

How a Land Value Tax would help resolve Britain's housing crisis

Jerry Jones

The huge escalation of house prices in recent years has put home ownership beyond the reach of many people. However, the cost of actually building houses has changed hardly at all. The problem, which has become a major crisis, is almost entirely due to the escalating price of land, and the demand for housing, exceeding supply. Many first-time buyers have been forced to borrow, sometimes, far beyond their means, and at a considerable risk to themselves.

Banks have drawn people into taking such risks by drastically relaxing their conditions for loans – from which, currently, they are making huge profits – in the belief that they have hedged against defaults through the use of complex financial instruments traded on the world's capital markets. This easy availability of credit has had the effect of further increasing the demand for homes to buy, adding a new twist to the escalation of house prices.

The problem has been made worse by successive governments and local authorities selling off public sector housing at subsidised prices, resulting in a chronic shortage of social housing. This, in turn, has led to private sector landlords taking advantage of the situation by charging exorbitant rents to people unable to get onto the housing ladder, or who are stuck on waiting lists for social housing. Meanwhile, local authorities or housing associations willing to invest in social housing are deterred by the high price of land.

An added ingredient to the escalation of house prices is that a major speculative element is involved. Many landowners, including house builders, are withholding land from the market, in order to support the higher prices, and in the expectation of making sizeable capital gains later when the land, with or without housing, is eventually sold. This, in the short run, tends to push up house prices all the more. According to the Royal Town Planning Institute, there is enough land in London with planning permission to deliver some 30,000 houses each year until 2016. Meanwhile, the Empty Homes Agency has estimated that, in England as a whole, there are some 680,000 properties standing empty.

The worry is that this escalation of house prices is a speculative bubble waiting to burst. If interest rates go up, or there is an economic downturn, it would not be long before defaults and house repossessions start occurring on a large scale, thus precipitating a major slump in house prices, and the spectre of negative equity in which people owe more than their house is worth, as happened in the 1991/92 recession, but on a much larger scale.

Had a system of Land Value Tax (LVT) been in place, all these problems could have been prevented. First, the market price of land, the main ingredient in the escalation of house prices, would have been kept under control because the bulk of its increase in value would have been collected as LVT. Second, it would have made no economic sense for speculators to withhold land from the market because they would have been penalised by having to pay LVT. Third, landowners, once they had received planning permission, would have had the incentive to develop the land for housing as rapidly as possible. This would have boosted the supply of housing, and dampened the tendency for house prices to rise. Fourth, lower land prices would

have made it more affordable for local authorities and housing associations to acquire land for social housing, thus increasing the supply of accommodation at affordable rents. In addition, the greater availability of social housing would have meant that private landlords would have been less able to charge exorbitant rents, which often, in effect, are subsidised by taxpayers through housing benefit.

Introducing LVT now would address the current housing crisis head on, but it would require a certain amount of political will, and support from the government.

First, the introduction of LVT, if the speculative bubble had not already burst, would likely bring down the market price for land considerably, which is the main element in the escalation of house prices. Since some 70 per cent of Britain's population is involved in some way with home ownership, this would have a significant impact on most people – at least on paper. In fact, for most people who own homes purely for their own accommodation, it would make little difference. If prices go down, they will get less when they sell, but will pay less for the houses they intend to move to. Their heirs will also get less, but they, too, normally, would not lose out because most people use their inheritances for acquiring homes of their own, or for trading up into larger accommodation or moving to better areas, which would cost less.

The main issue that the Government would need to address would be to help those who had recently stepped onto the property ladder, borrowing large amounts in order to acquire properties when prices were more or less at their peak, especially those left with negative equity. One approach would be to require banks, which in part were responsible for fuelling the house price boom, to hive off a part of the debt into special accounts that carry no interest apart from adjustment for inflation, and for banks to invest those funds to generate revenues that would gradually draw down the debt.

Meanwhile, because of the urgent need to step up the supply of affordable housing for rent – not just for key workers, but for all who need them – this should be supported by Central Government offering low interest loans to local authorities to acquire land for housing purposes.

With LVT in place – along with new regulations to control credit – booms and slumps in the housing market, which can be so disruptive, and which also impact on the rest of the economy, would be a thing of the past. Not only would this help resolve the current housing crisis once and for all. It would end also the inequalities arising from unearned wealth accumulation derived from landownership.