funding housing and local growth

how a British investment bank can help

By Dr Nicholas Falk

THE SMITH INSTITUTE

The Smith Institute

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Dr Nicholas Falk

Nicholas Falk is the founder director of URBED (www.urbed.coop), which he set up as a research and consultancy group in 1976. This followed work as a management consultant for McKinsey and Company, and as a Senior Research Fellow at the London School of Economics, where he secured his doctorate. He has helped start a number of companies, such as the London Small Business Property Trust, to demonstrate better solutions to the problems of urban regeneration and local economic development. He has previously contributed to Smith Institute publications such as *Housing and Growth in Suburbia*.

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T H E   S M I T H   I N S T I T U T E

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Executive summary

How are we to double our rate of house building without fundamentally changing the delivery model? This pamphlet shows how by setting up a Municipal Investment Corporation (MIC), linked to the proposed British Investment Bank (BIB), appropriate sites and private investment can be mobilised in ways that will not only boost small businesses but also help cut energy and transport costs and pollution. This would achieve what people in all political parties have long argued - a system that looks toward the future, as well as takes account of externalities or wider considerations rather than simply profit and loss. Most people do not want growth at any price but smarter growth that leaves a richer legacy for future generations by linking new housing with jobs and infrastructure.

The funding chasm

This pamphlet argues that the urgent priorities of building more homes, upgrading our worn out infrastructure, and promoting local economic growth together demand radical changes in the way major development projects are designed, promoted and financed. The volume house builders say they can only build around 150,000 a year - that is the on-trend level achieved over the last few decades, and prefer to build on the smaller and less risky sites. There is a gap of some 50-100,000 homes to be plugged, whether by new towns, garden cities, or urban extensions, and through housing associations and small builders, as well as local authorities and self-builders. At the same time investment is needed in local solutions to getting to work easily and cutting energy bills to keep living costs down.

The first section shows that the deficiencies in private banks, which nearly brought down the world financial system, have been reinforced by failings in the way public investment decisions are made in the UK. The costs of local infrastructure, such as a new roundabout on a main road, can often exceed the costs of building the homes, and require funding upfront. Land values, which should follow development, are ratcheted ever upwards by 'hope value'. We need to crack the problems of unrealistic land values and funding local infrastructure before we can achieve any of the housing, economic and environmental goals that have been set in recent years. A different approach is needed to make the numbers add up, and hence build on the scale required.

Funding sources

The second section examines where the extra funding can come from. It is going to be vital to find better ways of mobilising private investment in upgrading our infrastructure and building new homes as public finance becomes ever tighter. Fortunately there is a large potential supply of long-term private finance through savings for pensions. But simply freeing local authorities to raise large sums of finance on the private markets, for example through a Municipal Bond Agency, will not by itself produce better long-term investment projects that the Treasury would support.

Though examples of good development can now be seen in many cities, we need a larger supply of good projects to finance, and this requires access to appropriate sites at the right prices, along with appropriate planning permissions. A substantial increase in the rate of house building cannot be achieved simply by the use of more brownfield sites, or the redevelopment of existing council housing estates. Some growth is also required in the locations where people would choose to live because they can reach jobs, services, and open space.

Much of the resistance to new development on the edge of town in the Greater South East is due to legitimate concerns over the quality and the capacity of local infrastructure. Hence filling the gap also depends on building quality urban extensions, possibly to 'Garden City' standards, in places served by public transport, or agreeing to fund infrastructure improvements as part of a 'quality deal'. In some cases this means taking land out of Greenbelts where it is best located for development, but improving it elsewhere. It also means freezing land values where land is designated for housing, as in Germany, so that some of the uplift from development can be used to help fund local infrastructure.

While 40% of the large sites that the government considers suitable for development may be owned by the public sector, much is in locations that are not easily accessible to jobs and services, such as former airfields, rather than sites alongside railway stations or transport corridors. Nor will development corporations offer the complete solution, as the high costs of providing completely new infrastructure rule out building more than a few new towns in locations opened up by new railway lines. It is vital to join up development with available or planned infrastructure, but we lack the mechanisms. This requires changes in the way major sites for development or regeneration are brought forward.

