Forgetting Past Lessons? The UK Housing and Mortgage Markets.

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Abstract

The UK housing and mortgage markets appear to have now teetered over into what may become a significant downturn. Why is this so and to what extent has the experience of the last boom and bust in the housing market apparently been forgotten by the industry, by consumers and by Government? This short paper sets out the facts regarding lending, house prices, new housing and the UK's now dynamic rental market. It asks to what extent there are similarities with and differences to the last traumatic market cycle, and inquires into the effects of a credit crunch originating in the US sub-prime market, a slow down with dramatic effects on at least one major high street lender, Northern Rock? The paper urges caution in making these comparisons and reflects on the social and psychological factors that appear to be at play in both the media and the industry but which impact on market sentiment and perhaps on fundamentals, too.

Key Words: UK housing market, mortgage finance crisis, social housing.
JEL Classification: O18 , R20

1. INTRODUCTION

The UK housing market is now (May 2008) showing all of the signs of entering a significant market downturn after a relatively long period of consistently rising house prices (since the mid to late 1990s). The UK’s largest building society (the Nationwide) reported at the end of May 2008 that annual nominal house prices had fallen for the UK by more than 4%. This is occurring, ironically, at the same time as housing policy has risen to the top of the domestic policy agenda – as Government seeks to substantially increase housing supply for affordability and regional economic policy regions. The now emerging problems have been shaped in part by the UK ramifications of global credit market difficulties – the Northern Rock bank collapse, the necessity to provide substantial liquidity in credit markets and the ultimate nationalisation of Northern Rock. In recent months the decline in inter-bank lending has reduced the range of mortgage products available and, as a by-product, lending to social housing has virtually ceased.

Personal wealth is heavily concentrated in owner-occupied housing and aggregate consumption growth in the last 10 years has been fed by the housing market’s performance. There are widespread concerns that the macro-economy will be badly affected by problems in the housing and mortgage market. In particular, much has been made, at a sometimes subliminal level, that the UK housing market-economy relationship will repeat the boom-bust experience of the late 1980s and early 1990s wherein the stalling housing market dragged the economy further into recession.

This short paper seeks to explain what is happening in the UK housing market and why and to what extent the situation resembles or differs from that of the last downturn (1989-95). Section 2 provides an outline overview of the UK housing system. Section 3 sets out the recent evidence on housing and mortgage market behaviour in Britain. Section 4 reprises what happened in the last boom and bust before section 5 argues that there are important differences this time around – but that in fact some of the risks are greater than before (although there are also potential opportunities that did not exist in the early 1990s). Section 6 concludes.

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2. UK HOUSING

What are the distinguishing features of the UK housing system? Housing tenure is dominated by home ownership, now more than 2/3 of all housing in the UK. The rental market is now more than 10% and around one in five households are in the social rented sector.

Tenure change was driven in the 1980s by home ownership growth but this slowed in the 1990s. More than 2 million households have bought their council homes at discounted prices but ownership growth was also facilitated by income growth and a highly deregulated mortgage market offering a range of generous products to first time buyers. In the last 5 years there has been increasing use of inter-generational loans and gifts to make purchase possible as affordability constraints have made becoming a home owner more and more difficult[1]. In the last 5 years also the UK has experienced the rapid growth in buy to let mortgages – residential loan terms provided to landlords with properties marketed by letting agents. This has been the largest growth area for mortgage lending in recent years and is an important but controversial part of the emerging housing system, particularly in Britain’s cities. The slow decline of social renting masks large-scale change within the sector through the continuing growth of housing associations at the expense of the remaining council sector and the advent of arms-length management organisations who have taken over the management and modernisation of around a million council homes in England.

