Home economics

Financial policies to increase homeownership

Gideon Salutin

SMF Social Market Foundation

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Each of the reports is a comparative study of housing policy internationally, drawing on a combination of over 20 expert interviews and a literature review. There is a particular focus on Australia, Canada, Ireland and New Zealand in this study, although other case studies are used where relevant. As English speaking, liberal market democracies, they share many of the same challenges that the UK faces in its housing sector, and so solutions found there are especially instructive.

This series of reports covers the following topics:

- An introduction to housing
- Planning reform
- Affordable housing (social housing and co-operative housing)
- Homeownership policies
- Renting

ABOUT THE AUTHOR

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Gideon is a Senior Researcher at the SMF. He joined the research team in August 2022 having previously worked as a policy researcher and writer. His research portfolio focuses on environmental policy, poverty, and inequality.

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FOREWORD

People below the age of around 50 today have had a starkly different experience of the housing market from those above that watershed age. In 2002 alone, when today's 50-year-olds were approaching typical first-time-buying age, house prices grew by an astonishing 28%. This was part of a dizzying mid-2000s price surge that saw them transition from their late 20th century norm of around 4.5 times average earnings to a multiple of around 8, where they have broadly remained ever since.

By making it harder to save for a deposit and sucking in a much larger proportion of their lifetime savings, eye-watering house prices for would-be buyers have been the most obvious and unjust manifestation of intergenerational inequity.

But high prices were not the only – and perhaps not even the main – cause of the dramatic fall in home ownership in recent years. The ownership rate drifted down from a peak of almost 71% in 2003 to just under 70% on the eve of the financial crisis in 2007, before collapsing to 62.6% by 2016, even as house prices fell sharply relative to incomes.

The less obvious force at work was a sharp retrenchment of high loan-to-value lending. Radical changes in how the mortgage market operates – due to a combination of more conservative lending practices and new regulations on lenders – played a central (if not starring) role in the home ownership recession. While first-time buyer mortgages typically required a 5 per cent deposit in the 1990s, that proportion jumped as the financial crisis struck. And despite having recovered somewhat, it has remained at around 15 per cent ever since. This development alone would have tripled the deposit constraint on first-time buyers even if prices had remained at relatively affordable 1990s levels.

In place of risky first-time buyers, landlords stepped in to borrow money, buy houses and rent them to would-be owners. Even those first-time buyers lucky enough to be able to get a mortgage in the 2010s found themselves paying vastly higher interest rates than wealthier borrowers. These developments doubled the size of the private rented sector and tripled the number of families with children living in it over the course of a decade.

This report highlights how these two adverse trends – in prices and lending practices – lie at the heart of the home ownership policy challenge. In response it makes a comprehensive range of proposals that could move the needle, even in a world where house prices remain high.

Introducing a permanent mortgage insurance scheme and fostering a market in long-term fixed rate mortgages would finally begin to rebalance the unequal access to mortgages that young people have struggled with since the financial crisis, and which has only exacerbated intergenerational inequality. These measures, common elsewhere in the world, would allow more lending to young people without jeopardising financial stability. Meanwhile, developing innovative ways to help renters save for a deposit could further ease the barriers that have seen hundreds of thousands of them locked out of the mortgage market.

Today there are 1.5 million fewer owner occupier households in England than there would have been had the home ownership rate remained at its 2003 peak. While such a large shortfall remains this issue will remain high on the policy agenda. But to make progress, policymakers need to tackle the underlying problems in the mortgage market that put young people at a disadvantage. This report shows the kind of bold thinking that will be required.

Ian Mulheirn

Economist

EXECUTIVE SUMMARY

The homeownership dream is a constant for millions in the UK, and affects other aspirations including career goals and family planning. Homeowners avoid monthly rents, gain a viable alternative source of income, and build a nest egg to pass on to their loved ones. However, rising prices over the past 30 years have meant the homeownership dream will remain just that for millions of households.

Britain is not alone in this experience. People in Australia, New Zealand, Canada, and Ireland each feel similar draws to homeownership and first time homeowners in each of those countries are met with similar barriers. The following report surveys homeownership challenges and policies in each of these countries to understand what has gone wrong in the housing market and how it might be improved.

Since 2008, the British government has pursued two major policies to help people get onto the housing ladder. The first was to introduce home savings accounts in the form of Lifetime Individual Savings Accounts (LISAs). This was designed to protect income from taxation and be withdrawn only for major purchases including homeownership. The second was the introduction of the Help-to-buy equity loan, which provided an interest-free loan to mortgage applicants for the first five years of their mortgage to help buyers afford a deposit. Both policies helped some households save for a deposit, particularly those with strong incomes looking to buy in relatively affordable regions, but they have failed to increase homeownership in areas of high demand.

The following report recommends alternative policies. For first time buyers, buying a home requires three elements: a deposit, mortgage payments, and tax payments. Policies to address each of these elements are outlined in the below report, with a section devoted to each.

Deposits pose a massive barrier to home purchases for first time buyers. Since the Great Financial Crisis, deposits demanded for home purchases have increased. This was done to secure investments and avoid the risky lending which preceded the financial crash. Deposits worth less than 25% of the property accounted for 51% of all loans in 2007 yet have now fallen to just 27%. For first time buyers, the average deposit was worth £16,400 in 2007, yet today is worth £50,051, nearly doubling when accounting for inflation. This means buyers take a longer time to save for deposits, increasing buying ages outside of London from 29.7 in 2007 to 33.4 in 2022. This crunch has been compounded by rising prices, which have nearly doubled price-to-income ratios in the UK, further pushing up deposit requirements, and compounding with increasing interest rates for high loan-to-value (LTV) loans. While this is done to reassure private banks and secure home loans, other countries in the Anglosphere provide inclusive alternatives which do not sacrifice financial security. Canada's system of mortgage insurance, which insulates home loan defaults from the wider market, allows for cheaper deposits, and was credited as one factor contributing to Canada's status as one of the most resilient economies to the global financial crisis.

Monthly mortgage payments, in contrast, presents less of a strain on household finances, yet the loans mortgage holders receive can be dangerous both for their financial wellbeing and the safety of the wider economy. British mortgages are less likely to be long-term fixed rate than those in peer countries, endangering stability by making more homeowners vulnerable to rapid interest rate rises. Alternatives to this system are available, including shorter mortgages on longer fixed-interest deals, as are common in the countries surveyed.

Finally, tax payments present the final hurdle for British homeowners, who pay stamp duty upon the purchase of a property and ongoing taxes alongside them. The UK currently has the highest home taxes in the Anglosphere as a proportion of GDP. But these are not evenly distributed. Upper income households tend to spend less as a proportion of their income than lower income households, obstructing homeownership for the middle class. Our recommendations would reverse that, making home taxes more equitable, and turning council tax into a vehicle to bring renters closer to homeownership, rather than further away, by directing half of private tenants' council tax into a personal home deposit savings account. Additional taxes on foreign ownership, vacant homes, and house flipping could provide new revenue for the government.

It is important to note that this report does not deal with the issue of supply. While we agree that supply must increase, other reports in this series detail this issue and how it can be addressed. Instead, this policy looks specifically at homeownership policies, particularly in the mortgage market, to recognise where policy has failed, and finding alternatives in comparable countries where policies have succeeded.

The following report breaks each of these down in turn, looking at how changes to financial regulations for first-time home buyers can increase access to homeownership. Our policy recommendations include:

Table 1: SMF's policy recommendations for increasing access to homeownership

Challenge for policymakers	Recommendations
Lower deposits and increase security	Allow insurers to provide mortgage insurance for high loan-to-value mortgages as an alternative path to homeownership
Make mortgage payments more stable	Allow lenders to offer fixed rates for entire 30 year terms as well as 15 and 10 year terms by altering affordability requirements and encouraging demand by mandating greater information for mortgage applicants
More equitable property taxes	Replace council tax with regular taxation from councils based on property values re-evaluated every three years.
	Direct half of private tenants' council tax payments into a home deposit savings account to be used when purchasing a home
	Abolish stamp duty and make up revenue by decreasing capital gains exemptions for secondary properties
	Introduce 'housing sin taxes' including foreign buyers taxes, vacant home taxes, and taxes on house flipping

Source: SMF

CHAPTER ONE – INTRODUCTION

Before the Great Financial Crisis (GFC) cheap money, weak regulation, and a decline in insurance underwriting standards gave millions of Americans access to home loans. But when mass defaults on these loans crashed the financial market, strict regulations were brought in place to prevent the crisis repeating. These barriers are now preventing access to housing even for aspiring homeowners who could safely be relied upon for mortgages.

The danger of lowering barriers to home ownership is clear. In the GFC, low income households defaulted on their mortgage debts taken on through exploitative subprime loans. When interest rates rose and homeowners defaulted, a cascade of risky investments in the market led to the greatest market crash since the Great Depression.

This paper is one of a series in which researchers undertook a literature review to evaluate housing policy in the English-speaking world, including Australia, New Zealand, Canada, and Ireland. The literature review was combined with quantitative analysis of relevant statistics and administrative data in each country. Desk research was complemented by semi-structured interviews with policymakers, researchers, and advocates to understand how policies were designed and implemented, how they affect mortgage availability, and whether they had a positive effect on lived experiences. For more detail on our methods, see our introductory paper, "Dwelling on it."[1]

The UK needs policies that improve access to housing while protecting against the risk of defaults, predatory lending, and financial fallout. We argue that this is not a dichotomy. Widening homeownership by supporting aspirant homeowners is possible at the same time as protecting individual financial security and the global economy. The Anglosphere demonstrates ways Britain can protect the interests of both, and each is discussed in turn.

It should be acknowledged that homeownership will remain out of reach for many British households as long as home prices remain high. As such, policies should be introduced to restrain price growth. These policies include supply-side interventions to boost British construction, including planning reform, demand-side interventions including regulation, or by increasing social and co-op housing. These policies are discussed in detail in other papers within this series.

CHAPTER TWO – SAFER AND CHEAPER DEPOSITS

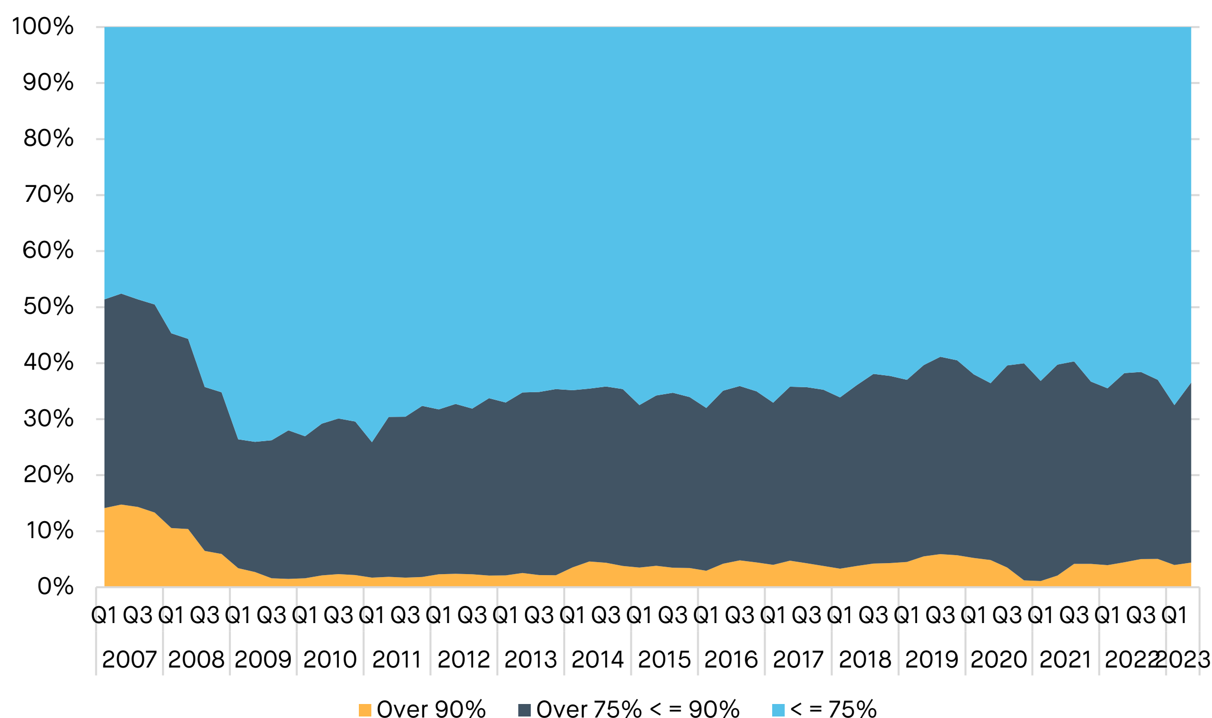
Since 2008, deposits have been the most often cited barrier to homeownership by the annual Building Societies Association (BSA) property tracker.[2] These were surpassed only briefly in the outbreak of COVID-19 in 2020 by worries over job security and more recently by concerns over monthly mortgage payments, likely caused by today's high interest rates. As interest rates fall, deposits are likely to again be the primary factor in obstructing access to homeownership.

