

The Rt Hon Sir Oliver Letwin MP
The Independent Review of Build Out

*c/o Ministry of Housing, Communities and
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The Rt Hon Sajid Javid MP
Secretary of State for Housing, Communities and Local Government
Ministry of Housing, Communities and Local Government
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9th March 2018

Dear Philip and Sajid

My terms of reference require me, by the time of the Budget in the Autumn, to “explain the significant gap between housing completions and the amount of land allocated or permitted in areas of high housing demand, and make recommendations for closing it”.

The output of new housing is determined by the number of homes permitted and the rate at which those permissions are built out. Successive governments have done much in recent years to increase the number of permissions granted by reform of the planning system and by introducing other measures to encourage local authorities to grant more planning permissions for new homes. I have decided to focus, in the first stage of my work, exclusively on analysis of the reasons why – against the background of the current planning system – build out rates are as they are, without yet making any recommendations for increasing such build out rates in future.

I have further narrowed my focus by considering exclusively the question why, once major house-builders have obtained outline planning permission to build large numbers of homes on large sites, they take as long as they do to build those homes. The many questions that surround the build out rates achieved by smaller house-builders and on smaller sites may well be worthy of investigation in due course; but the importance of the large sites and large house-builders to the overall house-construction numbers is such as to make it sensible for me to devote all of my attention to them at this stage.

I propose to publish the results of my analytical work by the end of June in the form of a Draft Analysis. This will contain only a description of the problem and of its causes. I will seek comments from interested parties and experts before I finalise this analytical aspect of my work.

On the basis of this careful approach to analysis of the problem, I hope to be able to formulate robust recommendations from the Summer onwards in order to produce a Final Report containing recommendations in time for the Budget.

So far, with my team of officials and with help from my panel, I have:

- visited large housing development sites in ten local authorities, meeting house-builders and planning officials;
- held round table meetings and individual meetings with stakeholders including land agents, house-builders, local authorities and NGOs; and
- reviewed the extensive material that has already been published about this problem.

Work on all of these fronts continues. Over the next twelve weeks, I envisage that we will:

- visit further large sites;
- obtain data showing the pipeline of large sites from application to completion on site;
- visit Germany and the Netherlands to examine ways in which build out rates are affected by the use of public or publicly-led mechanisms for increasing the variety of what is offered on large sites; and
- hold further meetings with stakeholders to test my diagnosis of the issue.

A point which has become abundantly evident from all of our work so far is that there are two distinct stages for building a large number of houses on a large site:

- Stage 1 (the ‘regulatory stage’) consists of securing all the necessary approvals to allow development to commence on at least part of the site.
- Stage 2 (the ‘build out stage’) starts at the moment when the house-builder has an implementable consent and is therefore able to start construction on the site (i.e. has received either the grant of full planning permission or the first final, detailed planning permission under reserved matters, and has satisfied all pre-commencement conditions).

We have heard from many witnesses that the rate of build out of large sites during Stage 2 is typically held back by a web of commercial and industrial constraints including:

- limited availability of skilled labour,
- limited supplies of building materials,
- limited availability of capital,
- constrained logistics on the site,
- the slow speed of installations by utility companies,
- difficulties of land remediation, and
- provision of local transport infrastructure.

Each of these reasons for a slow and gradual build out of large permitted sites deserves further investigation – and I intend, in the Draft Analysis, to provide an assessment of each of them. This will require further discussion with providers of the relevant items (e.g. training, building materials, finance, on-site utility-infrastructure) as well as further examination of the relevant data (e.g. on labour markets and building material markets) by the Treasury micro-economist that has been seconded to my team of officials.

But I am not persuaded that these limitations (which might well become biting constraints in the future) are in fact the primary determinants of the speed of build out on large permitted sites at present. They are components of the velocity of build out; but they are not the fundamental rate-setting feature.

