Britain’s housing shortage disenfranchises the young. We should use the tax system to encourage people to free up larger homes.

Britain suffers from a chronic shortage of housing, which has dramatically increased land values. This has disenfranchised the younger generation, many of whom can no longer realistically expect ever to own their own home. The Intergenerational Foundation’s David Kingman argues that one solution is to use the tax system to encourage more members of the older generation to downsize into smaller properties, bringing more traditional ‘family homes’ onto the market, lowering the price through increased supply.

The scale of the problem – not enough houses are being built

For a number of years, the stock of housing in Britain has been increasing by less than 1% per annum, much slower than the pace of demand. There is no doubt we need more housing – and lots of it. The problem is the difficulty of achieving this goal in the short to medium term. Private-sector developers are in a parlous state at the moment and have never managed to consistently build the level of houses required to meet demand in the post war era. The other main obstacle is that house-building is incredibly unpopular with existing homeowners. In response to the coalition’s draft National Planning Framework (NPPF), the Daily Telegraph launched its “Hands Off Our Land” campaign, with official support from the National Trust, English Heritage and the Campaign for the Protection of Rural England.

This is despite the fact that the current NPPF is unlikely to kick start house-building to the extent needed. Meanwhile, 2010 saw just 134,000 new homes built in Britain – the lowest number constructed in a single year since World War Two – while 230,000 new households are formed annually, worsening the shortfall.

Importantly, there is a very strong intergenerational divide in terms of home ownership. The baby boomer generation (those born during the prolonged spike in Britain’s birth rate between 1946 and 1964) was able to benefit from decades of government policies which explicitly encouraged homeownership. This period saw the mass building of new houses throughout the 50s, 60s and 70s as the baby boomers came of age, while they had the benefit of schemes like Mortgage Interest Relief at Source (MIRAS) (which allowed borrowers to claim tax relief on their mortgage interest from 1969 until the scheme was ended in 2000) and the 1959 Housing Purchase and Housing Act, which provided £100 million in loans for individuals who wanted to renovate older properties.

In the 1980s, many of them who hadn’t previously owned their own property benefitted from the Right to Buy, and there is ample evidence that the decline in new housing development since has created an unprecedented boom in house prices. Collectively, members of this generation own 40% of the nation’s £2.5 trillion pounds of property wealth, while one in five baby boomers owns a second home.

This is not necessarily problematic on its own. However, underpinning this issue is rising life expectancy. The baby boomers have also been the beneficiaries of enormous rises in longevity. In previous eras, our lack of new housing development would have been less of a problem because people occupied the property they owned for a shorter period of time; couples were likely to purchase their family home in their 20s or 30s, see their children move out when they were in their early 50s and then not live too far beyond their 60s, bringing family homes back onto the market more quickly when they were sold off by the children who’d inherited them.

As we have seen, house-building has slowed down to such an extent that this trend is effectively denying young people access to the nation’s limited stock of family homes. Statistical evidence bears witness to this: between 1991 and 2010, rates of owner-occupation fell 30% in the 25-34 age group and 13% among those aged 35-44. By contrast, owner-occupation increased by nearly 20% for those aged 65-74.

As older people usually don’t have children living with them this represents an inefficient use of the housing stock. Our report found that Britain’s houses contain the equivalent of 25 million unused bedrooms, mostly belonging to pensioners and pensioner-couples who have continued to live in the family home after all their children have moved out. If a significant proportion of these could be brought back onto the housing market where young families could access them, it would go a long way to address Britain’s present shortage of housing space.
Taxing larger homes is a solution

The key issue here is that if Britain is not going to solve its housing shortage by building new homes alone then it must achieve the most efficient possible allocation of its existing housing stock.

However, the large-scale occupation of large houses by small households represents an inefficient allocation. The current tax system makes this more likely – as you are taxed proportionally less the more housing space you use. The tax system could be altered in several key ways to put a price on this inefficiency and encourage older households to downsize into smaller dwellings:

- Abolishing stamp duty on people moving house to downsize
- Abolishing the council tax concessions for single occupation
- Introducing a property value tax, based on the size of homes

It should be pointed out that none of these changes would be targeted exclusively at members of the older generation; younger people using housing space inefficiently would be affected by them just as much, while older people already living in small houses would not be affected.

We are aware that the report has been misinterpreted in some quarters as calling for older people to be “forced” out of their homes; it should be emphasized that there is no question of coercing people to do anything they don’t want to do. Rather, our suggestions rely on “nudge” economics; they attempt to gently discourage people from doing something by a putting a price on it. The main recommendation, after all, is actually a tax cut for older people! The fact that young families are shut out of the housing market has economic costs, and all these proposals would do is offset some of them while attempting to improve the situation.

Our suggestions are not a panacea. Downsizing has advantages for the older generation, particularly lower energy bills and easier household upkeep, but in some areas a lack of houses that are the right size (especially bungalows) are holding people back. There is also, in the short term, a problem with the availability of mortgages for young people which is making it harder for would-be downsizers to sell their homes on to them, but conditions in this area will likely improve in the next few years. In the future downsizing options may well expand on a larger scale so we could move closer to the US experience, where downsizing is much more common.

What our solution does offer is an analysis of the demographic dimensions of the problem, along with a remedy which would directly address one of the main demographic drivers of inefficient housing use and pressures on housing demand. It would be irresponsible to pretend that we can deal solely with the problem through house building. Surely alternatives are worth exploring further.

A PDF of the full report is available online on the Intergenerational Foundation website.