European models
The third section shows how other countries have done much better. It brings together fresh case studies of how state investment banks and strategic planning work in France (Caisse de Depots), Germany (KfW) and the Netherlands (BNG). These examples show how the UK could release the potential growth locked up in local communities. Despite different financial and political systems, these three countries

(along with others in Scandinavia and many other parts of the world) all see the value of some kind of state investment bank with five main features:

- A commitment to funding major housing schemes that meet demanding environmental and design standards and hence meet the most serious local objections
- Sufficient expertise to assess and evaluate both the projects and the borrowers, and hence avoid the mistakes that private banks made in backing ill-conceived property development schemes in the upswing of the business cycle
- The capacity to help fund land assembly, master planning, and the release of sites and plots to a multiplicity of builders
- Good ongoing relations with local authorities, housing associations and banks that finance small businesses, and hence the ability to know about local needs and capacity in all parts of the country
- A large enough base of assets and investments to survive financial ups and downs and smooth out funding, and hence avoid the side effects of the financial crash that led to a period of 'austerity'.

How a Municipal Investment Corporation will work

A British Investment Bank (BIB) as proposed by IPPR and Nicholas Tott is one of the policy ideas that the Labour Party is considering.[1] A similar proposal has also been advocated by the centre-right think tank Policy Exchange to fund energy solutions, and is in line with the ideas of those like Lord Heseltine who believe radical institutional changes are needed to enable local growth across Britain.[2] Focussed on assisting housing delivery through land assembly and the provision of local infrastructure as well as the growth of SMEs, it would be the single best way of changing direction from austerity to posterity, as it meets a number of policy goals simultaneously. It would overcome the failings of the prevailing financial system as far as new homes are concerned, and could help make housing both better and more affordable.

This pamphlet goes further in proposing that a MIC should be established in collaboration between major local authorities (or city regions) and the Treasury on the model of the Dutch BNG Bank, the world's second safest bank after the German

1 Nicholas Tott, *The Case for a British Investment Bank*, Labour Party Policy Review, 2012
Tony Dolphin and David Nash, *Why We Need a British Investment Bank*, IPPR, September 2012
2 Dieter Helm, James Wardlaw and Ben Caldecott, *Delivering a 21st Century Infrastructure for Britain*, Policy Exchange, 2009

equivalent KfW.[3] It would aim to provide a large source of capital funding that would incentivise local authorities to promote housing development and local growth their areas need. A greater supply of serviced sites with planning permission would open up much more choice and competition in a housing market that is currently failing. It would also get the economy moving in ways that would be both fairer and more sustainable by opening up more opportunities for small businesses and community enterprises. Cities would regain some control over their destinies. It would also make better use of the accumulated pension pots and housing wealth owned by those of pension age, and provide higher and inflation-proofed returns than are currently available.

As development of major sites can take several decades, any proposals for change need to win support from future governments of all complexions. This means making the most of existing institutions, such as the Homes and Communities Agency, and also the City Deals that are being negotiated between government and some 28 local authorities, to ensure that long talked about schemes move ahead. This will support a long overdue shift towards devolving power away from central government, and enabling 'third sector' or local initiatives to flourish. A more contractual approach that generates confidence and reduces controllable risks and uncertainties should be welcomed by the private sector, rather than the project by project approach that has been found wanting. Our public bodies have to relearn strategic planning.

A MIC would fill the gaps in seven main ways:

- distinguishing the good projects from the bad ones, and channelling more investment into locations where the conditions for long-term economic growth are right
- de-risking complex projects, for example only lending money where local authorities are committed to allocating appropriate sites, and providing the necessary soft infrastructure, such as schools
- taking a longer-term perspective than the private sector, for example giving more weight to investments that reduce energy consumption and hence fuel bills (and carbon emissions) than a private investor would
- tapping private investment by demonstrating commitment on where development is to take place (and where it is not welcome)
- mobilising public investment by joining up public investments in local transport and energy solutions with related developments

3 Global Finance, 2013

- encouraging collaboration between adjoining local authorities and utilities by supporting sound long-term investment plans
- and ultimately raising our levels of growth and wellbeing to those of comparable European cities and city regions by building the capacity to plan and act for the longer term.

Hence a MIC will supplement, not displace, local government. Many local authorities are already starting to look more imaginatively at making the most of land they own, and at the potential for working in partnership with other organisations. But they will only be able to tap private funding on the scale required by agreeing a spatial plan that identifies appropriate sites for growth and regeneration in the sub-region. By adopting a similar system to the one that has worked so well in Germany and other Northern European countries, Britain will be in a much better position to increase levels of investment, rather than just house prices. Pensioners too will be able to see their savings used to produce tangible benefits, rather than chasing short-term gains.

Finally success almost always depends on strong and continuous local leadership to explain how the benefits will exceed the costs (as officers and politicians have done to good effect in Continental growth cities such as Freiburg and Amersfoort). A MIC will therefore play a key role in devolving power from London. It will then enable cities to reap the benefits from smarter growth where development is matched with infrastructure. A MIC as a subsidiary to a BIB, modelled on the best European experience and jointly owned by central and local government, could make a significant difference to both the quality and scale of growth. This paper shows there are real benefits to having such a state investment body, not least to secure a step change in house building. The question should be not *why* we need a MIC but *how* it will get operational as quickly as possible.