The UK housing market is both cyclical and highly regionalised. The present phase is the fourth downturn since 1970 though the last downturn in the early 1990s was particularly deep and lengthy (involving significant nominal falls in prices, negative equity, large numbers of defaults and a contraction in transactions and associated backward and forward linkages to the economy). Levin and Pryce (2007) have argued that the rental market evidence of fairly flat real rents suggest occupational demand and supply may be in short run or medium term balance – the long period of rising prices seems to owe more to speculation among investors, perhaps, an asset bubble, rather than specific identifiable demand growth or supply weaknesses (even if there are long term issues on both counts).

Consistent evidence has found the UK to be made up of a series of regional housing markets subject to ripple effects in prices originating in London and the south East. These appear to operate

1) In 2005-06, according to Council of Mortgage Lender data, as many as 2 in 5 first time buyers relied on informal financial support from families and friends to provide a down payment that would make a first mortgage possible.

across England and Wales but separate forces appear to prevail in Scotland and Northern Ireland. Weaker regional housing markets in the North have recently been the subject of significant levels of state intervention through housing market renewal pathfinders.

The long term tends of importance for the UK housing market (and policy strategies) are:

- Demand growth originating in demographic pressures through shrinking household sizes, natural growth and immigration
- Low long term interest rates and continuing favourable taxation of home ownership are likely to keep the user cost of housing low
- Supply price elasticities for new housing are very low in the long term and are considered to be a key explanation for the UK's high long term real house price inflation

Uncertainty about the competitive impact of large flows of residential investment competing with the owner-occupied sector for new and second hand housing.

What are the important institutional features of the UK housing system? The UK has a sophisticated and integrated lending system which is highly competitive and closely tied into the wider global financial markets. The structure of lending has been transformed by the gradual transformation of almost all building societies into banks, the extensive use of inter-bank lending to sustain the wholesale lending sector which, until recently, ensured a virtually perfectly elastic supply of housing credit. Mortgage lenders typically continue to rely for the majority of their mortgage funds from retail sources – the major exception to this was the Northern Rock bank which was heavily exposed to international sub-prime lending.

The UK system has generated a wide range of products (several thousand in late 2007 now reduced by more than half in a more conservative lending context). But the UK has not developed securitised products on a large scale and consequently has not, with the exception of Northern Rock, produced long term fixed rate products. Instead a range of variable, fixed and discounted products linked to different terms and conditions have been available rarely longer than 3-5 years in duration. A large re-mortgaging market also exists where borrowers are incentivised to re-negotiate their mortgage if there is a net saving to be made. In recent years, apart from Buy to Let loans, this has been the major area of lending growth for high street lenders. While there are some specialised sub-prime lenders – market exposure is negligible compared with the situation in North America.

Housing taxation has evolved to greatly favour home ownership with respect to other forms of investment or business taxation and compared with private landlords. Although mortgage rate tax deductions were phased out during the 1990s, there remains no capital gains taxation on real gains made on one's primary residence; neither is there taxation of imputed rental income benefits accruing to the owner-occupier. Value added tax is not levied on new housing and transactions taxes (Stamp Duty) are comparatively lightly taxed compared with much of mainland Europe[2]. There are property taxes levied: the council tax in England, Wales and Scotland (a relatively flat tax based on a banded estimate of property value as at 1991, which as this indicates has no general revaluation) and a flat percentage capital value tax based on 2005 values in Northern Ireland. Scotland plans to abolish the council tax and replace it with a tax on incomes though it is uncertain whether or not this will happen.

Housing supply is shaped by the close inter-relationships between private developers and the land release planning system. Housing supply depends on the granting of planning permission (increasingly supply is focused onto brown field urban land) and this generates massive premia for land owners (residential land is untaxed in terms of specific development taxes). This rather than contracting profit is the motivation for housing developers who trade land with planning permission and market property – and normally subcontract building to construction contractors. The industry is also characterised by excessive merger, rationalisation and take-over strategies. The UK system has evolved into large volume house builders who use centralised designs and procurement strategies to secure economies of scope and scale. Most house building is speculative though UK governments now use planning permission to secure quotas of affordable housing (often social housing). There is considerable debate but many believe that the historic low levels of private completions during the recent boom are indicative of a restrictive planning system seeking to control development and protect green belts around cities, etc while increasing densities of new build on brown field sites – alongside a rather inefficient and unstrategic hours building sector.

