

Levelling up the Green Book Stage I

A Cebr report for Homes for the North Executive Summary



Introduction

This report sets out the findings and recommendations of an initial stage of work that was commissioned by Homes for the North (H4N) to review the Government's appraisal process in relation to housing investment, with a view to examining whether there may be systematic biases with regional effects.

The key tasks that we have undertaken include:

- ▶ a review of the Treasury's Green Book and the guidance derived from it, together with the practical funding arrangements that are in place;
- ▶ a round table with H4N senior leaders to build an effective joint understanding of the issues;
- ▶ engagement with departmental officials and political advisers to build an understanding of the arguments that are likely to be persuasive to Government and the key opportunities for exerting influence with the Government;
- ▶ recommendations for the Government's Green Book review and related policy agenda;
- ▶ next steps for H4N research in this area.

Green Book principles

The Treasury's Green Book forms a core pillar of the Government's guidance on the use of public resources. Its purpose is to help officials develop transparent, objective, evidence-based appraisal and evaluation of proposals to inform their decisions.

Green Book principles are used at various stages of decision-making, from Treasury's spending review process, to individual policy ideas and the allocation of funding for individual schemes within the Government's investment programmes.

The DCLG Appraisal Guide, which was published in 2016, stands alongside the Green Book and provides detailed guidance on appraisal to inform decisions in relation to housing related investment.

The theory that underpins the Green Book and the various supplementary guides is drawn from welfare economics and involves comparing the 'social utility' of alternative courses of action. In principle, this provides a holistic means of considering the overall net impacts of a proposal or scheme on society as a whole, although this depends on all the relevant impacts being captured, which can be a significant challenge in practice. While the overall approach is neutral about the distribution of effects, these considerations can be factored in.

The case for intervening rests on demonstrating a scheme's 'additionality' – the impacts after displacement (crowding out of equivalent effects in other locations) or deadweight (impacts that would have happened anyway) are netted out.

Demonstrating value for money in housing investment appraisal

Land Value Uplift (LVU) is the core measurement that the Government expects to be used in appraising the value for money of housing projects. LVU is related to a residual land value that would typically be estimated in a standard development appraisal and which represents the price a developer is willing to pay for a parcel of land.

LVU is the residual value of land less its value in its existing use, e.g. agricultural or industrial. It represents the additional value of the change in use of a parcel of land that markets are able to capture, i.e. the benefits from moving to an economically more productive land use.

LVU does not necessarily capture all the economic, social and environmental impacts of such a change – only those that are reflected in market prices. The Appraisal Guide also recognises costs or benefits that fall on other people or on the rest of society at large.

The job of the appraisal is to identify a strategic case for intervening only where it is necessary. This rationale for intervention will usually be to correct a market failure, although the aim could also be redistribution in some cases. This means understanding the additionality of any housing investment is a crucial part of the analysis and the Appraisal Guide suggests applying a set of criteria to determine an additionality rate. The criteria include the strength of the market failure that forms the rationale for intervention, whether the intervention is demand or supply focussed and the stage in the housing cycle at which the intervention takes place.

A structural shift of investment away from the North

Recent experience of funding decisions suggests the current system is not working well for the North. Research by North Housing Consulting Limited,¹ commissioned by Homes for the North, found that in 2017/18, the North received just 17.8% of housing funding across the UK, despite having 23.3% of the population. Moreover, recent changes to the allocation rules for five housing supply programmes² mean only four of 72 local authorities in the North are eligible for 80% of the total in England. By way of example, the Government has so far committed just 9.9% of the total available through the Housing Infrastructure Fund (HIF) Forward Fund to the North (£340.7m of £3.427bn across five schemes).

1 North Housing Consulting Limited, March 2020, The Spatial Distribution of the Housing Infrastructure Fund and its impact on the North: Post Budget Review March 2020
2 The funds were: i) the Housing Infrastructure Fund (Forward Fund), ii) Estates Regeneration Fund, iii) the short-term Home Building Fund, iv) the Small Sites Fund, v) the Land Assembly Fund

Improving the Current Approach

What others are saying

We have reviewed recent work by the UK2070 Commission, academic commentators, industry bodies and think tanks. This shows that there is an emerging consensus that the current system is not fit for purpose in the context of the emerging regional policy agenda. Some key themes include:

- ▶ There has been a historic regional imbalance in infrastructure investment. Rather than being seen as a means of unlocking economic potential, it has been targeted at helping already high productivity areas grow faster;
- ▶ This reflects a piecemeal approach to addressing regional inequalities. To make a meaningful difference, a comprehensive, long-term approach is needed;
- ▶ Housing should be treated as economic infrastructure and policy should be devolved to a more local level;
- ▶ A greater emphasis on strategic spatial planning is required and funding decisions should be better linked to it;
- ▶ Current appraisal techniques are not seen as fit for purpose to meet these challenges and require development in key respects. Often the most measurable metrics are accorded a greater weight than equally important but less easily quantifiable ones, e.g. with those capturing market prices often outweighing more diffuse social impacts.
- ▶ There are variations in promoters’ ability to produce appraisals to a standard that will support successful funding bids, and this may systematically skew funds away from some areas and regions.