British lenders demand large deposits, and these are getting larger

Deposits and monthly payments have an inverse relationship. The more a purchaser pays in their deposit the less they will owe on their mortgage. For instance, if someone pays a 25% deposit, they will then pay 75% of the loan on their mortgage, plus interest. The proportion of one's loan to the home's total value is known as a Loan-to-value (LTV) ratio, and in the previous example would be worth 75%. The higher the LTV, the lower the deposit, which typically means higher interest rates, since the lender is putting more money at risk. That explains why smaller deposits come with higher payments.

Deposits have been particularly high since the GFC due to the regulatory responses to the crash. After the crash, better reinforced lending standards led to higher deposit rates. In 2007, 14% of mortgage lending involved deposits of less than 10%, while 6% involved deposits of less than 5%. Sub-10% deposit rate lending declined to a low of 1.5% in 2009 as banks cracked down on risky loans. Over the next decade high LTV lending crept back up to 6% on the eve of the pandemic, when a similar shock followed by higher interest rates forced the number down to around 4%.

Figure 1: LTV as a % of gross advances over time

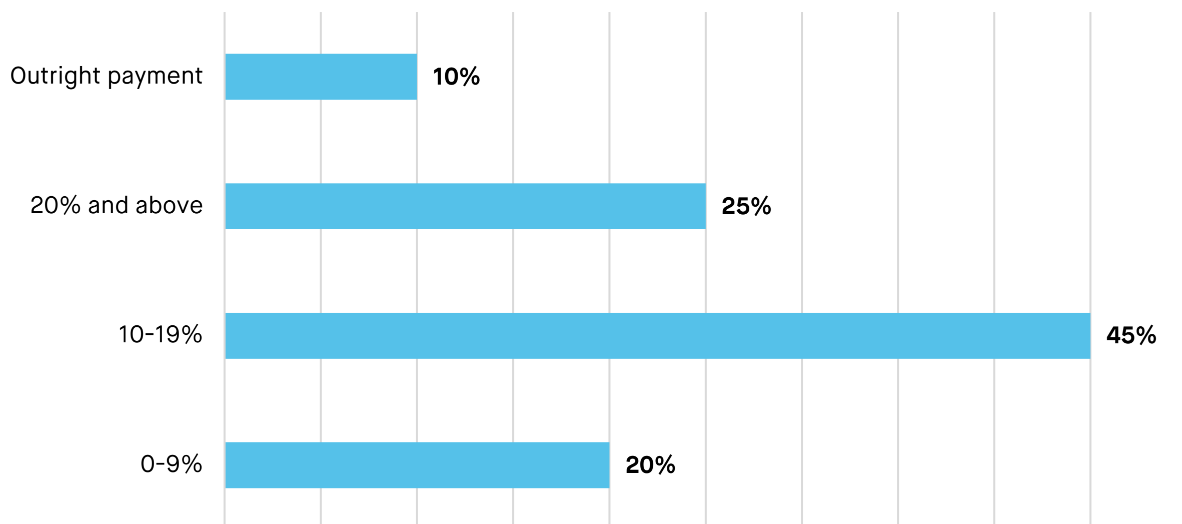


Source: FCA

The decline in high-LTV lending was mirrored by growth in residential lending to individuals who could afford a deposit over 25%, boosted by people moving up and down the property ladder and first time homeowners helped by the 'bank of mum-and-dad'. Low LTVs increased following the GFC from 49% in 2007 to 73% in 2009. Lending standards relaxed slightly over the following decade, increasing the proportion of loans with deposits between 10% and 25%, but a majority of lending remains concentrated among low LTVs, today worth 65% of individuals residential lending. This means buyers need more time to save for a loan: the average age for first-time buyers increased from 29.7 in 2007 to 33.4 in 2022.

Today, first-time buyers tend to prefer higher LTVs, with 45% paying between 10% and 19%, and 20% paying between 0% and 9%. This left 25% who paid higher deposits, while 10% bought outright.

Figure 2: Deposits for first time buyers (England)



Source: English Housing Survey[3]

At the same time, house prices increased. Between 1990 and 2022, British house prices more than doubled, increasing 142%, while prices relative to income increased by 56%. Despite these large increases, it is important to contextualise this growth within the wider Anglosphere. In this time New Zealand saw the most rapid increases, increasing house prices and price-to-income ratios by 346% and 154% respectively. While Britain's housing market has increased prices drastically over the past 30 years, it remains comparable to the other countries surveyed.

Figure 3: Real house price index, 2015 = 100

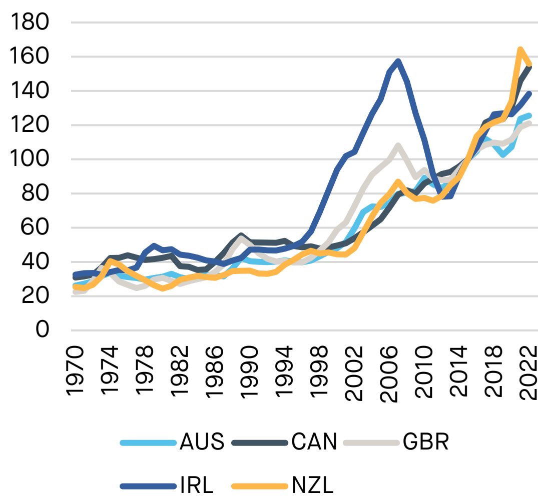
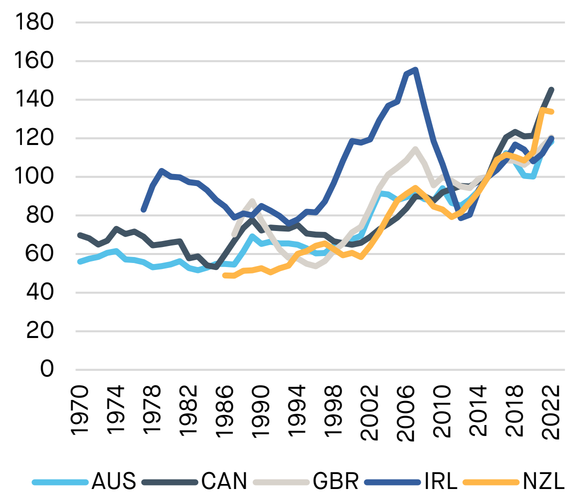


Figure 4: Price to income ratio index, 2015 = 100



Source: OECD

That said, the combination of higher prices and lower LTV ratios has fuelled a large increase in deposits. The average deposit demanded from UK first time buyers in 2007 was £16,400, yet today is worth £50,051[4]. As a percentage of median annual earnings, average deposits for first time buyers have more than doubled, increasing from 82% in 2007 to 180% today.[5]

This has increased the time it takes to save for a deposit. According to Generation Rent, in 2012 it would take just 6.8 years to save for a 10% deposit in England, yet today's higher rents and house prices now mean it takes 9.6 years.[6] This varies by region, with high prices in London pushing average time up to 18.3 years. Of course, this assumes buyers are asked to make a 10% deposit, and lower LTV loans will require an even longer timeframe. Resolution Foundation analysis found that in 1996 an average family aged between 28 and 34 would take four years to save for a deposit if saving 5% of their income. By 2019 that figure had risen to 21 years.[7]

One academic explained the mounting difficulties that come from renting longer among middle income tenants.

> *Renters generally have pretty low levels of savings. So if you're not having some help from parents...I wonder what's happening to that group? I'm not sure there's really any homeownership supports that are really going to be getting at those people."*

When these groups get older, it becomes more and more important to own a home, as one advocate explained.

> *"Middle income people are not your people in the highest need. But they are people who potentially are going to be in the highest need if you don't give them a hand. Because we know that if you get to retirement age without owning a house, you're looking at poverty in your old age."*

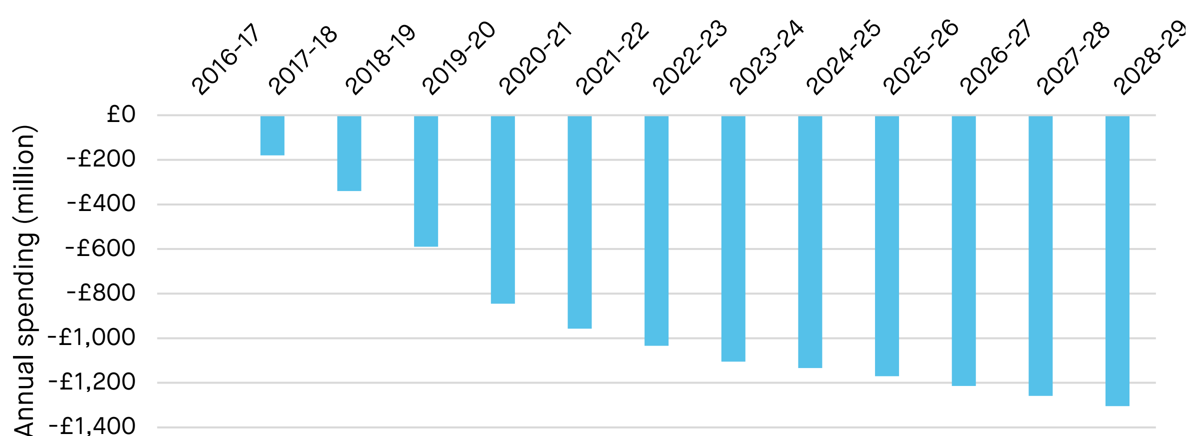
Under these circumstances, it is increasingly important that we help generations struggling to get onto the property ladder.

Lifetime ISAs have helped some first time buyers, but failed to reach others

Existing policies in the UK focus on personal financial accounts and tax incentives that provide a reliable and productive place for aspirant households to save for a deposit. The Lifetime ISA (LISA) allow individuals to save up to £4,000 annually to which the government adds 25%. Australia, Canada, and New Zealand provide similar tax-free savings accounts, while also allowing homebuyers to withdraw from their pensions when making a down payment.

Critics warn that LISAs are a costly policy that disproportionately benefits richer households. The combined cost to the government of foregone tax revenue and direct payments was £1.1 billion in the 2024-25 fiscal year. [i] 47% of this money went to those in the top income quintile. Since their introduction in 2016, LISAs cost the treasury £5 billion, with another £6 billion in losses expected by 2029.

Figure 5: Annual public spending associated with the Lifetime ISA[i]



Source: OBR[8]

The regressive nature of LISAs does not in itself mean the program should be scrapped. Fewer low income households will be in the position to consider buying a house, which means any policy to support homeownership is likely to be somewhat regressive. Our forthcoming report on alternative structures discusses measures that might be targeted specifically at the less affluent.

Where supply is constrained, LISA policy risks wasting government funds in a similar way Help to Buy Equity Loan Scheme once did. Help to Buy was announced in 2013 with various policies created under its purview. The Equity Loan Scheme provided interest-free equity for five years for first time buyers purchasing new-build houses to offset the cost of a deposit. These were found to have done little to increase homeownership in areas like London where supply is severely constrained and housing unaffordable, and there is evidence that it may have increased the prices of new-build houses affected in London.[9]

[i] Note that the OBR includes the cost of raising the ISA limit from £15,240 to £20,000 in their calculations, however this was only estimated to cost an additional £30 million over five years[9]

Yet it was able to increase supply without affecting prices near the English/Welsh border where there are less supply constraints and relatively affordable housing.[10]

While Help to Buy may have been useful in areas with low cost and few supply constraints, its use value in areas with high demand like London appears to be limited. In these cases lowering deposit thresholds would be more useful. However, fears of market volatility have prevented policymakers from pursuing this. Memories of 2008, when poorer households in the United States defaulted on their subprime mortgages causing the GFC, loom large in policymakers minds.