The key policy issues confronting the housing market concern the Government's ambition to increase supply, including the proportion of affordable housing, to simplify and better incentivise the housing planning system, to maintain housing credit and, at the sub-regional scale, to facilitate strategic housing interventions that will allow local housing systems to evolve in a way consistent

2 The tax is levied at 0% on properties priced at £125,000 or less, 1% between £125,000 and £250,000, 3% between £250,000 and £500,000 and 4% on values above £500,000. Lawyer and estate agency fees are also competitively prices, rarely above 1-2% of property value.

with demand. On accession the Prime Minister, Gordon Brown, highlighted the importance of housing and brought the housing minister into Cabinet. At the same time in Scotland the first major consultation paper produced by the new Nationalist Government was a wide-ranging housing policy programme. In Northern Ireland, the planning system is under close scrutiny and review after an intensive government review of affordable housing. In all cases, each Government seeks to expand supply in the long term, undoubtedly responding to both cyclical and long term pressures – but these proposed supply programmes will unfortunately coincide with the downturn in the housing market.

3. THE CONTEMPORARY UK HOUSING MARKET

What evidence is there about the UK housing market's recent performance? In one sense there is too much evidence. Several competing data sources use proprietary or commercially-sourced data to provide the most up to date news on prices, transactions, returns, market sentiment, equity withdrawal, lending, levels of starts or completions. Some of the data available is subject to small market shares and gaps at lower geographical scales, some of the data originate in a black box of unknown veracity, other data is 'professional' and qualitative in nature, other price data is subject to well-known index construction and quality-adjustment problems. Nonetheless, it is evident that there are important trends emerging – even if the media treats it both un-analytically and as a political weapon in bigger party political debates.

Table 1 provides a long term sense of the evolution of nominal house prices and an index (2002 quarter 1 set to 100). In a period of high inflation, nominal house prices rose 5 fold between 1970 and 1980 but it took two cycles and 22 years before they rose by the same factor again (i.e. to 2002). However, the long trend in price increases essentially from 1996-97 until the summer of 2007 has allowed house prices to rapidly inflate and in a period of low inflation to drive a wedge between housiing costs and income affordability.

Table 1 UK Regional House Prices, Selected years, 1970-2006

year	UK Nominal house Prices (£)	UK House Prices Index (2002= 100)
1970	4,975	4
1975	11,787	9.4
1980	23,596	20
1985	31,103	28.8
1990	59,785	57.4
1991	62,455	56.6
1992	61,366	54.5
1993	62,333	53.1
1994	64,787	54.4
1995	65,644	54.8
1996	70,626	56.7
1997	76,103	62
1998	81,774	68.8
1999	92,521	76.7
2000	101,550	87.7
2001	112,835	95.1
2002	128,265	111.2
2003	155,627	128.7
2004	180,248	143.9
2005	190,760	151.8
2006	204,813	161.4

Source: Wilcox, S, 2007, Housing Review. Joseph Rowntree Foundation: York, Table 47a and 47b
Note: average prices unadjusted for mix of properties in sample

More recent evidence has to come from a single data provider. HBOS is the largest mortgage lender in the UK and has a long-established hedonic house price index. Their data[3] suggests that in the year to April 2008 house prices in the UK fell by 0.9% but be 1.3% in the last month alone. Their competitor Nationwide suggested that house price shad fallen 4% over the last 12 months to April 2008. HBOS point out that house prices have trebled in the UK in the 10 years to August 2007 with average house prices rising by more than £130,000 over that period. This is considerably more than income growth in the same period. Allied to price trends completed sales have fallen by 20% in the year to March 2008. Indeed, the volume of transactions has come down considerably compared with previous cycles (there were 1.7 million sales in 1988 compared with less than 1.2 million in 2005-2007). The 1986-88 period saw turnover as a percentage of stock up at 12% whereas, according to Halifax research, this fell to 7% between 2005 and 2007. Mortgage lending has of course contracted in the wake of credit market problems and there is some evidence of house builders facing difficulties selling properties and talking to social landlords as a way to offload land.