Section 1

Why a new model for development is needed

Why a new model for development is needed

Government can encourage increased production by reducing the risks and increasing the opportunities for investors in the industry; Government can specify outcomes, such as good quality or environmental performance, but should allow the industry to determine the best means.

John Callcutt, The Callcutt Review[4]

This pamphlet shows how by putting together the capacity to devise and assess good development projects in the right places, supported by a MIC, private investment could be mobilised to double the current rate of house building, and to build neighbourhoods that are truly sustainable.[5] It seeks to answer four related questions: why is a new model needed for housing development, how do you grow more successful places, why do other countries do better, and what can be done to make the numbers add up in the UK? The simple answers are:

1. Provide infrastructure upfront
2. Pick the right places for smarter growth, such as urban extensions in locations with growth potential
3. Mobilise local authorities through local investment agreements that pull together all public funding
4. Tap private funds for collective investment through a new corporation set up by local authorities and government to back growth projects.

The sections that follow show how these principles can be made to work. The first section analyses the roots of the housing problem, and shows how it requires action that extends far beyond changes in planning to the roles played by local government and other stakeholders in building for the future. The second examines the weaknesses in both private and public approaches to investment in the UK in recent decades, and the potential for harnessing pension fund investments. In the third case studies from three countries that have been particularly successful in investing in infrastructure and new homes, show how state investment banks play the missing role.

The final section shows how the development process can be made to work much better. The proposed BIB would be an active participant, through the formation of a MIC with support from leading local authorities as well as the government (or Bank

4 *The Calcutt Review of Housing Delivery*, ODPM, 2007
5 Richard Rogers et al, *Towards an Urban Renaissance; report of the Urban Task Force*, Spon 1999

of England). It illustrates the benefits the new organisation would offer by explaining how each stage of the development process can be improved. This does not answer every problem. It does not seek to explain how strategic planning can be reinvented, or the benefits or shortcomings of the return of the Business Rate to city regions. Nevertheless it would enable visions for our cities to be turned into hard reality.[6]

1.1 The roots of the problem

Radical and long-term changes are needed in the way Britain funds housing and local infrastructure if we are to accelerate the rate of building, and also create places of lasting value. While there are now plenty of good examples around the UK to show how mixed tenures and higher standards of design can be achieved, and even some innovative schemes that save energy and water, we have lost the capacity to 'go to scale'. Though there is broad agreement on the need for growth in the right places, there is little consensus on how the formidable barriers to growth are to be overcome. The last recession has decimated the capacity to plan and execute ground-breaking developments.

It leaves young people in the UK struggling to place their first foot on the housing ladder, whilst poorer older homeowners struggle to find suitable properties to downsize to and are stuck in homes they can no longer afford to heat or maintain. A return to 'business as usual' simply will not close the chasm that has opened up since a median home came to cost 6.5 times moderate earnings in 2012 versus 3.5 times in 1997.[7]

Some hark back to the 'garden cities' for inspiration, and want to free up the private sector or encourage the use of a third sector of not for profit trusts. It has taken the intervention of the Chancellor of the Exchequer to get development moving at Ebbsfleet after some seventeen years of talk. Others refer to the new towns built after the last war, and the importance of having dedicated multi-disciplinary teams with the money to acquire land and install infrastructure. But there is an even longer tradition, such as the great estates in central London in places like Bloomsbury or in Edgbaston in Birmingham that demonstrate the importance of long-term plans with high design standards. An ABC of Ambition, Brokerage and Continuity underlies the schemes we admire most, as a series of case studies of major recent schemes illustrates.[8] This is because development of major housing schemes, unlike other forms of economic activity, usually takes well over ten years, and regeneration takes a generation. As

6 Both the Lyons Housing Review and the Adonis Growth Review are considering ways of accelerating growth and resolving the problem of development land lying idle.
7 'Call to judge success by average pay', Larry Elliott in *Guardian* report March 12, 2014 of Fabian Society pamphlet
8 Nicholas Falk and Barry Munday, *ABC of Housing Growth and Infrastructure*, Housing Forum 2014

the British successes in securing, constructing and then winning the Olympic Games confirms, we can still do big projects, provided we organise for the task in hand!