With a diverse market, we need multiple paths to homeownership

The British public have strong inclinations towards homeownership. But this is a large group and their needs and financial situations often differ. Britain's mortgage market needs to reflect that. Currently, the market is prioritising first time buyers who can afford a large deposit, who benefit from LISAs, and who want to buy homes areas where prices are cheaper. While this is useful for some demographics, it ignores those who may not be able save, or who want to buy in areas where the combined cost of lower LTV ratios and rising prices make saving for a deposit impossible.

No policy to lower defaults should come with additional risk to those households or to the wider mortgages market, but these two objectives are not irreconcilable.

Australia and New Zealand, are experimenting with mortgage guarantees in which the government backs a certain percentage of a home loan to lower the deposits being demanded by lenders (see comparison on the next page). These are similar to the government's proposed 99% mortgage guarantee scheme, which would have offered mortgages with deposits of only 1%.[11] Details remained scant, however, and it appears the government scrapped the plan in the spring of 2024. If the policy was to backstop the rest of the deposit with a guarantee akin to Australia and New Zealand, its unlikely many families would have benefited. Per household, the schemes are expensive for the government, which likely would have limited the amount of applicants who could benefit. At the same time, these applicants would need to have proven a sufficiently high income to minimize the risk of defaults or negative equity.

Canada, on the other hand, provides a path to homeownership for low income households that allows lower deposits through insurance, which offsets any wider risk of default and strict regulations regarding applicant finances.

Private mortgage insurance Canada

Canadian lenders are required to demand applicants purchase mortgage insurance when deposits are lower than 20%. This adds between 0.5% and 4% to monthly payments depending on the size of the deposit. Insurance providers are restrained from profiteering by national ceilings on the dollar value mortgage insurance products can reach.

This allows potentially risky applicants to access 5% deposits. In return, they must prove they can afford higher ongoing monthly payments through their existing income, wealth and budget, decreasing risks of negative equity. Banks meanwhile receive secure investments despite accepting lower deposits from poorer households.

Through higher regulation, the financial sector is supported against major crises including increasing interest rates or a credit crunch. Canada's mortgage underwriting standards and other supervisory practices are credited with creating Canda's relatively sturdy mortgage market performance during the GFC, with fewer mortgage defaults and limited damage to the financial sector.

Benefits

- Protects mortgage holders from default without creating risk exposure for government
- Protects wider economy from fallout from mortgage crisis

Limitations

- While deposits remain low, mortgage holders must take out additional cost of private insurance. In Canada this can add 4% to monthly payments

Mortgage guarantees Australia and New Zealand

When a lender considers an applicant to be risky, they can demand a higher deposit to offset the risk of default. Governments here can step in through mortgage guarantees which back a certain percentage of the loan, usually between 10% and 15%, which is set against the deposit. For instance, if a loan applicant was approved for a 20% deposit and the government guarantees 15% of the loan, the applicant can then receive a 5% deposit with similar assurances for the bank.

Examples include Australia's First Home Guarantee and New Zealand's First Home Loan. Australian applicants can apply to Housing Australia to guarantee up to 15% of their mortgage. More targeted schemes are connected, including one guaranteeing properties outside major cities and another for single parents. New Zealand, meanwhile, uses its state housing agency to underwrite mortgages and lower deposits to 5%.

Benefits

- Allows government to target support at select demographics and avoid the cost of private mortgage insurance
- Does so without high expenses so long as defaults remain uncommon

Limitations

- Government is exposed to risk in the case of widespread defaults, and may require high capital allocation.[2]
- Despite risk, government receives no reward as larger interest payments are pocketed by private banks.
- States therefore limit the amount of approvable applicants. Australia limits guarantees to only 50,000 households

[2] With the average mortgage nationally approaching £200,000, a 15% stake would place the government on the hook for £30,000 per house.

Recommendations

Provide mortgage insurance for high LTV mortgages as an alternative to high deposits

Mortgage guarantees are useful in that they lower deposits and do not increase costs for mortgage holders. However, this risk is instead held by the government, which therefore only offers a limited number of mortgage guarantees each year. Australia, for instance, offers guarantees for only 50,000 homes.

Instead, Canada's method of insuring mortgages is immediately actionable for a wider swathe of the British market. Canada requires private lenders to demand mortgage insurance in exchange for lower deposits. Insurance costs add between 0.5% and 4% to a monthly payment, with amounts inversely proportionate to deposits which range from 5% to 20%.

This policy should be adapted for the British context. In 2022, the Tony Blair Institute called for this number to be set at 80%, echoing the Canadian strategy.[12] However, the Canadian housing market has distinct features, including higher overall prices. In addition, Canada tends to have lower LTV rations than the UK. In Britain, 45% of loans are currently provided with deposits ranging from 10% to 19%. which could be obstructed by new insurance mandates. It also risks increasing costs for households who have been fortunate enough to purchase loans with deposits they could afford at under 20%. These includes households that purchased property outside of London, where prices are more affordable. Applicants in this demographic are likely to stay the course, continuing to take out loans between 10% and 19%.

Yet for those households who do not see a path to mounting the high deposit barrier, offering another option would be welcome. These may include middle income households who lack savings and inheritance, as well as those looking to purchase in expensive areas like London and the South East. For them, lowering deposits and increasing LTV ratios can decrease up-front costs which represent the largest obstacle to homeownership.

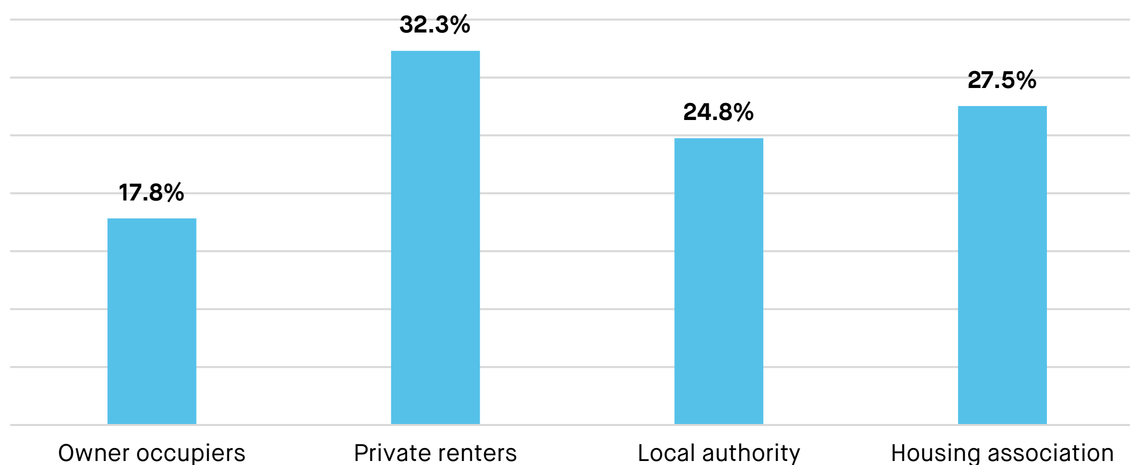
As such Canada's mortgage insurance policy should be adapted. Displacing a portion of the deposit costs to monthly instalments could open up access to private homeownership far earlier for first time buyers, and give hope to many who feel they will never be capable of affording a deposit. Despite increased monthly payments, these may remain attractive for many aspirant home buyers. Adding 4% to mortgage payments would increase homeowner payments as a percentage of their household income from 17.8% to 18.5%. This would allow them to exit the private rented sector earlier, while at the same time private lenders would feel secure in their investment.

When first time buyers struggle to amass sufficient savings, lenders should be permitted to accept insurance on the mortgage in lieu of deposits. This would require two major changes to the government's Mortgage Guarantee Scheme. Firstly, it would allow private sector insurers to offer insurance directly to mortgage applicants. Currently, this risk is held by the government with costs, included the expected losses, capital to provide the guarantee, and the administrative costs, paid for by lenders in the form of a commercial fee.[13] As observed in Australia and New Zealand, while government provision means first time buyers do not pay a fee, it also limits the amount of buyers who can benefit from the scheme. Between the schemes introduction in April 2021, just 41,052 mortgages have benefited from the scheme.[14] Instead, Canada's private sector insurance solution can provide insurance at scale. While these would increase the monthly payments of first time buyers, homes would remain affordable so long as strict regulations are in place which limit the pound value mortgage insurance products can reach.

Secondly, providing mortgage insurance effectively will require liberalizing affordability regulations that set a ceiling on the proportion of loans banks can offer which are more than the applicants' salary. Typically, mortgage applicants can borrow four times their salary when you get a mortgage with a LTV ratio of 95%, though lenders can offer up to 4.5.[15] This means if a home is £500,000 and the applicant makes a 5% deposit, they will still need to pay £475,000. That means to meet the regulatory requirements, lenders would prefer applicants' combined salaries of £118,000 annually. Where they are insured, this ceiling should be raised.

Although mortgage deposits are high, monthly payments remain relatively easy for most households to afford. Monthly mortgage payments generally cost just 18% of a household's income, compared to 32% for private renters and 25% for local authorities (Figure 6). This means most households can comfortably make monthly payments after their deposit is paid. Just 34,000 households are in mortgage arrears, equating to 0.5% of total mortgages, implying there is room to increase the proportion of payments and decrease the size of the deposit for a large amount of households.

Figure 6: Mortgage/rent as a proportion of household income including housing support (England)



Source: English Housing Survey[16]

This is not to say that all aspiring homeowners would choose to pay insurance premiums in favour of a lower deposit. But by adding this route, British policymakers can present an alternative to aspiring homeowners seeking relief from rents who would not otherwise be able to gain entry into British homeownership.

At the same time, adding mortgage insurance to high LTV loans would encourage mortgage lenders to offer lower deposits to first time buyers. Currently, banks who offer low deposit loans often receive high demand, and look to increase low LTV loans in order to offset that risk. Mortgage insurance provides an alternative strategy to offset the risk while lowering barriers to first-time buyers.

High deposits are designed to increase confidence in the market and ensure lenders trust mortgage holders, but they now present large obstacles which obstruct access to homeownership. When breached, mortgage holders find payments to be relatively relaxed. Offsetting some of the cost of the deposit with higher mortgage payments therefore seems an attractive alternative for households struggling to amass a deposit.

CHAPTER THREE – KEEPING MORTGAGE PAYMENTS AFFORDABLE

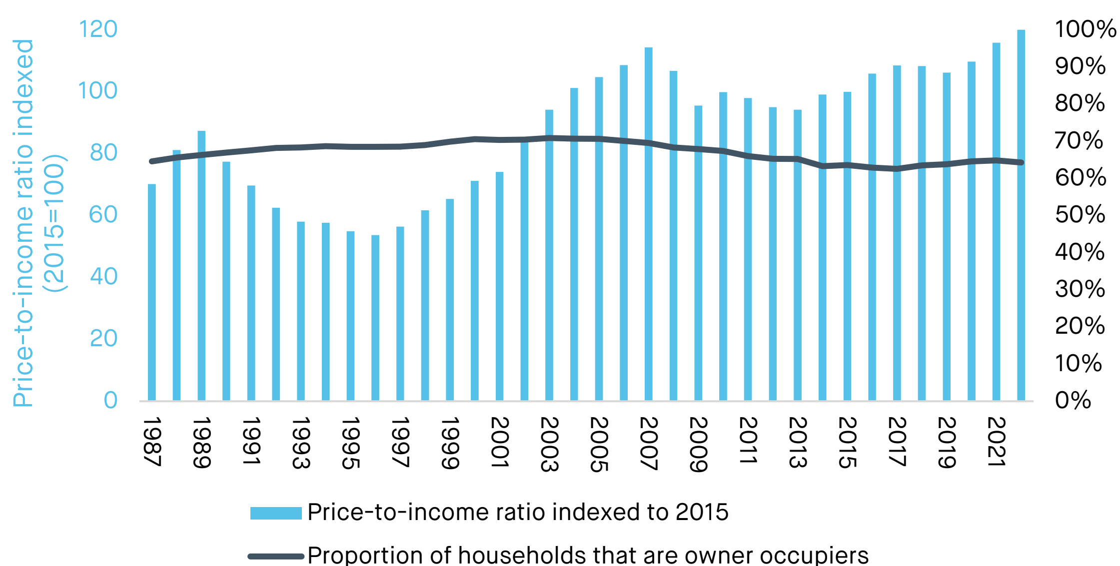
While mortgage payments are a far smaller hurdle than deposits, they remain a costly one for UK households. This has been particularly true over the past two years as high interest rates push up payments. The coming decade may see higher interest rates than homeowners experienced in the previous one, so it is important that policymakers prepare and respond.