3) Halifax house price index – national index April 2008.

Council of Mortgage Lenders data suggests that that since the summer of 2007 there has been a significant contraction in loan provided. Table 2 summarises monthly data for loans and other indicators for successive March figures in 2006, 2007 and 2008. This data is presented for all mortgage loans and for first time buyers separately. The table makes a series of strong points: mortgage lending has collapsed particularly in the period after the summer of 2007 with both first time buyer and all loans falling by 50% in 12 months. This has also had large negative impacts on the value of business done by lenders. Yet, at the same time, income multiples and payments continue to rise.

During the period since August 2007, there has also been a major shift in the type of loans being offered. CML data on fixed and variable rate lending indicates a major restructuring of products while at the same time there has been a significant reduction in the range of products available. In April 2007, 75% of new loans and remortgages were fixed rate products, 6% were discounted for a limited period, 14% were tracker loans (linked directly to movements in the base rate), 1% were capped and 4% were standard variable rate mortgages. Eleven months later in March 2008, only 54% of loans were fixed, discounted products had risen to 10% but tracker loans had shot up to 31%.

Table 2 UK Mortgage Lending , Monthly Comparing March 2006-2008

Indicator	*March 2006*	*March 2007*	*March 2008*
FTBs:			
Number of loans	34,500 (38)	32,500 (35)	17,800 (38)
Value of loans £	£3.598 b	£4.145 b	£2.274 b
% advanced	90	90	89
Median Income multiple of advance	3.14	3.32	3.35
Median interest payment as % of income	16	18.3	20
All loans:			
Number of loans	90,100	88,800	46,500
Value of loans £	£11.964 b	£13.143 b	£7.022 b
Median income multiple of advance	3	3.14	3.15
Median interest payment as % of income	15	17	18.4

Source: CML Tables ML2 and ML4, May 2008.

The credit crunch has had several direct and indirect effects on mortgage and housing finance markets more widely:

- A lack of funds, market downturn and a broader correction to more risk averse conservative lending practices has reduced the scope and size of new lending massively (see table 2).

- The reliance on wholesale funding has been particularly problematic and this is has been the main source of intervention by the Bank of England to try to provide liquidity by making, effectively, wholesale funds available when the banks would not lend to each other. Nonetheless, less funds are available and lending has become considerably more difficult for house purchase.
- This also reduces funding available to social landlords – the UK's housing association model relies on long term mortgage finance to develop, and even though it is relatively low risk, social housing borrowing has largely disappeared.

For the time being, the Northern Rock problem has been staunched and the contagion prevented, though the political damage to the Government has been incalculable in both promising to bail out the Bank's savers to stop the run on the bank and ultimately nationalising it – if only as a temporary measure (if a buyer can be found). The government though was surely right to do what it did even if it should have intervened earlier and perhaps should have drawn a tighter regulatory net around lender risk practices.

Ultimately, a struggling housing market, a much tighter lending market and problematic economic indicators (inflation, energy costs, etc) will manifest in mortgage arrears and repossessions. Data collected by Wilcox (2007) shows that the regulated mortgage market operated in the 1970s with levels of repossessions below 5,000 a year. This grew to 19,300 in 1985 before the housing bust of the early 1990s when these numbers grew to more than 75,000 in 1991 (Wilcox, 2007, table 51). Despite the deepening of the deregulated mortgage market, economic growth and a buoyant housing system kept repossession levels lower thereafter, falling as low as less than 9,000 in 2003 and 2004. However, the profile of annual repossessions has been upward since (i.e. even before the present crisis): 14,600 in 2005, 22,400 in 2006 and 27,100 in 2007. As a percentage of the entire mortgage book these numbers are tiny but again the trajectory is worrying (CML tables, 2008, Table AP4). This is reinforced by a similar trend on mortgage arrears of more than 3 months.

