, Published by University of Cambridge Centre for Housing and Planning Research.

<sup>52</sup> Gerald Eve with the Department of Land Economy, University of Cambridge (1992) *The Relationship between House Prices and Land Supply*, Planning Research Programme, DoE, HMSO, London

<sup>53</sup> Holmans, A. E. (1990) *House Prices: Changes through time at National and Sub-National Level*, Government Economis Service, Working Paper No 110, DoE, London

<sup>54</sup> Stephens, M. et al. (2005) *Evaluation of English Housing Policy 1975 – 2000, Lessons from the past, challenges for the future*, Office of the Deputy Prime Minister, London

<sup>55</sup> MHCLG (2018) *Analysis of the determinants of house price changes*, Ad Hoc publication, MHCLG, London

<sup>56</sup> NHPAU (2007) *Affordability Matters*, NHPAU, DCLG, London

- If the number of households increases by 1%, house prices would increase by about 2%;
- A 1% rise in real incomes would increase house prices by 2%;
- If interest rates increase by one percentage point then house prices would fall by around 3%; and,
- If housing stock increases by 1%, house prices would fall by around 2%.

### International perspectives

15. International comparative evaluations are often restricted to regular publications such as the annual statistical publication by the European Mortgage Federation's Hypostat<sup>57</sup> which includes an annual review of housing and mortgage market across Europe and regular articles on topics of current interest; and the OECD's regular reviews of each OECD country and overview publications such as *Housing Taxation in OECD countries* which covers Market Trends and Challenges as well as a comparative assessment of housing policies and possible reforms.<sup>58</sup>
16. Other relevant evaluations address taxation and subsidy differentials. For instance, in 2021 Lunde and Whitehead reviewed the full range of taxation arrangements by tenure across twenty European countries plus Australia and the USA.<sup>59</sup> They found that housing taxation systems differ greatly but all are complex and inconsistent with any formal set of principles. There are however some consistent trends away from favouring owner-occupation as compared to rental properties.
17. Housing finance more generally has been relatively well covered in the international comparative literature at least since the 1990s. *Housing Finance in the 1990s* brings together papers from a European conference and describes developments over that period in many European countries together with the USA and Australia.<sup>60</sup> It stresses the growing internationalisation of finance markets in general and the effect that this has had on housing finance in particular. Patterns identified include that specialist

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<sup>57</sup> ECBC (2022), EMF Hypostat 2022: An In-Depth Look At European Housing & Mortgage Markets In 2021, Available at: <https://hypo.org/ecbc/press-release/emf-hypostat-2022-an-in-depth-look-at-european-housing-mortgage-markets-in-2021/>

<sup>58</sup> OECD (2022), *Housing Taxation in OECD Countries*. Available at: [https://www.oecd-ilibrary.org/taxation/housing-taxation-in-oecd-countries\\_03dfe007-en](https://www.oecd-ilibrary.org/taxation/housing-taxation-in-oecd-countries_03dfe007-en)

<sup>59</sup> Lunde, J and Whitehead C (2021) *How taxation varies between owner-occupation, private renting and other housing tenures in European countries*, UK Collaborative Centre for Housing Evidence, Glasgow.

<sup>60</sup> Turner, B and Whitehead, C, eds (1993), *Housing Finance in the 1990s*. National Swedish Institute for Building Research

institutions tend to diversify while mainstream financial institutions organisations entered and sometimes dominated the housing market. What was also noted was that in many countries the growing importance of debt finance had been associated with greater volatility in the housing market, leading to problems of affordability, possessions and lower levels of housing investment.