There are four costs associated with a mortgage: loan interest, loan principal, taxes, and insurance. These vary depending on region and agreement, with some countries dispensing of insurance and others dispensing of taxes. As insurance is discussed above and taxation below, this chapter will focus on the loan principal and loan interest.

Loan principal

Rising house prices mean mortgage principals are increasing. However, this appears to have had only a modest effect on homeownership, despite house prices more than doubling as a proportion of wages since 1995 (Figure 7).

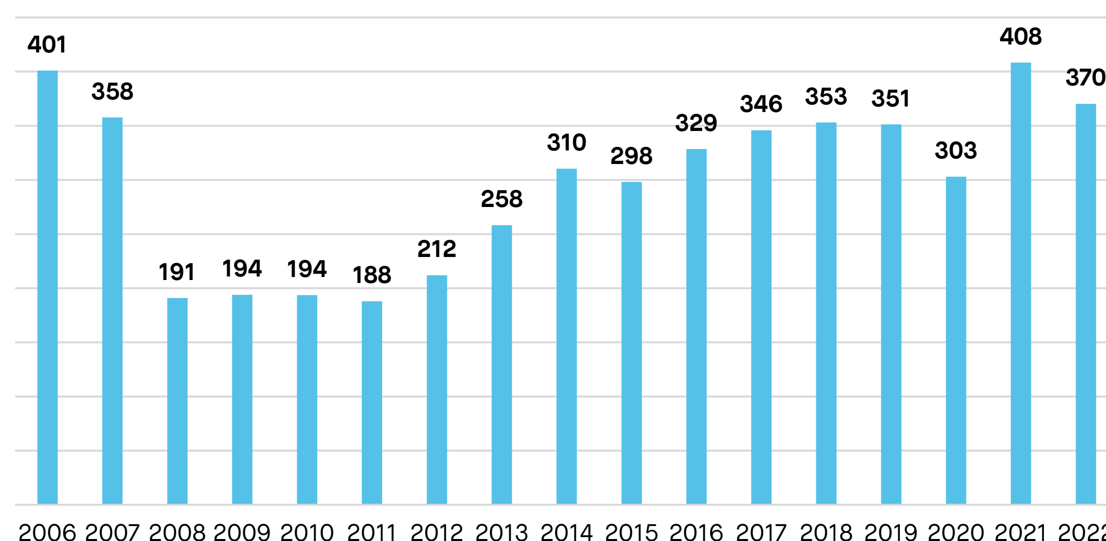
Figure 7: Price in UK homes vs proportion of population who are owner-occupiers



Source: DLUHC[17]

Despite these severe increases in the value of homes relative to earnings, people have still been entering the property market. The number of first time buyers acquiring homes is nearly back to pre-GFC levels in the UK. How have they managed to get into the market, when prices have so outpaced incomes?

Figure 8: Number of first time buyers in the UK (thousands), 2006-22



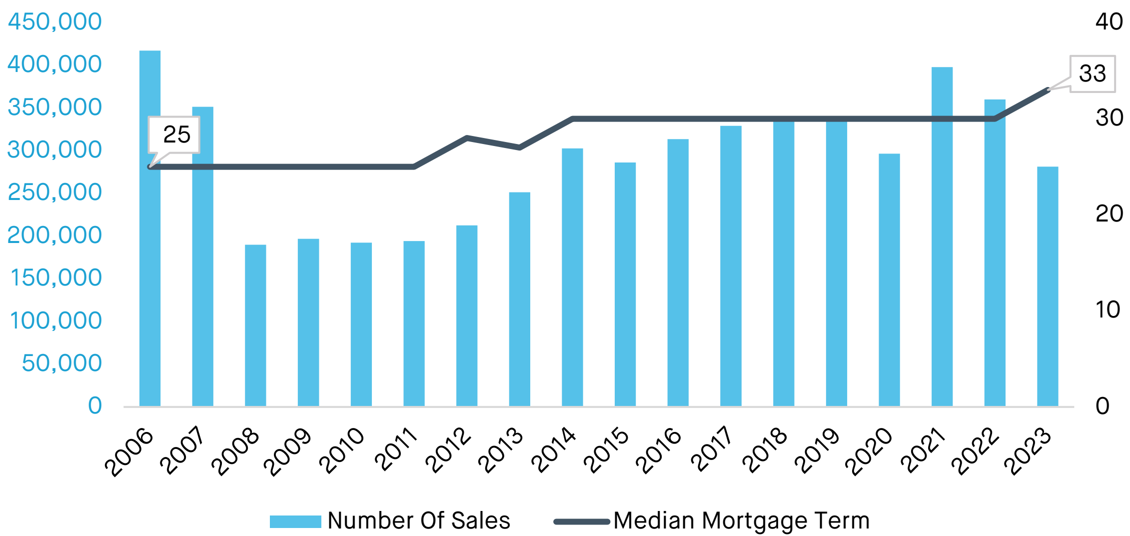
Source: Money.co.uk

Lenders need to keep their books of borrowers growing. Half of those remortgaging in the UK stay with their current mortgage provider, so getting customers in for their first mortgage pays off in the long term.

Homeowners are also incentivised to get into the market if they are able. In the UK there is the cultural expectation of property ownership, but buyers may be more influenced by the reality that real estate can be both a home and an investment. Low interest rates, rapidly increasing prices, and the profitability of rents mean homeownership can be very valuable. The sense of security and the ability to put your stamp on a place is only one of many elements that make homeownership attractive.

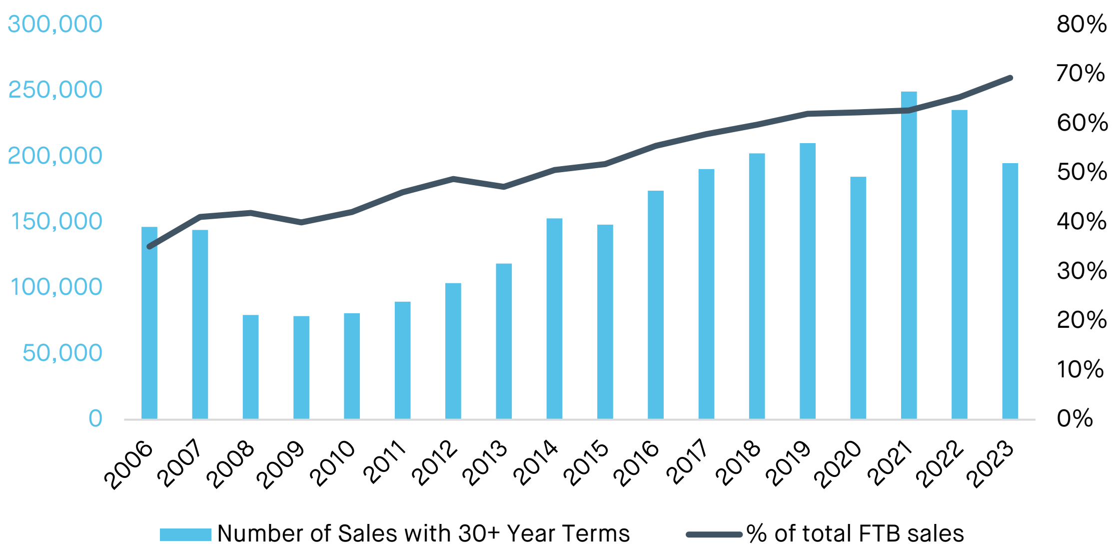
The rise of 'marathon mortgages' is therefore appealing to both lenders and borrowers. Figure 9 illustrates how the median length of a mortgage for first time buyers has increased from 25 years in 2006 to 33 years today. At the same time, Figure 10 shows how the percentage of first time buyers who take out mortgages with over 30 year terms has increased from 35% to 69%. This keeps monthly repayments manageable, and therefore has kept mortgages steady, as shown in both figures by the increasing number of sales as the market recovered from the GFC. First time buyers (FTBs) continued to accept these loans despite it meaning a greater spend on interest over the course of the mortgage – again, a boon for lenders.

Figure 9: Median and mean mortgage terms among first time buyers (FTBs)



Source: FCA

Figure 10: Mortgages with 30+ year terms among first time buyers (FTBs)



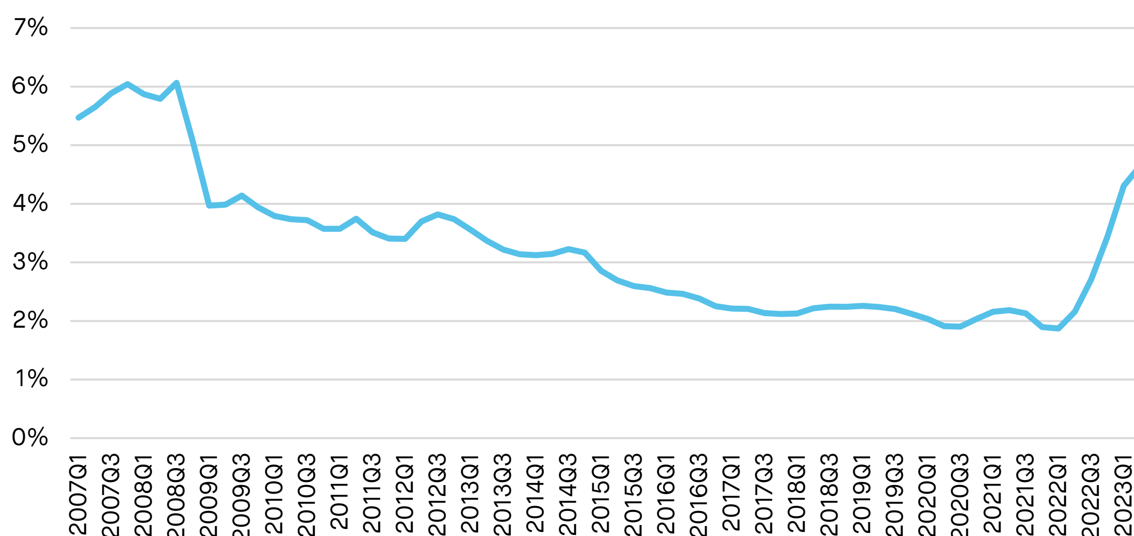
Source: FCA

Interest rates

The second aspect relates to interest. Interest rates are particularly dangerous as rapid rate rises can cause defaults even on properties that the mortgage lenders considered safe investments. The shorter the interest rate terms, which determine how long each deal is made, the more danger there is for mortgage holders that interest rates may increase.

Mortgage rates fell alongside interest rates following the financial crisis. Figure 11 shows how average mortgage rates declined from 5-6% before the financial crisis to as low as 2% during the pandemic in the UK. Figure 13 shows how interest rates across our focus countries have followed a similar pattern. Over the past year, interest and mortgage rates have shot up as part of efforts to tackle inflation. Up until this period, the continual decline in the cost of borrowing would, like extended terms, have enabled people to manage monthly mortgage bills.

Figure 11: UK overall average weighted mortgage rates on gross borrowing, 2007 - 2023



Source: Bank of England and FCA[18]

Although monthly repayments were kept down through ‘marathon mortgages’ and lower rates, that does not help the burden of saving for a deposit. Not only are prices higher, higher loan-to-value (LTV) mortgages are harder to come by than they were in the 2000s. 100% mortgages were available prior to the financial crisis, but it has taken until 2023 for one or two such products to return to the UK market.[19] 95% LTV products are possible, but the higher the LTV, the less favourable the borrowing rates are, and the harder it is for low income households to access them.

