

Housing and construction: a troubled relationship

Housing construction is the neglected part of housing policy. The Foundation's Housing and Construction Research Programme concludes that housing market structures and volatility, together with the internal workings of the industry, lead to low investment, low productivity and high costs in both new home building and in repair and maintenance. In a review of the programme, Professor Michael Ball of South Bank University found:

- f** **New housing investment in the 1990s has been the lowest over a five-year period since the Second World War and is far less than in other major economies. It shows no prospect of increasing despite the fact that demand over the next decade is likely to be far higher than current supply.**
- f** **Volatility in the UK housing market - much greater than in other industrialised countries - impairs the efficiency of the industry, making it difficult to make long-term investments in things such as training.**
- f** **UK housebuilding techniques are labour-intensive and innovation is discouraged.**
- f** **Homes must last much longer with greater flexibility of use than current designs generally allow.**
- f** **Expenditure on housing repair and maintenance is now almost twice as great as new building though its distribution across the stock is uneven. The repair industry, particularly for private housing, is fragmented, technically backward and lacking in business skills.**
- f** **Subcontracting, although an efficient use of labour, creates problems for innovation and training. The numbers of apprentices and trainees are falling. Site-based training is becoming increasingly rare.**
- f** **Building is less flexible than is generally believed. Firms, subcontractors and workers are active only within limited areas of expertise. New small firms have great difficulty starting up, particularly minority ethnic group contractors.**
- f** **Social housing is now frequently built using design-and-build contracts which has significantly changed its relationship with the building industry.**
- f** **The researcher concludes that the result is a housing supply industry that produces over-standardised, high-cost homes; one which can only respond weakly to variations in cyclical demand and preferred housing requirements.**

A vicious circle

There is no evidence to suggest that most participants in the building industry - firms, subcontractors and building workers - are individually failing. Individual efficiency and competitive forces are generally high. But the economic and industrial structures within which they work lock all of the industry into a cycle of low investment, low productivity, low training, low innovation and poor value-for-money in contrast to the situation in many countries in Europe and North America. A series of market processes and failures have trapped British housing construction into this situation. Addressing some of these issues would help shift the industry onto a more productive plane.

Low housing investment

New housebuilding has declined for over 35 years, with some temporary surges. Council housebuilding has declined the most but private sector housebuilding has also diminished. Because of the sharp fall in social housebuilding, the biggest losers have been households with below average incomes and those wanting rented housing, although everyone faces higher housing costs, less flexibility and poorer value for money.

One result of low housing investment is that houses are expected to exist for hundreds of years, rather than for their design life of about sixty years. So housing has to last much longer and be more flexible in use than it is designed to be. Mismatches between consumer needs and the housing stock are consequently likely to grow. A backlog of replacement is also mounting.

Prospects of strong housing demand

Excessive pessimism about the state of future housing demand has been engendered by the current problems of the owner-occupied market, which in time will disappear. There are prospects of strong demand over the next decade for both rented and owner-occupied housing. Present shortages, greater household numbers and a higher level of replacement will more than absorb today's output. But the greatest stimulus to housing demand will be rising living standards, once the current housing market recession has worked its way through. How much people will be prepared to pay for better housing standards over the next decade may rise by up to twenty per cent, driven by increases in real incomes. The resultant search for higher quality living space will intensify the demand for new housing and put pressure on prices.

Other major economies invest far more in new housing than does the UK, and have lower market volatility. Since the early 1980s, new housebuilding

(both social and private) in the UK has probably been the most volatile of the industrialised nations. It is over three times more volatile than in France or Germany. Volatility has considerable adverse consequences on how much firms are willing to invest in the business of housebuilding and how willing workers are to acquire housebuilding skills and remain in the industry. It is a major cause of the low productivity trap the industry is caught in.

If housing output was more predictable, say by the government having a credible national housebuilding target, there would be considerable long-term productivity gains - bringing the UK closer into line with housebuilding productivity elsewhere.

Repair and maintenance

Expenditure on repair and maintenance is now almost twice as large as that on new building although there are substantial pockets of dilapidation. Many private owners do not maintain their housing adequately. Too much is being spent on repairing some rundown council estates and on some private sector dwellings rather than rebuilding. Yet there is no systematic evaluation of the best relationship between new building quality, subsequent maintenance and replacement. Pressures in the private and social housing markets suggest that there are significant biases against building in minimal maintenance for new homes, against repairing many houses to an adequate standard, and against replacing outmoded, expensive-to-repair dwellings by new ones.

The repair industry, particularly for private housing, is fragmented, technically backward and lacking in business skills. Private repair and maintenance is dominated by small undercapitalised firms which do no training. Reputable firms face problems combating 'cowboy' firms that charge no VAT. Governments and homeowners effectively condone poor quality work.

The organisation of production

There have been many changes in the organisation of production, among the key ones being:

- The wholesale switch from traditional contracting to design-and-build in social housing has produced cost savings and reduced risks, but has also had several bad effects.
- Training has declined with the growth of subcontracting.
- It has become more difficult for small firms to set up and prosper in housebuilding.
- Innovations are reduced by firms out to limit risk.

In speculative housebuilding for owner-occupation, production costs are only one factor affecting firms' profit-making calculations. Fluctuating sales, attempts to reduce working capital tied up mainly in land holdings, and the land development process all mitigate against using the lowest cost building techniques and against innovative practices.