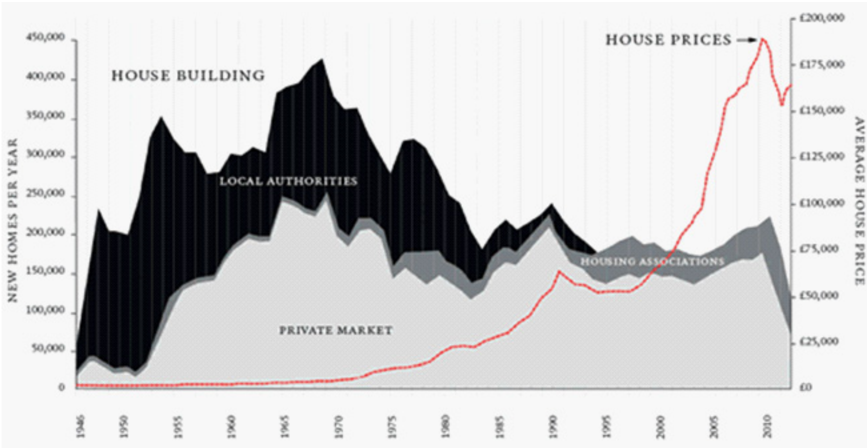
In his powerful report on unblocking the barriers to growth, *No Stone Unturned* Michael Heseltine argues compellingly for giving local authorities a proactive role by trusting them to raise finance. He recognises that the UK is far too centralised, so that cities have lost their resilience and capacity to shape their destinies. Opposition Parties often talk about reforming property taxes and devolving power, but once in power Ministers become distracted and less enthusiastic about letting go. It is therefore essential to use the period in the run-up to a General Election to work out how to overcome the failings in the current financial and development situation.

The Labour Party has commissioned a review led by Sir Michael Lyons into the housing crisis, which includes looking at 'what are the barriers to private investment and what part can institutional investment play.[9] Lyons' work will no doubt build on that of John Callcutt, former Chairman of housing developer Crest Nicholson and also English Partnerships. The Callcutt Review argued in his well-researched report on housing delivery, that we need a new 'investor' model for house building. This he concludes would supplement the 'trader' model of land speculation that has led to a handful of house builders controlling most of the supply, and effectively forming an oligopoly in many areas, and take away some of the risks that require high profit margins.[10] The need for radical change has been put forward by all ends of the political spectrum, with few doubting the need to build on a much larger scale, while many think that changes are also needed to the way social housing is funded, so it does not depend on private house builders.[11] The size of the problem is well charted by James Meek in a recent essay, which includes the correlation between the recent rise in house prices and the decline of housing output, based on figures from Sheffield University.[12]

The implication of the Callcutt Review was we cannot wait for developers who hope to benefit from increases in land value. We need better ways of bringing together the upfront finance to assemble and prepare appropriate land, within agreed spatial and investment plans. This will make it possible to sell plots off to house-builders of many more kinds and set up the long-term management arrangements to achieve mixed communities that really work. The developers should of course include small

9 The Lyons Housing Review, A Call for Evidence, December 2013
10 *The Callcutt Review of Housebuilding Delivery*, HMSO 2007
11 See for example Highbury Group on Housing Delivery evidence to the Lyons Housing Review, 2014 www.westminsterac.orguk
12 James Meek, *Where will we live: the housing disaster*, London Review of Books 9th January 2014

House building, 1945-2010

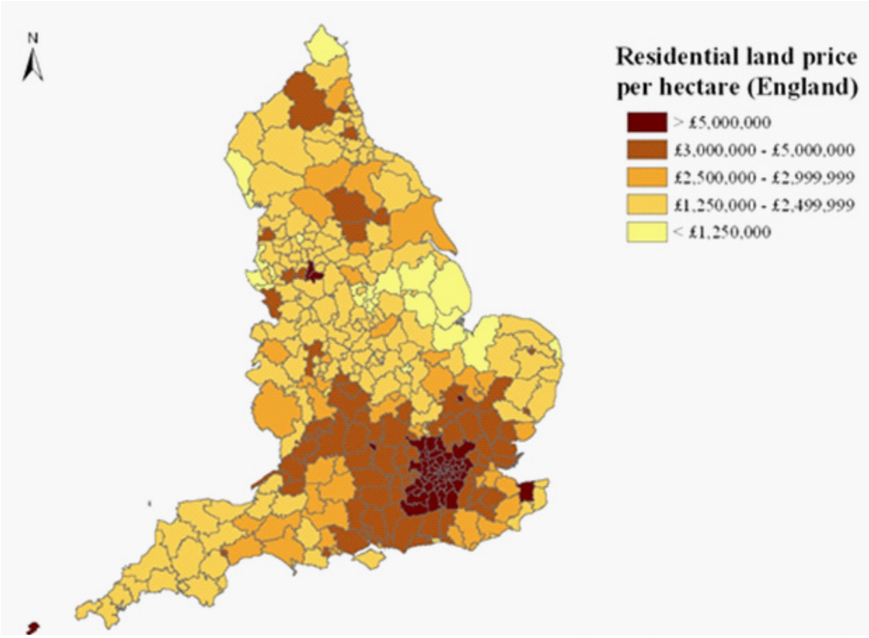


Source: A Parvin et al, *A right to build*, University of Sheffield School of Architecture, 2011