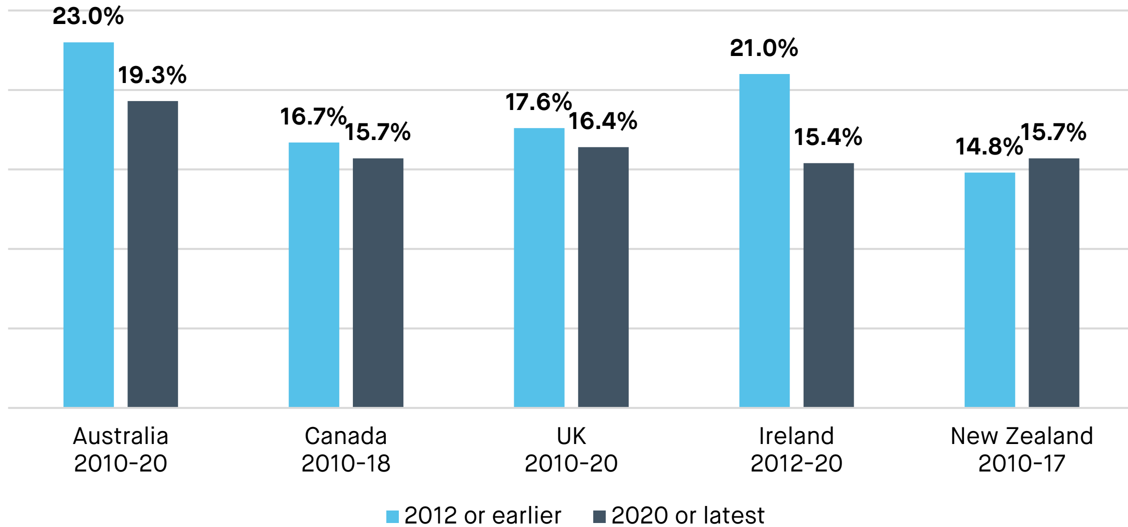
British mortgage holders can choose between three types of interest payments. The first introduces a fixed rate for a set amount of time, generally between two and five years but with the ability to stretch longer. The second allows mortgage holders to pay a rate that tracks the base interest rate. This means they are less insulated from changes to the interest rate but are only locked into high rates for as long as the central bank keeps them high. Lastly, mortgage holders can hold a standard variable rate (SVR). These are often introduced when a fixed or tracker mortgage term expires, and transitions holders to a rate which, while influenced by the base rate, includes other factors and does not necessarily follow rate trends precisely.

In Canada, Ireland, Australia and New Zealand, mortgages come as either fixed rate terms or as floating rates similar to the UK’s SVR, while Ireland provides tracker rate mortgages like the UK. Canada and New Zealand allow mortgage holders to split their mortgage payments between fixed and variable loans.

Interest rate rises are now hitting the incomes of those lucky enough to be on the property ladder, after a decade of declining mortgage bills

If we look before the pandemic, housing costs for those paying a mortgage were in a relatively benign state. In fact, they fell as a share of disposable income everywhere except in New Zealand over the 2010s, as we can see in Figure 12.

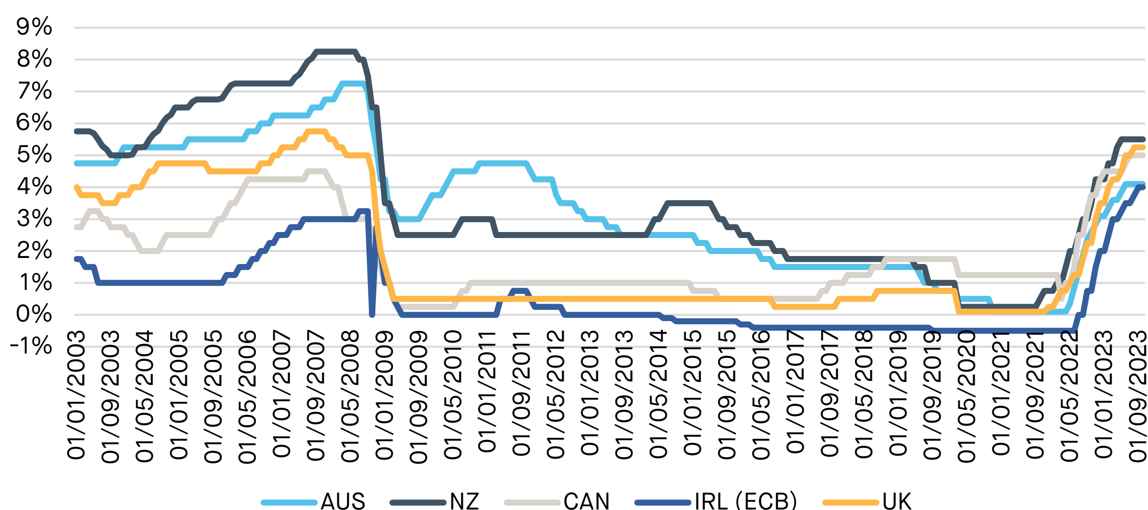
Figure 12: Median of the mortgage burden as a share of disposable income, 2010s



Source: OECD[20]

The post-pandemic economic situation, however, with accelerated house price rises and higher interest rates, is likely to create more pressure. Higher house prices mean dearer mortgage payments for a given house for first time buyers. Rising interest rates, meanwhile, affect costs for all those whose mortgages are not on long-term fixed rates. These have followed similar patterns across the countries of focus. In the early 2000s, these steadily rose before sharp drops in the GFC. Rates hit close to zero in the UK, Ireland and Canada, and then stayed fairly low. In Australia and New Zealand, rates did not fall as much in 2008/09, but then tapered down over the following decade. Rates were slashed before the pandemic, and have now been moving up in lockstep to deal with global inflationary pressure.

Figure 13: Headline Interest Rate



Source: OECD[21]

UK mortgagors are fairly exposed to changes in interest rates. Although over 90% of borrowers are on fixed term deals, these are almost all for less than five years – most typically one to three years. This means that once those periods are up, households will have to move to a new fixed deal (or go variable) at the now higher rate. It is a similar picture in New Zealand[22] and Ireland.[23] In Australia, meanwhile, most mortgage holders are on variable rates, so many will feel the impact of rising rates immediately.[24]

Recommendations

Decrease the proportion of variable rate mortgages and increase fixed rate offers for entire 30 year terms as well as 15 and 10 year terms

The decade following the financial crisis saw low and steady interest rates. The next decade may be different. Rising geopolitical tension makes interest rates increasingly unpredictable. In this climate, introducing longer terms for mortgage holders can increase the stability of their finances as well as for the economy more broadly. As such, fixed rates mortgages should be offered to borrowers over a longer period than is currently common in the UK, following the policies of Canada and the United States..

Although long term fixed rate mortgages such as those lasting 15 or 30 years may look good to policy analysts, the British public has historically proven more wary. When products have been offered they are often in low demand and are generally replaced by shorter terms or replaced with tracker/SVR mortgages.[25] However, recent experience with inflation and high mortgage rates may have changed the mind of the British public. Further, with pressing international issues including the war in Ukraine and various conflicts in the Middle East, there is no guarantee the coming decade will have rates as slow or stable as the last.

There are various ways for policymakers to increase the availability of fixed rate mortgages in the marketplace. One solution proposed by the Tony Blair Institute is to scrap affordability regulations which limit the proportion of loans lenders can issue which are worth more than 4.5 times the borrower's income.[26] This is designed to protect mortgage holders from default in the case of increasing interest rates, but by definition these do not apply to fixed rate mortgages and should therefore be outside the scope of the regulations. Such liberalisation would follow the policy of the United States, which has a larger proportion of mortgages on long term fixed rates.[27]

This would require lenders to take on more risk due to the chance the base rate is higher than anticipated over the term of the loan. That said, lenders tend to benefit as long term mortgages tend to be more expensive for that reason. Additionally, lenders benefit when base rates are lower than anticipated. and their loans are less likely to default due to the steady payments required of mortgage holders.

In addition to liberalising affordability regulations policymakers should require a that lenders offer advice related to 30 year fixed rate amortisation mortgages, as well as others for 15 and 10 year terms. Long term fixed rate mortgages are often alien to consumers, who may demand extra information or support in this area. These requirements, alongside deposit insurance, would allow households to plan for the long term while protecting against the risk of widespread defaults.

CHAPTER FOUR – MORE EQUITABLE TAXATION

The UK's housing taxation system privileges wealthier property owners, whose homes are effectively subsidised by lower income individuals including the owners of less expensive properties, renters in the private sector, and social housing tenants. To increase access to homeownership, British authorities must rebalance housing taxation. Households on lower incomes need an easier path to homeownership, while the wealthy who have benefited from property spikes over the last 30 years need to pay their fair share.

Taxation has complex effects on the price of a home. Their direct effect is to increase the price. However, the 'second order' effects based on who pays and how they do so are more difficult to pin down. For instance, stamp duty is a transaction tax payable upon purchase. This creates an additional hurdle for home buyers and increases the savings they need to make a down payment, and contrasts with home value taxes which are paid annually elsewhere in the Anglosphere. Understanding who pays is also vital. Take council tax, which is applied to renters and homeowners alike. This fails to disincentivise owners from converting their homes into buy-to-let properties, constraining the supply of purchasable properties.

How we tax our property often depends on the motives which inspire its designers, and most countries use a mix of taxes which reflect their multiple priorities. If the goal of property tax is for homeowners to fairly compensate the community for shared services, such as the use of land, sewage systems, and roads, tax revenue may be cycled back into the local community. Local taxes are levied in all the countries studied in this report, through the localised council tax system of Australia, New Zealand, and Ireland, and through municipal taxes in Canada and New Zealand. Growing demands for services from these localities has increased tax pressure in some areas. For instance, Canada's largest city, Toronto, effectively increased its property tax by 9.5% in 2024 to cover investments in transport, housing, and safety.[28]

Meanwhile, if property taxes are also meant to redistribute wealth, they may be levied through regional or national systems. By widening the geography beyond local municipalities, these taxes are able to spread the wealth generated from home purchases across higher levels of government. In the UK, stamp duty generates 0.7% of the central government's revenue, funding programs across the country, which is complemented by capital gains taxes on housing sales.[29] Both Australia and Canada levy a property tax beyond local taxes at a state/provincial level. However, both New Zealand and Ireland do not levy property taxes beyond the local level.

Finally, if the goal of property taxes is encourage or discourage social or financial practices, in a similar form as alcohol and tobacco duties, an extra tax may be introduced. With the housing market increasingly being blamed for social problems, more countries are experimenting with new forms of housing taxes on housing by taxing foreign buyers, investment properties, and vacant homes. We refer to these as "housing sin taxes" mimicking the nomenclature of taxes meant to discourage behaviour like smoking, drinking, and gambling. Like housing sin taxes, these taxes are permissible in the market, but often discouraged by government due to perceived the effects on local social and personal health.

On the one hand, homeowners should pay a portion of their property wealth back to the community, either for shared services, equitable redistribution, or to maintain social stability. However, taxes also increase the cost of buying a home, potentially preventing first time home-buyers like the young and those without family wealth from getting on the property ladder. The below section details how we can learn from experiences abroad to maintain funding for services, maintaining social equity, and improving access to housing across the country.

Local taxes

The below table categorises local taxation across the Anglosphere by who is charged, how charges are decided, how often home values are updated in relation to the charges, and their average cost for the median home.

Table 2: Local taxes across the Anglosphere

	Form	Value proxy	Charged to	Value update	Average cost
UK	**England + Scotland:** Council tax charging residents based on the value of their residency as divided into eight bands	Capital value (8 bands)	All residents	1991	ENG: £2065[30] SCO: £1903[31]
	Wales: Council tax charging residents based on the value of their residency as divided into nine bands	Capital value (9 bands)		2003	£1879[32]
	Northern Ireland: Domestic rates charging residents based on the value of their residency multiplied by the district rate set by local authorities	Capital value		2005	£1112[33]
Australia	Council rate charging property owners based on the annual income needed by the council divided by the combined value of all local properties, with individuals paying for the value of their property multiplied by this factor	Capital value, land value, or rent value based on council decisions	Property owners	Every one to six years	£1000[iii]
Canada	Property taxes are determined by the province and municipality which decide a flat rate for all properties. Owners pay this rate multiplied by the value of their home	Capital value	Property owners	Every one to four years	£4,135[iv]
Ireland	A Local Property Tax (LPT) is levied by the central government which divides properties into one of 20 tax bands based on their value, progressively taxing residents based on this amount. Counties may increase or decrease LPT by 15%. For properties over £1.5 million, higher rates are charged	Capital value (20 bands + surcharge)	Property owners	Every three years	£270[v]

[iii] Based on LGIU figures of total council rate revenue divided by the amount of property owners in Australia, totaling AUD $1902.45 or GBP £998.94

[iv] Canadian rates generally fall between 0.25% and 1.75% of a property's value. Researchers therefor used 1% as an indicative property tax and multiplied it by the Canadian Real Estate Association's average selling price of a home which in 2023 was CAD $716,000 or GBP £413500

[v] Based on Citizens Information figures on LPT bands and local property tax data showing the median home price of EUR €320,000