One of the most discussed features of the UK housing market in recent years has been the rapid growth in residential investment largely associated with Buy-To-Let (BTL). These are loans to private landlords but are negotiated on terms equivalent to standard mortgages rather than business loans (but still benefiting from business tax codes). Although the UK rental market was deregulated in 1988, it was not until the last 6 or 7 years and the linking of such loans to letting agencies (which were supposed to reduce the lending risk) – that the market took off. It has been the best performing part of the mortgage industry for several years and continues to grow. 2007 saw the largest new loan addition through BTL mortgages – 346,000 new loans and over a million such loans outstanding. BTL is very controversial as it is often viewed as inherently speculative, something exacerbating the problems facing first time buyers (since BTL purchasers are competing in the same market and pushing prices up) and a sense that the investment is short term and ultimately damaging. However, it should be borne in mind that the sector is small, hard to research, new and disproportionately the subject of anecdote and little hard evidence.

In this light, a recent research literature review by Ecotec (2008) has summarised what is now known about the sector:

- BTL accounts for about a quarter of the rental market (3% of the national housing stock).
- Specific investor groups can be identified: including small-scale investors with small portfolios who expect to be letting property into the longer-term, in contrast to speculative investors, many of whom 'buy to leave' and do not actually let their properties. Ecotec argue that there is an increasingly close relationship between these latter investors and the new build apartment market (2008, p.7). A third group of larger often corporate landlord investors can also be identified, focused more on a rental income stream and hence letting as a going concern than on speculative capital growth.
- Aggregate vacancy rates are stable at around 6-7% (within considerable local variation).
- There is evidence of cyclical behaviour: landlords appear to reduce their portfolio of holdings as interest rates rise and increase them as rates fall and house prices rise.

The evidence for BTL pricing out first time buyers is not definitive despite localised anecdotal evidence. It does appear that the residential investor has become an important purchaser of new housing. Low prices in older terraced urban stock have also been important to BTL purchasers (Ecotec, p.9) but there is no evidence of a clear house price effect from BTL investment.

4. THE LESSONS FROM THE PAST

A central theme of this paper is the link between the last boom and bust in the housing market – the traumatic experience from broadly 1986-1995 – as compared to what the market now faces. To better understand the relationships between the two, this section briefly summarises the earlier episode.

What happened in the last 'bust' from broadly 1989-1995? The boom that preceded the market downturn was the result of several factors coinciding. There were sustained house price increases induced by financial deregulation, income growth, low interest rates, tax cuts and the botched abolition of a tax concession that generated a short duration bubble of market activity. The crash was brought on by rapidly accelerating interest rates (as high as 15% in 1989) aimed at tacking wider inflation, alongside the wider economy slowing down (see: Maclennan and Gibb, 1993, for more analysis of the boom and bust in the early 1990s).

The main symptoms of the bust were:

- Collapsing mortgage and housing transactions activity (with consequences through backward and forward linkages for the wider economy – exacerbating slowdown).
- Nominal house prices falls of more than 30% by the time the market had fully unwound.
- Falling prices generated negative equity and low positive equity – more than a million households were unable to move because the value of their homes was less than the sum of their outstanding mortgage debt and the transactions costs of moving. This also deepened recession because it reduced consumption and increased savings and mortgage repayments.
- The sustained boost to aggregate consumption delivered by housing equity withdrawal (as much as 6% of all consumption in 1988) vanished and was replaced by net investment in housing,
- This was also associated with rising mortgage arrears and ultimately repossessions, which rose to 72,000 in 1992 alone. There was evidence that rising mortgage defaults were also associated with further falls in house prices.