builders (who have shrunk from 12,000 to 3,000 in twenty years, and now account for only a third compared with two-thirds of housing).[13] Many have been bought up by their larger rivals, creating an effective oligopoly through the limited number of major house builders who operate in any one area, five of whom account for half of national production. A huge increase in the output of housing associations is also called for (who account for a half the new homes in the Netherlands). We also need local authorities to build on land they own, and new types of developer, such as cooperatives and custom builders. To rely on volume house builders, a few Treasury backed experiments or philanthropic largesse will not enable the annual rate of house building to match household growth – at 230,000 per annum compounded with a current build rate of just 140,000.

Such an approach also needs to crack the ongoing problem of land values, which have far outstripped house prices, and which reflect the real divisions within England and the United Kingdom. It is what Ebenezer Howard called the 'Unearned increment' that lies behind successive property booms and busts, and which is largely to blame for the period of austerity the country has endured since 2007. The problem is bound up with the very uneven spatial distribution of wealth in the UK, where so much radiates around London as the map of land values clearly shows.[14]

13 Figures quoted by Sir Michael Lyons at the Fabian New Year conference, January 25th 2014
14 This chart comes from work by Paul Cheshire, and a presentation for the Wolfson Essay Prize in January 2014



Source: Paul Chesire, blog

The hope of making large profits from a change of use motivates many developers. The GLA estimates that some 40% of the 10,000 sites identified for housing development in London will never be developed by their owners.[15] As we shall see, other European countries have avoided the 'irrational exuberance' which has fuelled spates of development in the UK and USA. This is partly because local authorities play a much more proactive role in determining what gets built where, but also because other cities have much stronger economies, and lead rather than lag behind their regions, as Michael Parkinson has long demonstrated.[16] The changes needed to produce more and better housing are also those which will free cities from the burdens of excessive central control.

As Michael Ward points out in his review *Public Services North: time for a new deal?* the time is ripe for a rethink on how to fund local authority services, if only to overcome the 'Graph of Doom' in which local authorities start imploding as their revenue

15 The source is work being undertaken for the Greater London Authority
16 Michael Parkinson, *Second Tier Cities in an age of austerity: why invest beyond the capitals*, 2013,

sources dry up while their commitments continue to grow.[17] This financial squeeze is leading to a more adventurous approach to local government finance by some local authorities which are starting (or indeed have no choice) to make more use of their land and borrowing powers. The income from business property taxes – the Non-Domestic Rate – which is now shared with government - is starting to be used to borrow for investment through some form of Tax Increment Finance and 'Earn Back', as Manchester and Cambridge have negotiated with the Treasury. Others will no doubt follow.

Local authorities can also now borrow against their Housing Revenue Account, but have complained about the prudential borrowing gap. They would need to raise another £7 billion over five years (£4.2 billion more than existing headroom) even to produce an additional 12,000 homes a year.[18] But borrowing only helps if the funds can be repaid. Hence there needs to be a step change in local economic growth to tap the full value of local infrastructure, along with measures to generate vastly more viable development projects. This means supporting growth in the very places that have tended to be most resistant to any development, such as Central Oxfordshire or York, and utilising public land much more imaginatively. It also means joining up development and infrastructure investment with changes in the way property taxes are used (perhaps in the ways proposed by the London Finance Commission, and by the Core Cities).[19]

The progress being made in some places in negotiating City Deals and tapping local authority pension funds offers an excellent starting point for the 'investor model'. So does the success of the Homes and Community Agency in unblocking a number of major schemes to 'get Britain building'. But the scale at present is too small to meet the challenges, and the approvals system is far too centralised. Major housing developers such as Crest Nicholson and the Berkeley Group have found the long-term risks too great to make it worthwhile to start major regeneration projects unless the public sector provides the funding to get started. More schemes will need to be de-risked if the finance is to flow, and more homes are to be built. We have to learn again how to act strategically at local and sub-regional levels.