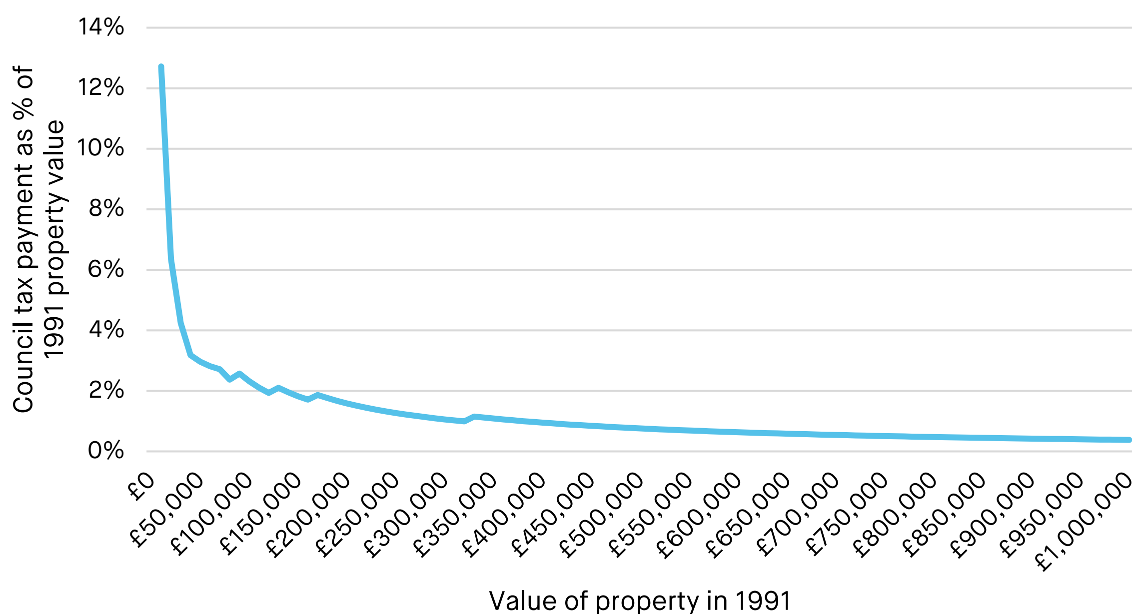
New Zealand	Council rates are decided by local councils who decide a general rate that is multiplied by the home's property value. Most properties pay the same general rate, however some councils charge a differential rate which alters the general rate based on value, location, or area. This can be complimented by uniform annual general charges (a flat fee for every property regardless of value) and targeted rates which fund particular utilities.	Capital value, land value, or rent value based on council decisions	Property owners	Every three years	£1285

The UK stands apart from the Anglosphere in four categories

Valuations

The first is the interval in between house valuations. Most municipalities revalue properties within four years, though some states in Australia do so every six. In England and Scotland, the last property valuation was over 30 years ago. As a result, Britain's local tax system privileges owners of properties whose value has increased the most. Council tax payments fall as a share of property values as the value increases, as outlined in Shreya Nanda's IPPR report *Pulling down the Ladder*.[34]

Figure 14: Council tax payment schedule based on the average Band D payment, England



Source: Shreya Nanda, IPPR analysis of VOA, London Datastore, and MHCLG data[35]

This means families in the North or in relatively worse housing are paying more in council tax as a share of their home value, and of their income, while those in the South and London are paying less.

Banding

The second way that the UK is an outlier is its banding system, with eight distinct rates based on homes' assessed value. For instance, Band G includes homes with a market value between £160,000 and £320,000, meaning owners may be charged the same rate even when one owns a property worth twice as much as another. In contrast, Canada, Australia, and New Zealand all tax properties on a continuum based on a set percentage of their home's value. Ireland, the only other country to use bands, includes twenty, which can better accommodate price variations and charges owners more progressively than the English system. Ireland also has a surcharge for properties worth more than EUR €1.75 million, meaning large homes and mansions pay a higher rate.

Tax base

The third unusual feature about the UK is based on who is charged. Within the Anglosphere Britain stands alone by charging all residents for local taxation. In Australia, Canada, Ireland, and New Zealand, as well as the United States, local property taxes are paid only by property owners. This is considered appropriate as, unlike tenants, property owners see direct financial returns from these investments in their local community. In addition, exemption from property taxes allow tenants more flexibility to save for a mortgage and down payment. The logic is similar to the government's exemption of full-time students from paying council tax. Of course, in other countries, renters may still carry some of the burden of property taxes indirectly, if landlords pass the cost onto them.

Cost

Finally, the amount Britain pays in council tax is higher than most other countries, British values are nearly double that of Australia and New Zealand, and over seven times that of Ireland. Within the OECD, Britain has the highest proportion of taxes resultant from property. Within the countries for this report, only Canada's burden is higher, and it should be noted that by only taxing property owners, Canadian municipalities tend to put the burden on those who can better afford it, rather than the British strategy which taxes all residents regardless of their tenure. By heavily relying on council tax relative to other countries, the UK leans too hard on a regressive tax which protects the most wealthy and prevents the poorest from accessing the housing ladder or taking steps on it.

Transaction taxes and capital gains

In the UK, stamp duty is levied in addition to council tax and is a transaction tax owed by the purchasers of a property. Stamp duty only applies on homes valued above £250,000, or over £425,00 for first time buyers. Buyers must pay an additional 5% of the home value if the home is worth between £250,000 and £925,000, 10% if it is worth between £925,000 and £1.5 million, and 12% if it is worth above £1.5 million.

But with the average home price valued at £290,000 in 2023 and rising, stamp duty is now hitting more middle income households. Since 2000, stamp duty revenue as a percentage of GDP has doubled from 0.33% to 0.69%.[36] Adding an extra tax on homebuyers makes existing homeowners less likely to move, and tends to slow down housing transactions, leaving less homes available for first time buyers.

Meanwhile, capital gains tax (CGT) is levied on sellers for the assets sold, based on the difference between the sale price and the purchase price, with rates increasing with larger gains. Primary residences are exempt, with CGT only levied on second homes and rental properties. Primary residences are exempt, despite making up the bulk of sales. Further, these are taxed at a lower rate than income, encouraging speculation and increasing prices.

The UK is not alone in their transactional taxes. Unlike local taxation, Britain's transactional taxation tends to resemble our peers, which often combine some form of stamp duty with CGT. However, key differences apply, and recent changes to national tax policy can provide useful insight into what the UK's could experience if transactional taxes change. These differences are outlined below.

Table 3: Transaction and capital gains taxes across the Anglosphere

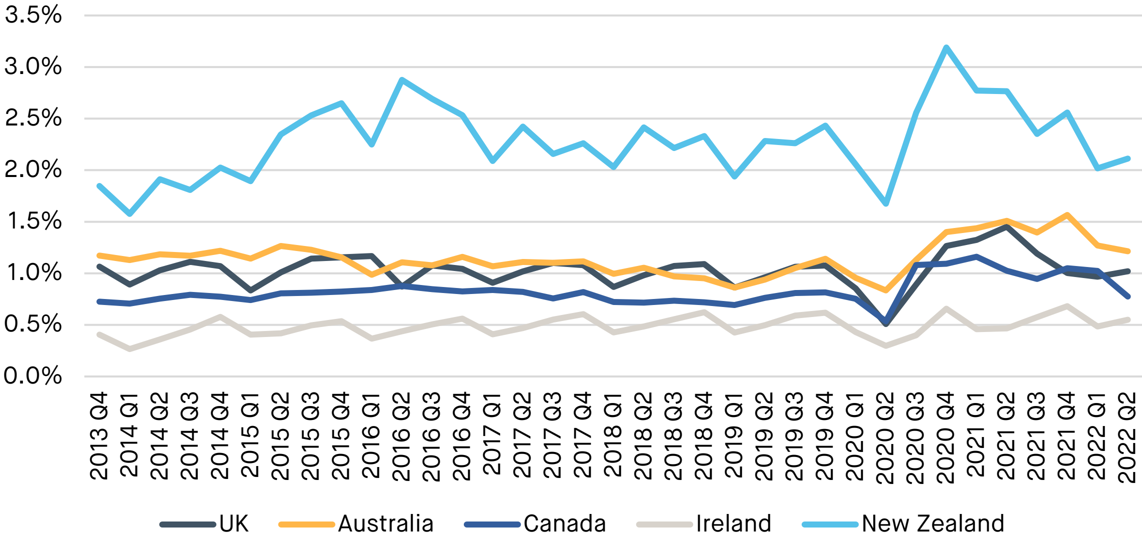
	Transactional tax (Buyers)	Value:	Capital gains tax (Sellers)	Value:	CGT on primary residence?
UK	Stamp duty on home buyers on properties over £250,000, or over £425,000 for first homes, with an additional 3% levied on secondary properties.	5% if ≤ £925k 10% if ≤ £1.5 m 12% if ≥ £1.5m	The central government collects CGT on secondary homes,	18% basic rate, 28% for higher rates	No
Australia	In Australia, stamp duty or transfer duty is levied on home buyers based on the market value of the property on the day it is registered. This is a transactional tax paid once and its value is set by each state. In general, rates increase with home values, though the amounts and thresholds are decided by the province. They may contain a surcharge for more expensive homes.	1% - 6.5%	Capital gains are taxed as income in Australia, however, a 50% discount is applied to homes owned for more than a year	All profits are taxed as income	No
Canada	In most of Canada,[vi] a land transfer tax is levied on home buyers based on the market value of the property on the day it is registered. This is a transactional tax paid once, and its value is set by the province. In general, rates increase with home values, though the amounts and thresholds are decided by the province.	1% – 4%	The federal government collects CGT on half the value of sales from secondary homes.	Half of profits are taxed as income	No
Ireland	Stamp duty of 1% is charged in Ireland on residential properties worth up to EUR €1 million with an additional 1% added to homes with higher prices	1% - 2%	The central government collects CGT on secondary homes	33% of profits	No
New Zealand	Not charged in New Zealand		Not charged in New Zealand		

[vi] Alberta and Saskatchewan are the only provinces which do not charge a land transfer tax, though there are smaller mortgage and property registration fees, usually worth less than GBP £1000

Transaction taxes are often criticised for discouraging buying and selling of properties, “gumming up” the market. For instance, imagine a couple in a small home want to buy a larger property to start a family, but are discouraged from doing so because stamp duty pushes the cost up. The couple’s existing residence would be a perfect fit, but is unavailable as a result of stamp duty. This effectively slows down transactions in the housing market, leaving middle income households unable to upsize, and limiting the availability of middle income housing for those just starting out on the housing ladder.

Such an analysis is borne out by the data. For the past 10 years, New Zealand has been the only Anglosphere country we surveyed not to tax housing transactions, and has at the same time seen higher transactions than anywhere else as a percentage of their total housing stock. In that time, New Zealand has often seen double or even triple the number of residential property transactions than the UK.

Figure 15: Quarterly residential property transactions as a percentage of 2022 total housing stock



Source: Stats NZ, HMRC, CSO, CREA, ABS

While it is possible New Zealand’s lack of a capital gains tax also amplifies their housing transactions, it is doubtful that this is the only factor. Canada levies half the capital gains taxes that Australia does, yet for the past 10 years has seen fewer transactions as a proportion of their total housing stock.

Further, to the extent that capital gains tax impedes sales, it only prevents owners buying secondary properties, meaning they are not preventing individuals from getting on the property ladder. All countries surveyed which levy capital gains on properties levies them on secondary or investment homes. This is useful for two reasons. Firstly, capital gains taxes of this kind disincentivise property speculation and accumulation in favour of more widespread homeownership. By applying capital gains tax exclusively to secondary properties, the UK and other countries advantage first time buyers and those seeking a primary residence and dissuade investors who might leave the homes vacant or let them to incoming tenants. Secondly, capital gains tax is progressive, redistributing revenue equitably across the UK. The tax was applied to 139,000 taxpayers and 151,000 property transactions in the 2023 financial year, providing £1.8bn to the treasury.[37] London and the South East together accounted for over 50% of all capital gains revenues.

Housing sin taxes

Housing sin taxes have grown in popularity as more attention is paid to particular aspects of the housing crisis. These are bolstered by supply side analyses that warn there are not enough homes being built as well as demand side solutions that warn against the price increases caused by investment properties. Housing sin taxes are being designed around the world to respond to these ideas, but it remains uncertain how well they function, and whether they are capable of meeting their goals. The table below analyses foreign buyers taxes, vacant home taxes, and rapid sales taxes where they are applied.