Sharp increases in land prices at times of rapid house price inflation destabilise the housebuilding industry because the subsequent collapse of the land price results in firms having to reduce the value of their assets in the balance sheets and can lead to bankruptcies. Companies try to avoid land losses but at the expense of continuity in production.

The industry responds very slowly to increases in real house prices. A one per cent increase in house prices in the second half of the 1980s only increased new building by 0.16 per cent on average. One reason for this is that housebuilding has to compete with non-residential private sector building for its labour, plant and materials. Since the mid-1950s, the two sectors have tended to move in opposite directions: housing output has declined when non-residential private sector building - shops, offices, factories and other commercial buildings - has grown, and vice versa. This suggests that house building is crowded out by other private sector work.

Competition in new housebuilding, social and private, is often competition between a few contractors in any locality. This may have detrimental effects on price and quality.

The common image of building as a highly flexible and mobile industry is false for most of its activities, including housing. Specialist skills are needed and these are not always transferable between types of construction work. In addition, reputation, market positioning and the need for detailed local information induce firms and others to stay in the areas of work they know best. This accounts for the much sharper fluctuation in prices than outputs.

Because of undercapitalisation, generally poor business and estimating skills, and difficulties in plugging into local networks, new small firms have great difficulty starting up. The problems are worst for minority ethnic group contractors. Even housing associations, whose expenditure has often been targeted at deprived inner city areas, have not employed many firms from minority ethnic communities.

Labour and training

Even at today's low housebuilding levels, firms are having problems attracting enough skilled labour. Any major upturn in housebuilding (or in repair and improvement) is likely to be constrained by labour

shortages. Construction training in Britain is generally of lower standard than in leading continental European countries. Skill shortages also act as a barrier to innovation. The types of training in Britain are based on the labour requirements of the simple techniques currently used in housebuilding - advances in technique would require a wider range of skills.

Policies to boost employment

Using local housing expenditure to draw the long-term unemployed into construction produces limited successes. Even if the schemes were better targeted they are unlikely to place many unemployed people in jobs.

Similar problems arise with national programmes to reduce unemployment through more housing work. These only succeed if the unemployed are already committed to the building industry. Maintaining employment in the building industry in recessions through targeted housing policies and raising its long-term capacity to build and repair houses is likely to have far more impact on employment as well as producing substantial efficiency gains.

Main policy recommendations

The report argues for the need for more investigation and for reforms in five areas of the housing supply process:

Housing output and market efficiency

Government should aim to bring housing investment volatility more closely in line with that in other major EU countries. This would enable the housebuilding industry to invest more and improve its efficiency. To achieve this, governments should intervene in the social housing and the owner-occupied market to adjust for cyclical swings. Housing production subsidies (such as Housing Association Grants and improvement grants for home owners) should be increased and where possible operated in a counter-cyclical manner.

Housing quality and repair and maintenance

Building regulations should be toughened, or subsidies offered, to increase initial housing quality and design flexibility to minimise the expenses of subsequent repair and adaptation to changing household needs. The introduction by some housing associations and planning authorities of a requirement to build to the Lifetime Homes standard developed by the Joseph Rowntree Foundation is one possible step in this direction. The repair and maintenance industry needs a range of reforms

including quality of work warranties, better training and improved information, a stronger role for trade bodies and less or no VAT on this work.

Organisation of the industry

The relationships between firms, and between firms and their clients, need to be improved, emphasising the benefits of co-operation without compromising general market competition. Changes in permissible market structures and contracting arrangements, some of which have already been suggested by the Latham Report, are necessary to achieve this. The role of design-and-build contracts needs to be subject to detailed enquiry, taking into account the wider effects of how they are used as well as the direct impact on the cost and quality of social housing. Local competition between housebuilders should also be subject to investigation and mechanisms put in place to avoid potential market abuses.

Innovation

Consumer conservatism needs to be overcome with government sponsored warranties and information campaigns. Financial incentives should be devised for housebuilders and materials producers to encourage them to innovate and to co-operate over finding improvements in housebuilding methods.

Labour markets

Setting and credibly sustaining a housebuilding target would greatly increase quality employment in housebuilding, and is the best strategy for increasing long-term employment opportunities through housebuilding. Training initiatives have to be enhanced to cope with existing labour shortages and future needs.

About the study

Over the past three years, academic researchers have been working on six independent projects in the JRF's Housing and Construction Research Programme. The projects have covered housing investment levels; small firms repairing private housing; housebuilders and subcontractors; building techniques and training; minority ethnic contractors and housing associations; and local housing expenditure initiatives to help the long-term unemployed. This overview report uses the results of this research and previous research on the industry to present an in-depth assessment of housing supply.

Further information

The full report, *Housing and Construction: A troubled relationship?* by Michael Ball, is published by The Policy Press in association with the Joseph Rowntree Foundation (price £11.95).

Related Findings

The following *Findings* look at related issues:

- 140** Creating local jobs from construction expenditure (Mar 95)
- 143** Housing associations and minority ethnic building contractors (Jun 95)
- 163** Improving the efficiency of the housing repair and maintenance industry (Nov 95)
- 172** Skills and the construction process (Mar 96)
- 173** Housing investment: lessons for the future (Mar 96)

For further information on these and other *Findings*, contact Sally Corrie, Publications Officer, on 01904 629241.



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