1.2 The funding chasm

As is widely recognised by people on all political sides, the UK needs simultaneously to build more affordable homes, to upgrade our worn-out transport and energy

17 Michael Ward, *Public Services North: time for a new deal?* The Smith Institute, 2013
18 *Local Housing Authorities – the self-financing regime: progress and issues*, House of Commons Library, December 2013
19 Tony Travers, *Raising the Capital: Report of the London Finance Commission*, 2013

infrastructure, and to rebalance our economy away from its over-reliance on London and the South East. All require a step change in the way we fund and select investments projects, and are inter-related. The scale of the funding gaps looks truly frightening at first sight. The UK, for example, has the oldest houses in Europe, with only 10% built since 1991.[20] Most are inadequately insulated, greatly increasing our fuel bills and carbon emissions. The UK is at the bottom of twelve European countries for fuel poverty, and the impact will get worse as energy bills continue to outpace inflation.[21] Not only are we building far fewer homes than we need, but the new homes are much smaller than those built in the rest of Europe, and most are not designed for growing families. Doubling the rate of building means not only finding much more land for new housing, but also doubling the rate of investment at a time of fiscal constraint.

New funding mechanisms are required if development sites are not to fester, because the upfront costs in getting going are so large. The initial cost of redeveloping a large failed council estate or brownfield site can easily exceed £50 million.[22] Building a new tram line can cost £25 million a mile when utilities have to be replaced, while the Guided Busway that is opening up development sites in Cambridge has involved well over £150 million. District heating and Combined Heat and Power are feasible and can cut energy costs, but only on larger and mixed schemes, and require investment upfront in providing ducts alongside the new roads.

New housing schemes on the edge of existing towns and cities could cut the demand for energy by making use of renewable and local solutions, and by cutting transport times and costs, and in some areas could be linked to upgrading failing council estates. A number of organisations agree that around £500 billion needs to be invested in energy, transport and water alone over the next decade or so simply to maintain current standards. The backlog of work to be done, according to the McKinsey Global Institute, would provide a much needed boost to the British economy.[23] About half of the infrastructure finance, according to Oxford energy expert Dieter Helm's calculations, is needed for energy to avoid the lights going out. Without that investment, 'a ruthlessly competitive global economy and the challenges of climate change mean that sticking plaster updates are no longer sufficient. The UK is in need of a step change in its infrastructure provision.'[24]

20 Building Performance Institute, Europe

21 Association for the Conservation of Energy, quoted in the Guardian 30/11/13

22 See case studies in *The ABC of Housing Growth and Infrastructure report and case studies*, www.housingforum.org.uk, 2014

23 McKinsey Global Institute, *From Austerity to Prosperity: seven priorities for the long term*, 2010

24 Dieter Helm, James Wardlaw, Ben Caldecott, *Delivering a 21st Century Infrastructure for Britain*, Policy Exchange, 2009

Whereas Dieter Helm estimates that £136 billion needs to be invested in renewables his costs for promoting energy efficiency measures are comparatively small – around £21 billion. A new home could save around £1,400 a year on energy bills according to a study by the NHBC and the Zero Carbon Hub, based on figures from the Department of Energy and Climate Change.[25] Energy costs will inevitably rise over time given global competition for limited resources.

Successive governments' attempts to get energy companies to organise and fund the upgrading of existing homes have not worked. Nor have incentives to get private house-builders to build much more, or to fundamentally change what they build. The target of building 250,000 homes a year, or twice the current level, to high environmental standards simply cannot be achieved through the prevailing centralised system, as Shelter has persuasively argued.[26] So many of the answers lie in a return to municipal enterprise, but operating at the city region level. However localism without access to locally generated resources does not work. As Paul Hildreth points out in a useful review:

Despite the rhetoric of localism "we want powerful innovative cities that are able to shape their economic destinies, boost regions and get the national economy growing" HMG, 2011, the tone of 'City Deals' remains conditional and dependent on cities offering something in return: that is "we will give you additional powers if you prove yourself". In practice, Whitehall is uncomfortable with devolution. England remains a highly centralised country.[27]

Experiments such as Oxford's Low Carbon Hub or the work of the Manchester Low Carbon Coop show the importance of organising at a local level and the potential for saving energy to play a key role in improving ordinary people's quality of life and living standards. However in looking for solutions it is vital to distinguish between growth and regeneration areas, and to adopt policies that match the very different economic circumstances facing different parts of the country. As the analysis in *Good Cities, Better Lives* shows, there are at least four quite distinct economic geographies in the UK. What might work in London and the Greater South East, for example by building at higher densities, is quite irrelevant to most of the rest of the country, where property values are much lower, and development costs often higher, thanks to the consequences of de-industrialisation, such as contaminated land.[28] Rural areas face quite different issues to urban areas.