Table 4: Housing sin taxes across the Anglosphere

	Foreign buyers tax		Vacant home tax		Rapid sales tax	
	Form	**Value**	**Form**	**Value**	**Form**	**Value**
UK	Non-resident Surcharge: Surcharge on stamp duty for non-residents[vii]	2% of value	Council tax empty homes premium	Double council tax for homes empty over two years	N/A	
Australia	Foreign Investment Review Board fee Stamp duty surcharge Land tax surcharge	1-3% of value 7% – 8% relative to state 2% – 4% relative to state	Vacant residential and tax surcharge only in Victoria	1% - 3% increasing over time	CGT discount	50% discount on CGT if sold after a year
Canada	Surcharge on purchase applied by some provinces[viii] Temporary federal prohibition on home purchases outside rural areas for those not Canadian or permanent residents	20% - 25%	Underused housing tax (federal) Additional taxes (municipal/ provincial)	1% 0.5% - 3%	CGT discount	50% discount on CGT if sold after a year
Ireland	N/A		Vacant homes tax applies when a home is occupied for less than 30 days of the year	Three times the local property tax	N/A	
New Zealand	Federal prohibition on home purchases by non-residents		N/A		Bright line test	Profits from a property sale sold within 10 years of the purchase are taxed as income

[vii] Does not apply in Scotland and Wales

[viii] Currently includes British Columbia and Ontario. Nova Scotia taxes non-resident properties a more modest 2%.

Foreign buyers taxes

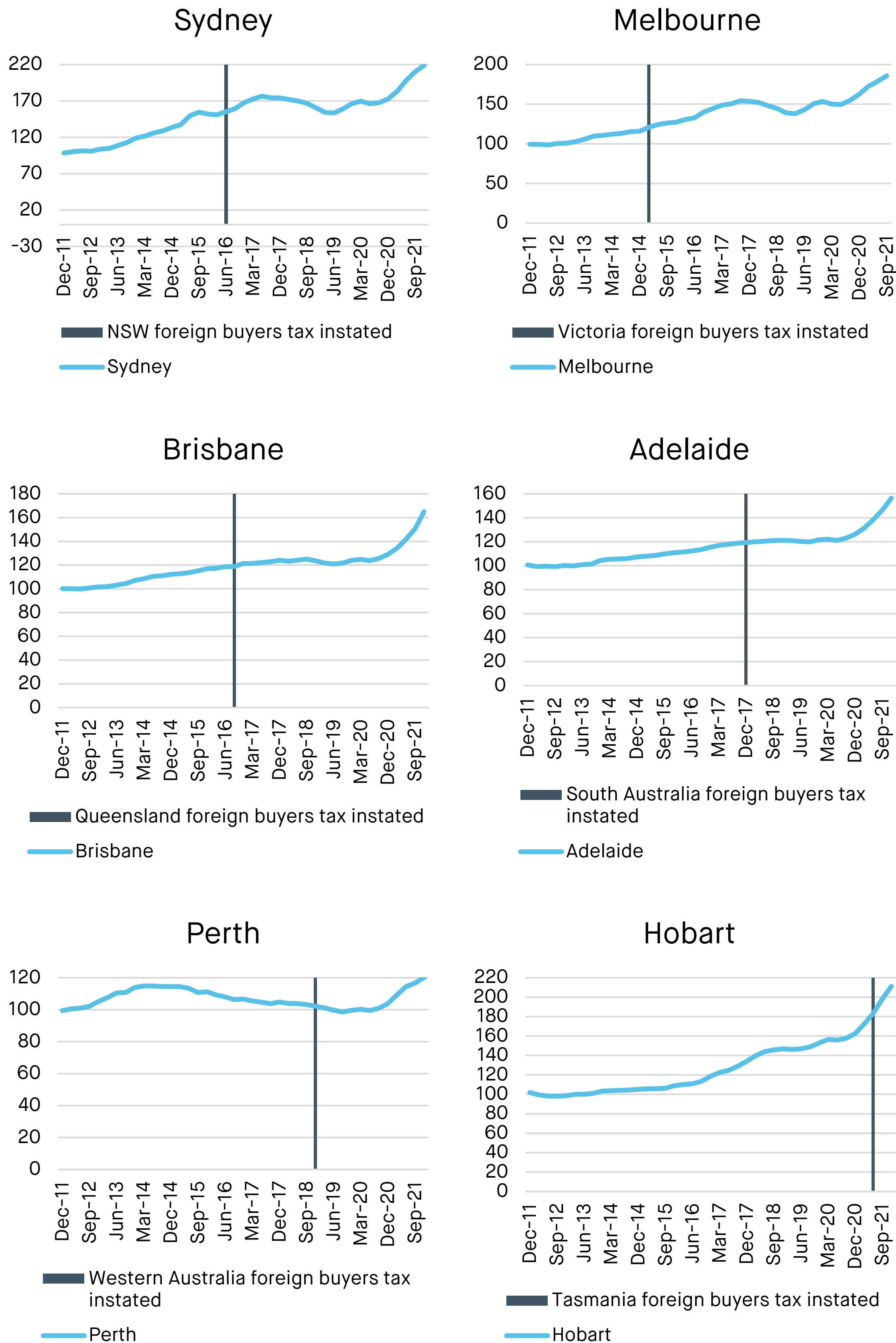
Foreign buyers taxes add an additional charge on a home purchase for individuals that do not have citizenship or residency in the country where they are buying. At times, these taxes extend to include corporations. In England and Northern Ireland, the non-resident surcharge was introduced in 2021, and adds two percentage points to stamp duty if the purchaser spends less than half the year in the UK. The surcharge does not apply in Scotland and Wales.

Yet at 2%, Britain's foreign buyers tax is modest compared to Australia, where combined housing sin taxes on non-residents approach 15% in some states, or Canada, where they can reach 25%.

But the same appears to be true in Australia. Although foreign buyers fell as a proportion of total demand for property from 16% to 3% between 2015 and 2021, this has since rebounded. An estimated 10.1% of demand for new properties came from foreign buyers in 2023.[38] This may have to do with increasing prices in Australia. Over the past twenty-five years, house values have increased 6.8% on average and have done so relatively steadily.[39] A 7% surcharge on stamp duty only equates to a little over a year's worth of returns. Federal charges on foreign home purchases are a one-time fee worth a maximum of 3% of the home, again failing to be sufficient to dissuade investment. While more regular taxes may decrease foreign demand, Australian land tax surcharges for foreign owners vary between 2% and 4%. This means a foreign investor can buy a home in Australia, forgo returns for the first 18 months, and see the investment reliably increase at 3% per year.

Although data is limited in Australia tracking non-resident property transactions, it appears they have not been able to slow price growth. Figure 16 shows home prices in Australia's six state capitals, all of whom had foreign buyers taxes instated at a state level at different points over the last eight years. The cost varied between 7% and 8% of the home's value.

Figure 16: Capital city home prices in Australia indexed to 2011

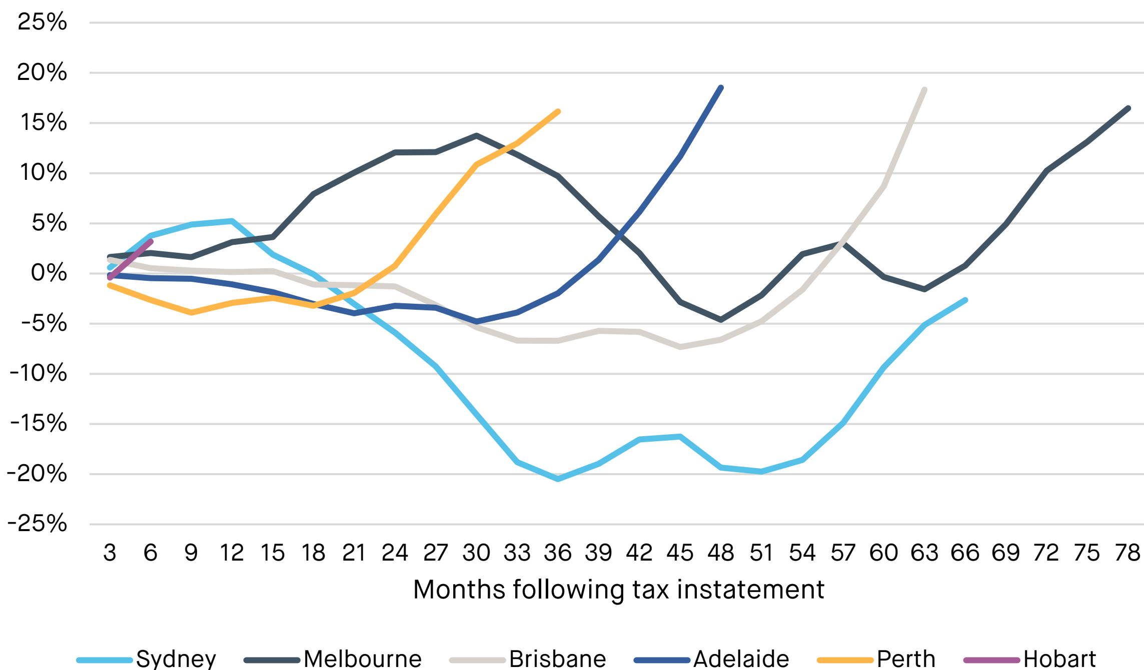


Source: ABS and SMF analysis[40]

It appears foreign buyer taxes failed to decrease price growth in each state, despite the higher rate set by Australian states relative to the UK experience.

Figure 17 compares the charts to show how much home prices increased or decreased in the months after the tax was imposed. Only Sydney saw a reduction in prices compared to the pre-tax trend which might have been ascribed to the foreign buyer tax, yet today these gains appear to be being reversed. In every other state capital, prices increased at a faster rate following the tax than the trend they had been on previously.

Figure 17: Percentage home prices were higher or lower relative to the pre-tax trend



Source: ABS and SMF analysis[41]

If the goal of foreign buyers taxes is to accumulate more money for the state, they have done so. But if the goal is to prevent foreign buyers altogether, they are failing. As long as taxes are set below the returns investors can reasonably expect to gain, they are incapable of decreasing demand at the scale required.

If policymakers really want to decrease foreign land purchases, they can ban them entirely, as has been done in New Zealand. In 2024, Canada banned purchases of land in high-demand areas by non-residents for two years. Both include exceptions in certain cases, but for the most part non-residents are unable to purchase land. Non-resident demand therefore falls by nearly 100%, with the effect on overall demand dependent on the relative size of the non-resident market. In England and Wales, close to 200,000 properties are owned by foreign individuals, amounting to 0.7% of the market. The benefits of such a boost would be welcome but limited, and it should be noted that any foreign buyers ban would apply to purchases rather than ownership, meaning it would take many decades to see an equivalent increase in stock. Many of these properties are also being rented out rather than left vacant, so while gains may be available to increase homeownership, the overall stock of housing in the country would remain similar.

That said, the financial benefits could be welcome. Between January 2010 and August 2021, non-resident individuals made 11,500 property purchases per year, not including Northern Ireland for which there is limited data. If these buyers paid the average house values in each devolved nation, the combined value of sales each year is worth £3.5 billion. A tax on this might not greatly cool the market, but could provide a useful source of revenue for the government.

Vacant housing taxes

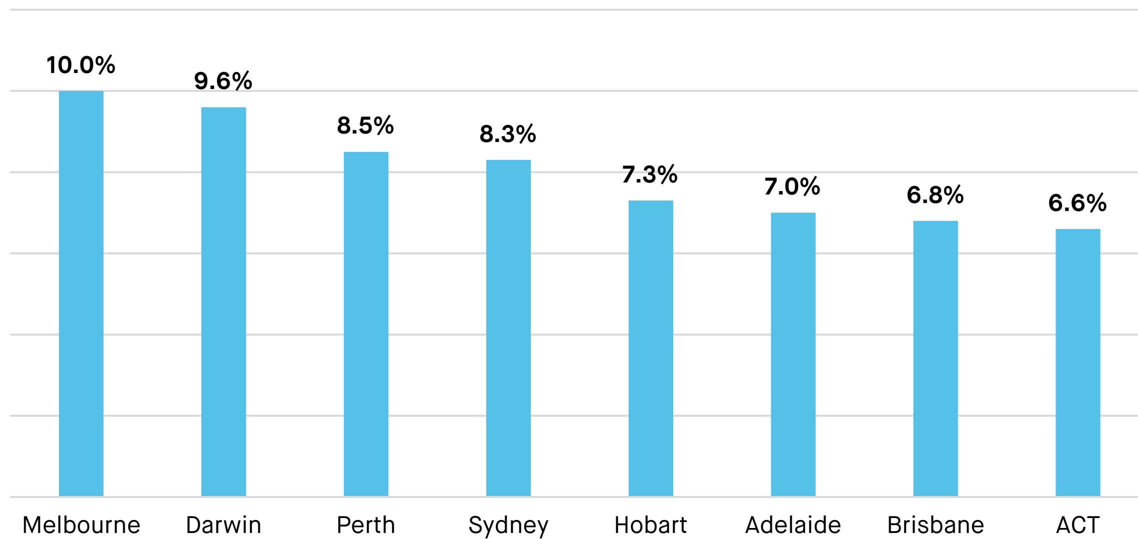
Vacant home taxes apply an additional tax for property owners who leave their properties vacant. This does not apply to owners who rent their property to tenants.