Mortgage lenders were bailed out to an extent by the mortgage indemnity guarantee insurance (MIG) polices they held on losses made against the unsecured portion of the properties on their mortgage book. Thus the fall in value was ultimately borne not by the lenders but by insurance companies and ultimately, in the form of higher insurance premiums, by consumers of general insurance. This moral hazard, where liberal lending was not penalised by market correction led to a redrawing of MIG insurance contracts such that co-insurance became more common.

In the North, deindustrialization has reduced employment levels, introduced new forms of less protected and more flexible work (one quarter of jobs in the UK is part time or temporary) and weakened the ability of workers in developed countries to preserve their wage levels, welfare benefits, labour rights and working conditions, resulting from a century of struggles of the national labour movements and of far-sighted welfare and social policies of national governments.

5. WHAT'S NEW AND WHAT IS THE SAME?

It is unlikely that, if the UK is about to experience a more extensive market downturn, it will simply repeat what happened during the last housing market recession (Gibb and O'Sullivan, 2008). This is so for several reasons (not all of them helpful to medium term market stability).

In the first place, this time around many more transactions in the housing market involve residential investors with different motives to owner-occupiers. Unlike the situation in the early 1990s, there is significant market penetration by investors in both the traditional first time buyer market but also in the new build (usually urban apartments). This is important for several reasons:

- Investors may respond differently to owner occupiers in response to a downturn and such responses will depend on attitudes to risk and the timescales associated with their investments. For instance, falling prices in the short run may offer purchase opportunities although for others they may reflect fears about future capital gains, precipitating market exist and further downward pressure on prices.
- To the extent that the investment in the rental market is sustainable (an empirical question in different cities and regions), this offers the opportunity to increase the flexibility of local housing markets – this is still early stages in the product life cycle for modern market renting in the UK but it may offer important labour market and easy access housing benefits if it takes root.

A second difference is that there is less of a safety net for mortgagors getting into difficulty because of changes to specific social security assistance (income support for mortgage interest) and under-provision of mortgage payment protection insurance which was supposed to be the market solution. Back in the mid-1990s, government saw social security help with mortgage costs preventing a market insurance solution and worries about public expenditure led them to redesign public assistance requiring at risk borrowers to take out mortgage payment protection insurance to protect payments for up to 12 months. It was envisaged that a market would develop accordingly. In practice, throughout the benign economic conditions of the last 10 years or so – take-up has, for various reasons, been low and currently stands at around 20% of mortgagors. It is not at all clear that the vulnerable or at risk group are disproportionately more likely to purchase insurance and hence there are concerns that mortgage default will worsen in the absence of the safety net and that this will convert into public expenditure through subsequent homelessness and social housing programmes or indeed rental housing allowances.

A third key difference from the early 1990s is that the current market correction is occurring at the same time as supply is being rapidly increased to meet housing policy objectives relating to affordability, demographic projections and regional economic policies. While there is a longstanding debate regarding the distorting impacts of the planning system on house prices, densities and development, housing supply expansion plans can only work with the grain of the market. In practice, it is only by tightening the market and keeping it in balance that proposals to expand supply could work – provided they remain in step with long term demand.

Fourth, it can be credibly argued, as was indicated earlier, that the recent house price inflation experience has in many areas been primarily about the formation of a now unwinding asset bubble masking a fairly stable demand-supply situation for housing, with the latter evidenced by static real rents in the private rented sector (Levin and Pryce, 2007). If true, this suggests that concerns about affordable housing shortage and subsequent fears regarding falling market demand may both, from a medium term perspective, prove exaggerated.

A fifth point is that the greatest uncertainty relates to the wider economy and whether recession will cross the Atlantic in the wake of credit market problems. An important lesson from 1989-1993 was that housing market bust can both worsen and feed off wider economic turbulence. We are used to hearing about how recent economic growth has been strongly supported by both unsecured credit and housing wealth effects. Unfortunately, the converse is also true in recession (Maclennan and Gibb, 1993).