25 Statement by Director of NHBC with the Zero Carbon Hub

26 Shelter, *Solutions for the Housing Shortage*, 2013

27 Paul Hildreth and David Bailey The Economics behind the mover to localism in England, *Cambridge Journal of Regions Economy and Society*, March 2013

28 Peter Hall with Nicholas Falk, *Good Cities, Better Lives: How Europe discovered the lost art of urbanism*, Routledge 2013

Best value from limited investment resources can only be achieved by looking at development in the round at a sub-regional level, as other countries do. Simply ranking schemes nationally in terms of some form of Cost Benefit Analysis is intrinsically flawed because it fails to take account of agglomeration costs and values. As the former Chief Economist to the Greater London Authority Bridget Rosewall points out in her recent book:

There are two challenges, therefore, in thinking about the payback to infrastructure investment. One is to establish what constraints are imposed on future developments by not undertaking the investment, while the other is to value the consequent growth.[29]

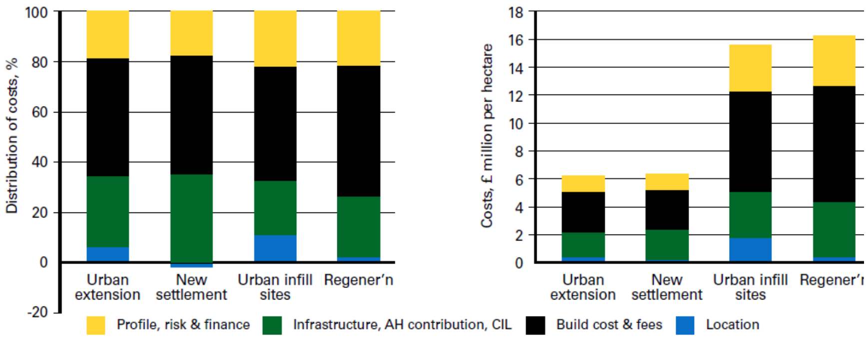
Viability, as every surveyor knows, depends largely on location. In many parts of the UK where industry has declined, the values for a new home will be insufficient to overcome the risks and costs involved in development even if the land was given away. In regeneration areas such as in Manchester or Newcastle, though land values may be low, build costs can be much higher as a result of remediation works to deal with contaminated land. Demand will be higher in infill locations, and on the edge of villages, where there is already local infrastructure in the form of the schools, shops, open space, and access to jobs and services that people value most when looking for a home.

As the chart opposite shows, extending existing settlements is generally far more viable than trying to build from scratch.[30]

Infrastructure costs can be as great as the costs of construction, and are only recoverable over a long period. Greater levels of public investment in infrastructure such as transport and energy help explain why European cities have grown faster and better than their English equivalents, and why the gaps between their capitals and second tier cities are much less.[31] For good infrastructure is key to retaining talented young people. Reduced time spent travelling to work creates higher wellbeing as people can spend more time with their families or on leisure pursuits. Reduced energy bills enable people to live fuller lives. Indeed living at higher densities can also add to social capital, as people develop closer relationships with each other, which contributes to the renaissance in city living.

29 Bridget Rosewall, *Reinventing London*, London Publishing Partnership, 2014
30 This chart has been produced by Pete Redman of Traderisks, to whom I am very grateful, and draws on national statistics as well as local knowledge
31 Michael Parkinson, ESPON SGPTD: www.ljmu.ac.uk/EIUA/second-tier-cities

Distribution of residential costs



Conclusion

So long as housing is looked at in isolation, it will be hard to make development viable of the scale and quality required. It is no longer feasible to fund a whole range of benefits such as affordable housing on the back of building new private housing. By looking at the bigger picture in terms of transport, energy and biodiversity, very different results can be secured from the larger sites, which now need to be deployed. But what might work in parts of London may be irrelevant in Liverpool. This is one reason why local authorities need to play a much more proactive role as far as allocating and even servicing major development sites is concerned and in setting development priorities. Some form of development corporation may also be needed where there is deadlock, given the scale and complexities of the task, as many strategic sites are near rivers and straddle authority boundaries, and reclamation costs for brownfield sites can be high.

Section 2

How smarter growth would help

How smarter growth would help

Much more of the inspiration for our economy should be based on the strength and ambition of our cities and their communities. It was this local leadership that built our country in the first place.

Lord Heseltine, *No Stone Unturned*

The funding chasm in the UK is partly due to low productivity, but also because for decades the UK has been investing much less than our Continental counterparts in new housing and local infrastructure. We have neglected the towns and cities that should have been the 'engines of growth'. Household borrowing has supported higher levels of consumption than we can really afford and boosted land values and property prices especially in the Greater South East. It has also greatly widened inequalities, as Danny Dorling brings out in his latest book on the housing crisis.