Vacant home taxes have similar issues to foreign buyers taxes. So long as home prices increase at a higher rate than taxes are set, owners make a profit (although of course that generates revenue for the government). Canada's federal Underused Housing Tax illustrates this difficulty, forcing owners to pay an additional 1% on the value of their home. Given that the value of Canadian real estate has increased by 7.5% annually since 2010, a tax of 1% means housing remains a valuable asset.[42] And it is difficult for policymakers to predict the pace of price growth beyond the short term.

In British Columbia, which instituted a vacant home tax of 0.5% in 2017, the effect was modest. In 2018 the tax applied to 8,920 properties, and by 2020 that number had fallen to 6,556, increasing provincial housing stock by 0.1%.

In Australia, the only state to impose a vacant land tax is Victoria. Since January 2018, the state has charged homeowners in 16 councils in Melbourne 1% of their property's value if it has remained unoccupied for more than half the year. Next year, the tax is expanding to include the entire state, with owners paying up to 3% if homes are left vacant over long periods. However, Melbourne has continued to see relatively high rates of vacancy. About 10% of Melbourne's homes are vacant, which is the highest proportion across Australia's state capitals.

Figure 18: Inactive dwellings in Australian capital cities (2022)



Source: AHURI[43]

Further, according to SQM research, in the month before the tax was imposed Melbourne's vacancy rate was lower than the national urban average. Yet today, six years after the policy was imposed, the city's vacancy rate has increased, and is above average.[44]

Like foreign buyer taxes, vacancy taxes tend to fail in their stated aim of increasing housing supply. This occurs for two reasons. The first is that taxes are set too low to shift incentivise owners to sell or fill their property. So long as investors can make more from growing property prices than they pay in tax, they are incentivised to do so given the safe investment real estate offers.

Secondly, they apply to too few properties, either because conditions for the tax are too restrictive, or because there are too few vacant dwellings. When it was imposed in 2017, Melbourne's tax was only likely to affect approximately 3,280 dwellings, while in Vancouver this number was closer to 9,000. Often, this is due to overestimations of inactive dwellings. In Ireland, the Census Statistics Office estimated there were 245,00 empty dwellings in the country, equating to 12.3% of the housing stock.[45] Yet this included 62,000 holiday homes, as well as those whose occupiers were away on holiday on census night, temporarily absent for medical reasons, refurbishing their property, or in between lettings. It is now estimated that just 3,000 homes, or 0.1% of the national stock, are eligible for taxation. Although any increase in stock is welcome, these numbers can do very little when compared to the scale of the problem.

In the UK, refurbishing these homes has limited returns. The charity group Crisis estimates that a strategic approach over four years to decreasing vacant homes could provide an additional 40,000 homes, increasing the English stock by 0.2%. It should also be noted such a policy could be expensive, costing £1.38 billion to finance renovations and refurbishments.

However, this could generate financial returns for the government. In the UK, there are an estimated 1.5 million vacant properties. Based on average home prices in each of the UK's devolved nations, a tax of just 1% on the value of these properties would raise £4.5 billion annually. Although it is likely this number would decrease when personal factors are taken into account as Vancouver and Melbourne experienced, the additional income from such a scheme could provide welcome funding to increase housing stock in other areas.

Vacant homes are a blemish on neighbourhoods and can frustrate homebuyers who see underused properties. But they are rare in the UK, which suffers less from vacancy than other countries in the Anglosphere. Although a vacant home tax is unlikely to greatly increase the availability of housing, it may become a useful source of revenue while slightly disincentivising vacancy.

Rapid sales taxes

Rapid sales taxes are designed to discourage "house flipping", when an investor buys a property and sells it quickly to make a profit. Profits may be generated from simple price increases or from renovation and refurbishment. Such sales have been blamed for increasing market prices and overheating the market, obstructing first-time homeowners from getting on the ladder.

Australia, New Zealand, and Canada all levy some form of rapid sales transaction tax to discourage rapid sales. Australia and Canada fully tax gains made from the sale of a property if it is sold within a year of the purchase, essentially denying sellers the benefit of capital gains tax exemptions. New Zealand has extended this rule to 10 years, meaning properties are taxed as income if sold within 10 years of the purchase. This rule may stretch the definition of "flipping" beyond its original intent, and under the new National government it may be rolled back to two years.

These policies were brought in recently, and it remains unclear how they will affect the practice of house-flipping as well as affordability. That said, if the goal is to reduce sales of homes to investors who will flip houses, it appears unlikely that the Canadian and Australian models will succeed. Real estate developers generally advise that selling a home can take one to three months in these countries. When combined with the time it takes to renovate or refurbish, and the pace of property price increases, waiting 12 months is unlikely to create a burden heavy enough to dissuade investors.

In Hong Kong, which implemented an additional tax for sales made within two years of purchase, rapid house flipping reduced by almost 90%, yet failed to cool the price of housing which saw an upward trend after the tax was imposed. This implies sellers were willing to defer sales until after the two year window to circumvent charges.[46] Singapore, which introduced a similar tax for sales made within three years, also saw a reduction in the reselling rate alongside an increase in selling prices, again implying sellers were willing defer sales. [47]

It remains unclear whether New Zealand's experiment will succeed. By increasing the term owners must wait to benefit from capital gains tax exemptions to 10 years, it is possible the state will finally dissuade speculative investors. However, as the law does not apply retroactively, it is still too early to tell whether it has had an impact on the domestic residential property market.

In 2022, house flipping (the proportion of homes bought and sold within 12 months) was estimated to include 26,340 homes, accounting for 2.3% of total England and Wales sales, up from 1.9% in 2021 but down from its peak of 3.7% in 2007.[48] While it is possible that cracking down on this practice might increase the market power of first-time buyers, it is unlikely that this would lead to price reductions unless the term imposed on house flippers was longer than they are willing to wait. In time, New Zealand's 10 year time frame may point a way forward regarding rapid sales taxes. however for the moment it seems unlikely that a real estate investor would not be willing to invest in a safe long term asset which can provide rental income in the interim. Instead, ending capital gains exemptions for investment properties may have a greater overall effect, as discussed in the previous section.

Recommendations

Replace council tax with regular taxation from councils based on a property tax re-evaluated every three years

Our council taxes are unjust, inefficient, and promote behaviour that is not conducive to an equitable market, failing on all three categories upon which property taxes are based. They are unjust because they allow richer homeowners to pay less as a percentage of their wealth, inefficient in that they do not allow for the proper funding of services, and they fail to disincentivise the types of property speculation that is driving increases in the price of a home.

The UK stands alone in this regard, and the bands which these valuations categorise property into remain the most simplistic and least reflective of value distribution. This experience also shows that it is electorally feasible for a party in power to update these rules without facing anger at the ballot box in the next election.

Council tax should therefore be replaced with a system of taxation more analogous to other countries in the Anglosphere. This would require two major changes.

The first would be to introduce a more regular valuation system to re-value every property every three years, based on its average value over that period. As in municipalities in Australia and Canada, local authorities would determine how much the coming year of services would cost, and charge a council tax on each property which would be proportionate to that home's value within the local authority. This would abolish banding and tax property owners on a continuum. This would ensure homeowners pay a fair amount for the value of their home and ensure councils receive a more steady income to avoid Section 114 notices, which effectively declare them bankrupt. Further, by re-adjusting every three years and charging residents on an average rather than on a single value, local residents would not be victim to temporary increases to their home's value.

Direct half of private tenants' council tax payments into a home deposit savings account

There is no other country in the Anglosphere which charges a local tax on those who do not own property. This is because in other countries property value is seen to increase in part as a result of local services, and taxes are seen as a fair charge for this public contribution to personal wealth. In the UK, local authorities charge tenants in the private rented sector the same rate as homeowners, despite tenants not seeing direct financial benefit from their property. This prevents tenants from raising the funds necessary to put down a deposit and escape from the rented sector.

Local authorities should direct 50% of a renter's council tax into a personal savings account. As previously laid out in a 2022 SMF report, the account would function similarly to the Help to Buy ISA as a government-protected savings pot.[49] Tenants would be able to save in this account over the long term and accumulate interest on their contributions. Savings could then be used to purchase a property on the market and enter into homeownership. Those who do not buy homes would have the option to withdraw their savings after a certain date or transition them into a pension fund.

Ringfencing half of renters' funding for personal use would decrease council tax revenue for local authorities. There are two ways this could be offset. The first would replace lost funds with increased rates for homeowners, thereby offsetting any losses and making the scheme revenue neutral. Alternatively, formula grants could be introduced from the central government to avoid increasing council tax. The latter method would also help offset any discrepancies that may result among some councils which have a higher proportion of residents in the private rented sector. A mix of the two, which sets a limit on the increased council tax on homeowners through the provision of formula grants, may be preferable. This is especially true where local authorities have a higher proportion of renters, such as major cities like Manchester (29%), Brighton and Hove (29%), Blackpool (26%) and London (26%).[50]

Abolish stamp duty

Stamp duty is paid by wrong parties in housing transactions and prevents efficient movement in the property market. These transaction taxes are likely to increase home prices and slow down home-buyers hoping to get onto the property ladder. As such, stamp duty should be abolished.

However, residential stamp duty currently brings in approximated 0.5% of the exchequer's annual funds, or £11.7 billion.[51] As a replacement, capital gains exemptions for secondary property sales should be abolished and taxed as income, cutting the cost of the policy down to between one and five billion.

According to a GetAgent study, the second home property market is currently worth £43.5 billion.[52] 35% of households own these as investment properties, 45% are used as a holiday home, with the rest used for other reasons. In 2022-23, capital gains axes were levied on 139,000 property owners disposing of 151,000 residential properties, resulting in a total liability of £1.8 billion. It is unclear how much of this came from owners paying the basic rate of tax and how much came from those paying higher rates. As such, ending capital gains tax exemptions on secondary properties could increase revenues between £6.4 billion and £10 billion. This would significantly help to decrease the cost of abolishing stamp duty while cooling demand for secondary homeownership, leaving more homes available for first-time buyers.[53]

Consider and design "housing sin taxes" on non-resident home purchases, vacant homes, and house flipping

Although housing sin taxes on foreign ownership, vacancy, and house flipping have failed to curb the practices or increase housing supply, they nonetheless can generate a useful source of revenue for the government.

In 2021, there were an estimated 181,000 properties in England and Wales owned by individuals with a correspondence address outside the UK, having increased by about 10,500 per year since 2010. An additional 20,000 are in Scotland, which if it followed a similar trend to the rest of the UK increased by almost 1,200 per year on average. Northern Ireland does not collect data on the issue. Assuming these are residential properties worth the average cost of homes in each respective devolved nation, a 25% tax based on the value of purchases made by those not resident in the UK would bring in an additional £855 million for the exchequer. This could be captured by increasing the surcharge on stamp duty land tax, currently set at 2%, as the Labour party announced it was considering in the spring 2023.[54]

Taxes on vacant homes encounter a similar issue. While they are unlikely to redistribute housing or greatly increase housing stock, they can provide a new source of government revenue. There are approximately 1.5 million vacant homes in the UK according to the 2021 census and its devolved equivalents. However, many of these may be recorded as vacant despite having a resident. These cases may include those who were not available when the census was taken, who may be away for temporary reasons like studying, and other reasons that make cataloguing vacant homes notoriously difficult. Regardless, the benefits from such a tax could be large. If these vacant homes are worth the average value in their devolved nation, a relatively small 1% tax would generate £4.5 billion per year. While the data remains uncertain or unavailable, the potential rewards of such a policy warrant further study given the benefits and likely distribution of such a tax.

Lastly, taxing house flipping could prove lucrative. Data is scarce, but in England and Wales, real estate agency Hamptons estimates that 26,340 homes were flipped in 2022, and that owners made an average profit of £42,800 per home. That means a 50% tax on profits generated on these home sales would raise over £550 million in England and Wales alone. Given the experience of Hong Kong and Singapore, the real-world proceeds of such a tax would likely be lower, as purchasers would delay the sale to avoid taxation. As such, the threshold to avoid the tax should be set higher, both to capture a wider share of the value uplift and to decrease the attractiveness of house flipping to investors.

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