Recommendations to Government

Despite the North being home to 28% of the English population, the Government’s funding rules mean that just four of its 72 local authorities are eligible for the bulk of the public sector investment aimed at increasing housing supply. These funding rules are separate from the appraisal process, and in effect override it by ringfencing funding pots for particular areas. Replacing them with a rational system of allocation based on sound appraisal principles is a top priority.

Recommendation I: remove the 80:20 funding rule and identify a more strategic method for the geographical allocation of Homes England funding aligned with national objectives.

Having the right investment programmes in place

There is a limit to the ability of scheme level appraisal alone to bring forward investment that aligns with overarching regional policies. A strong strategic case also needs to be made to influence decision making at the programme level in order to make the design of new housing policy consistent with other policies associated with the Northern Powerhouse and Levelling Up agenda etc. Public investment in housing needs to be more integrated with broader policies to enable housing to play its full role in unlocking economic potential across the country.

Recommendation II: develop the levelling-up concept into a more specific and measurable strategy (eg a Northern Powerhouse Strategy) around which convincing strategic cases can be developed, which cover a range of sectors

Developing a housing specific regional rebalancing toolkit

The emerging understanding of the role of housing in helping drive transformational economic change in the North of England needs to be translated into a resource that can be used by scheme promoters in the North to articulate a consistent and persuasive strategic case for their proposed housing schemes.

As well as providing an evidence base to help scheme promoters demonstrate the contribution their scheme can make to meeting broader regional development objectives, this should be a practical resource to help them produce consistent, high quality strategic cases, to help level the playing field in terms of the capabilities and resources of scheme promoters in different parts of the country.

Alongside this, there may be a need to focus on strategic case making capacity building, with consideration given to opportunities for pooling resource across local authorities and other strategic partnerships to write better quality appraisals and funding bids.

Recommendation III: develop a strategic case making toolkit to help promoters of housing schemes produce consistent, high quality strategic cases

Consistency between economic and strategic case making

Current appraisal guidance prevents the economic case from reflecting any transformational change that is included in the strategic case. In particular future land values take current values and applies a uniform growth rate across the country, in effect fixing the existing relativities between different locations.

As a result, the approach takes account of past trends and no account of any future departures from trend that, for example, regional policies might bring about. It is in effect therefore a backward-looking approach that could be in conflict with the objectives of the strategic case, e.g. if these are based on changing the trajectory of economic performance of particular areas.

Recommendation IV: reform guidance on future land value assumptions to be used in appraisal of schemes that form part of transformational investment programmes

Funding rules

Increasing
transparency
around
additionality

Intuitively, the higher the land value uplift, the more likely that a development could be funded privately. Where other constraints are present in high demand areas, such as local planning decisions serving to hold back housing supply of otherwise viable housing schemes, then a different approach might be needed to increase housing supply. This would suggest a policy design flaw resulting in poor value for money.

If LVU is not adjusted for additionality appropriately, it can be assumed that the generally higher level of land values in the south east and London will skew funding away from the North and other areas with lower land values. There is already evidence that funding is flowing away from the North, either by design due to the 80:20 rule or through the inherent bias in the decision-making process which fails to measure additionality well and subsequently follows existing land values somewhat blindly.

Recommendation V: research should be focussed on improving the evidence base for additionality rates so that future guidance can demand greater rigour. In the meantime, provide greater transparency over how additionality rates have been estimated in real investment decisions

Developing
the evidence
base around
externalities

While the Appraisal Guide recommends that the external costs and benefits of housing investment are included in calculations of value for money, many of them are poorly understood and do not have robust data or an evidence base to support the monetisation of the costs and benefits. This means that in practice appraisal results are typically dominated by the LVU measure and the effect appears likely to disadvantage regions of the country with lower land values.

There are a number of strands of research that could usefully be undertaken to extend the evidence base that is available for MHCLG guidance to draw on. We see priority areas of work as:

- ▶ impacts on quality of life associated with changes in local population, both positive and negative;
- ▶ the environmental impacts of new housing and implications of transition to net-zero;
- ▶ the value of housing investment in terms of its contribution to public realm and shared spaces, the quality of the local built environment and its impacts on overall perceptions of place level quality;
- ▶ the health and wellbeing effects of poor housing.

Recommendation VI: support further research to develop a better evidence base about the values of positive and negative externalities associated with housing investment

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Homes for the North is an alliance of 17 housing associations who want to deliver more homes across the North of England. Collectively members already provide homes for almost one million people in the North of England but want to do more.

Homes for the North commissions research and shares expertise and best practice to inform policy makers regionally and nationally on creating the conditions for more and better homes, extending home ownership in the North and making the North of England a more attractive place for businesses to invest.

Get in touch

Hugh Owen

Call: 07980 761716

Email: hugh.owen@riverside.org.uk

Ian Birch

Email: ibirch@cebr.com