A final difference concerns provider insurance. The 1989-95 episode did not affect lender balance sheets as badly as it might because UK mortgage lenders had indemnity guarantees insured with general insurance companies. This protected them from negative equity losses after repossession. Instead it was the insurance companies and ultimately their consumers who paid for it through higher premiums. The industry response was co-insurance that would hopefully lead to less liberal lending and sharper incentives for lenders in general. The anecdotal evidence (it is not straightforward to find these things out) is that the lenders are in the current period relatively under -insured in terms of possible losses. This may of course be changing in response to market conditions but of course the terms will not be so favourable. Under –insurance may also revise the lenders' willingness to repossess in a falling market.

Taking these issues together, it is not unreasonable to suggest that the housing market is now more exposed to the market downside than 20 years ago. The great unknown remains the credit crunch and its impacts on the wider economy. There is much talk of stagflation currently and the housing market faces both ways on how the economy moves – downward pressure on interest rates seems unlikely because of inflationary worries yet higher interest rates pose massive problems for borrowers with mortgages in terms of affordability and the more than a million households who annually renegotiate their mortgage terms when the product they have comes to an end.

6. CONCLUSIONS

The UK housing market is now in decline as measured by price change, volumes, lending, rising repossessions and market pessimism. This picture is not uniformly seen across the UK – Scotland has been to an extent insulated thus far, for example. Britain has contributed to the worldwide credit crunch, as a number of other nations have, by experiencing one (so far) cathartic banking collapse directly related to risky sub-prime undiversified lending. However, this was the fifth largest high street bank in the UK, a major employer in the North East of England and precipitated an unexpected run on the bank that threatened the financial system (or so it appeared at the time). The Government's decisions to underwrite savings and then to pump liquidity into the banking system (and then to bring Northern Rock into ownership under new management) were viewed by some as crisis management, by others as politics of failure and still by others as acts of extreme moral hazard – bailing out banks and propping them up through liquidity etc implies perverse incentives for risk taking by the banks.

What is to be done about the housing market? The UK housing minister recently (May 2008) arriving at a Government Cabinet meeting during which journalists clearly saw her briefing papers about the housing market on which it was said: 'we cannot know how bad it will get'. The lack of direction and indeed economic knowledge about such a fundamental facet of modern British life is of great concern. There needs to be a clear purpose to housing policy that works with the grain of the market and is socially and economically responsible and, indeed, fair.

In any market commentary, it is difficult to draw medium term conclusions when a market is on the cusp or at a turning point. There are many uncertainties. This paper urges caution in either making doom-laden predictions or in imagining that the market will rapidly and painlessly correct to a more stable footing. There are particular worries about the vulnerable consumer and the lack of a safety net but the key issue remains stabilising credit conditions in money markets which require both confidence-building and co-ordinated international action.

A longer period of flat or falling prices does create opportunities. Other things equal, this may, as in the case of mortgage tax relief, offer opportunities to develop fiscal instruments in housing markets that might help reduce damaging distortions and correct tax-induced inequities. A period of market stagnation should also be a period where policymakers think hard about the goals of housing policy and the required instruments to achieve sufficient supply to match housing demand change (building up from the sub-regional level to national aggregates) and develop an adequate evidence base to understand market dynamics better and the interactions, for instance, between market renting and owning. The aim of housing market policy should be sufficient quantities for occupational demand in a context where excessive price volatility is ironed out. Britain needs a more honest economic and political debate about the full set of instruments including taxes and planning policies that might secure such worthwhile objectives.

Staying on the same predictable path will not do. Continuing to facilitate a housing market which is under-regulated (apart from new supply) and wherein the implicit goals seems to be expansion of price and volume above all – will simply repeat the tragedy once more. Britain's problems with regard to the housing market are in part because of a reluctance to give up or even revise long standing political dogmas. The politics of normalising home ownership as an asset and a housing tenure are difficult, complex and long term – but now and the next few years will be an idea opportunity to make some much needed progress.

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