18. This conference in turn led to *Milestones in Housing Finance* which compared the housing finance systems and their impact for some 20 countries over a twenty five year period from 1989 to 2016.<sup>61</sup> It sets out the different models of funding; and in particular discusses the relationship between mortgage debt and increases in house prices. Of particular relevance is the chapter by Professor Judy Yates which showed how reforms from the early 1980s to mid-1990s had had a positive impact on how the Australian system responded to the GFC in terms of stability but negative impacts on distribution.
19. This reflected a more detailed article by the same author in 2011.<sup>62</sup> It showed that after the Global Financial Crisis, the Australian Government, unlike many others, successfully offset some of the downward economic pressures by not only reducing interest rates but also directly incentivising first time buyers to enter the market and, in particular, to buy newly built homes. These counter cyclical measures however did little to change the underlying structural issues – the rise in first home buyers was short lived and both renters and future first home buyers have almost certainly ended up paying more. The paper noted that the current body of research across developed countries showed similar patterns but concentrated more on the role of financialisation in generating worsening conditions both for tenants and first-time buyers. The impact of the increasing market power among existing owners deserves similar analysis.
20. A particularly relevant article by Jorda et al (2015) reinforces her message.<sup>63</sup> The paper looks at seventeen countries over the past 140 years and demonstrated that it is only leverage bubbles involving massive increases in credit availability that generate the real costs leading to deeper recessions and slower recoveries. Credit fuelled house price bubbles they argue have become particularly dangerous. A PhD thesis on

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<sup>61</sup> Lunde, J and Whitehead, C (eds) (2016), *Milestones in European Housing Finance*, Wiley Blackwell, Chichester

<sup>62</sup> Yates, J (2011) Cyclical versus structural sustainability of home ownership: is counter-cyclical intervention in housing markets enough? *Housing Studies* 26, 1059 - 1080.

<sup>63</sup> Jorda, O, Schularich, M and Taylor A (2015) Leveraged bubbles, *Journal of Monetary Economics* ,76, Issue S, pages S1 to S20

housing bubbles by Sergio Basco in 2018 is valuable for its review of relevant material on the nature and impact of bubbles with detailed examples from the USA and Spain.<sup>64</sup>

21. There has been a number of comparative studies following on from the Global Financial Crisis. A paper by Scanlon et al (2011) argued that many of the trends observed during the prior boom, especially the innovations in financial instruments, were reversed.<sup>65</sup> It reported on a 2009 survey of housing experts from 16 industrialised countries, which clarified how each country's mortgage system responded to the crisis and how governments addressed the problems of borrowers. A selection of essays in *Global Housing Markets Crises Policies and Institutions* covers the causes and consequences of the sub-prime crisis and the GFC across the USA, Western Europe, Transition Countries and Asia – plus four countries Australia, Brazil, Canada and Israel which showed various levels of immunity to the contagion effects of the GFC.<sup>66</sup> Lessons included: regulatory structures when enforced made a difference; global linkages played a role; quick decisive public sector responses helped (with Australia as the main example).
22. In this context an article in the Financial Review using Morgan Stanley data noted that there had been six national price downturns of 5% or more in real, inflation-adjusted terms over the past 45 years, including two in the past decade.<sup>67</sup> They also suggested that there was very little the Reserve Bank of Australia (RBA) could do to help lower borrowing costs further and bring forward demand, especially should the cost of money continue to increase in other parts of the world.

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<sup>64</sup> Basco, S (2018) *Housing Bubbles, origins and consequences*, Palgrave Macmillan

<sup>65</sup> Scanlon, K, Lunde, J and Whitehead, C. (2011) Responding to the housing and financial crises: mortgage lending, mortgage products and government policies. *International Journal of Housing Policy*, 11 (1).

<sup>66</sup> Bardhan A et al (2012) *Global Housing Markets: Crises Policies and Institutions*, Wiley. The chapter by Scanlon and Whitehead covers selective bubbles in the UK and Europe.

<sup>67</sup> Scutt, D. (2018), A history of Australian housing market downturns in one chart *Financial Review*, April 6th <https://www.afr.com/property/residential/a-history-of-australian-housing-market-downturns-in-one-chart-20180406-h0yeob>

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