The fundamental driver of build out rates once detailed planning permission is granted for large sites appears to be the ‘absorption rate’ – the rate at which newly constructed homes can be sold into (or are believed by the house-builder to be able to be sold successfully into) the local market without materially disturbing the market price. The absorption rate of homes sold on the site appears, in turn, to be largely determined at present by the type of home being constructed (when ‘type’ includes size, design, context and tenure) and the pricing of the new homes built. The principal reason why house-builders are in a position to exercise control over these key drivers of sales rates appears to be that there are limited opportunities for rivals to enter large sites and compete for customers by offering different types of homes at different price-points and with different tenures.

When a large house-builder occupies the whole (or even a large part) of a large site, the size and style (and physical context) of the homes on offer will typically be fairly homogeneous. We have seen examples of some variation in size, style and context on some large sites; but the variations have not generally been great. It has become apparent to us that, when major house-builders talk about the absorption rates on a large site being affected by “the number of outlets”, they are typically referring not only to the physical location of different points of sale on the site, but also and more importantly to differences in the size and style (and context) of the products being offered for open market sale in different parts of the site. Even these relatively slight variations are clearly sufficient to create additional demand – and hence additional absorption, leading to a higher rate of build out.

It is also clear from our investigation of large sites that differences of tenure are critical. The absorption of the ‘affordable homes’ (including shared ownership homes) and of the ‘social rented housing’ on large sites is regarded universally as additional to the number of homes that can be sold to the open market in a given year on a given large site. We have seen ample evidence from our site visits that the rate of completion of the ‘affordable’ and ‘social rented’ homes is constrained by the requirement for cross-subsidy from the open market housing on the site. Where the rate of sale of open market housing is limited by a given absorption rate for the character and size of home being sold by the house-builder at or near to the price of comparable second-hand homes in the locality, this limits the house-builder receipts available to provide cross-subsidies. This in turn limits the rate at which the house-builder will build out the ‘affordable’ and ‘social rented’ housing required by the Section 106 Agreement – at least in the case of large sites where the non-market housing is either mixed in with the open market housing as an act of conscious policy (as we have frequently found) or where the non-market housing is sold to the Housing Association at a price that reflects only construction cost (as we have also seen occurring). If freed from these supply constraints, the demand for ‘affordable’ homes (including shared ownership) and ‘social rented’ accommodation on large

sites would undoubtedly be consistent with a faster rate of build out. And we have heard, also, that the demand for private rented accommodation at full open market rents (the scale of which is at present uncertain) would be largely additional to, rather than a substitute for, demand for homes purchased outright on the open market.

So further questions arise:

- would the absorption rate, and hence the build out rate be different if large sites were ‘packaged’ in ways that led to the presence on at least part of the site of:
 - other types of house-builder offering different products in terms of size, price-point and tenure? Or
 - the major house builders offering markedly differing types of homes and/or markedly different tenures themselves?
- would the absorption rate be different if the reliance on large sites to deliver local housing were reduced? And
- what are the implications of changing the absorption rate for the current business model of major house-builders if the gross development value of sites starts to deviate from the original assumptions that underpin the land purchase?

As I continue my investigation into these questions over the next few months, I shall also investigate what constraints would be imposed on build out rates by the supply of finance, the supply of skilled labour, the supply of utility-infrastructure, the availability of building materials, and the management of site logistics if the fundamental constraints currently imposed by the absorption rate for the type and price of home currently being offered on large sites were lifted for any of the reasons to which the questions refer. I shall investigate what effect faster build out rates would be likely to have on the 'land banks' held by the major builders. And I shall continue to seek views from industry participants, planners, NGOs and others on the possible answers to the questions in order to deepen the analysis published in June.

Yours ever,

A handwritten signature in black ink, appearing to read 'Oliver Letwin', written in a cursive style.

The Rt Hon Sir Oliver Letwin MP

cc. Dominic Raab MP, Minister of State for Housing