2.1 The case for smarter growth

Housing accounts for half of national wealth in Britain, according to Thomas Picketty - more in France and Germany.[32] Housing is worth £5.5 trillion, of which about a quarter is in London, and £4.5 trillion is unencumbered by mortgage debts, according to Hometrack.[33] Half of all the wealth in owner-occupied housing belongs to the baby boomers, according to David Willetts, MP in his provocative book *The Pinch*; those over 65 are estimated to have over £800 billion tied up in their homes.[34] Others talk about £400 billion, and surveys for Demos suggest that the majority of pensioners would be interested in moving if somewhere suitable was available. Whatever the true facts, there is a lot of potential wealth to be tapped if the right investment opportunities were available! There will be even more now that pensioners no longer have to lock up funds in an annuity, as a result of the 2014 Budget.

Regional and social disparities have widened, as those old enough and lucky enough to own their home have received an untaxed dividend. Successive governments hoped that opening up markets, and reining back the role of the State would somehow fill the gaps. They looked enviously at the apparent ability of North America with its liberal institutions to create new jobs to replace those that were lost when industries declined. In fact the model was flawed, as the collapse of industrial cities like Detroit has highlighted. Many US cities are crippled by debt obligations, and urban flight. Their

32 Thomas Picketty, *Twenty-First Century*, Harvard University Press, 2014
33 Danny Dorling, *All That Is Solid: the great housing disaster*, Allen Lane, 2014
34 David Willetts, *The Pinch: how the baby boomers stole their children's future, and why they should give it back*, Atlantic Books, 2010

suburbs have sprawled, and guzzle huge amounts of oil and concrete to keep them going. And inequalities exceed those in the UK.[35] A more compact form of city is intrinsically more sustainable, so long as there is a balance in the income levels of those who occupy the residential areas.

Many in the UK are understandably against growth that is unsustainable or that destroys what many most value, such as beautiful countryside. Smart Growth, a term originally coined by the Congress for New Urbanism,[36] describes a better form of development that minimises environmental impact and that secures social benefit; it has been expressed as a charter to guide development that many authorities are adopting (www.cnu.org). A similar set of principles has been promoted in the UK by a number of bodies, including the influential Campaign to Protect Rural England (CPRE), though limited to building on brownfield land. The idea was summed up in a McKinsey Global Institute report on what makes a city great, where smart growth forms one of three key themes:[37]

Smart growth depends upon a strategic approach that identifies the very best growth opportunities and nurtures them, planning so the city and its surroundings can cope with the demands growth will place on them, integrating environmental thinking, and ensuring that all citizens enjoy their city's prosperity.

The concept of smart growth is also being promoted through the European Union as part of their Cohesion policy for the period 2014-20, to link economic and spatial development more closely and avoids society becoming further polarised. Integrated Territorial Investment Strategies will access loan funds as well as grants. The European Investment Bank already prioritises affordable housing and renewable energy, and is looking to invest in packages of over £100 million put forward by local authorities or other public bodies. The guidelines for territorial investment call for careful targeting:

Smart specialisation means identifying the unique characteristics and assets of each country and region, highlighting each region's competitive advantages, and rallying regional stakeholders and resources around an excellence-driven vision of their future.[38]

35 Richard Wilkinson and Kate Pickett, *The Spirit Level: why more equal societies almost always do better*, Allen Lane, 2009
36 The Congress for the New Urbanism (CNU) is the leading American organisation promoting walkable, mixed-use neighbourhood development, sustainable communities and healthier living conditions
37 McKinsey Global Institute *How to Make a City Great*, 2013
38 Integrated Territorial Investment guidelines, EU 2013

Smarter growth involves investing in projects that boost productivity and support a more sustainable way of life, one that both our grandchildren and poorer nations will appreciate as they use less non-renewable resources. This is only possible through reinforcing existing towns and metropolitan conurbations, as Harvard economist Ed Glaeser convincingly argues, and not building small housing estates that sprawl all over the countryside as Britain has been doing.[39] By investing in home improvements or new homes that use little or no energy (passive houses), or building homes where residents can reach jobs and services without adding to congestion, or funding rapid transit systems in dense enough neighbourhoods, society benefits in social and economic as well as environmental terms. At the same time our addiction to house price inflation and excessive consumption on credit cards can be reined back. So smarter growth should benefit all, and anything else can be criticised as stupid! So what stops more investment going into building the homes and local infrastructure we so badly need?

2.2 Barriers to public investment

The first barrier is the way we allocate public finance for capital or investment projects. As a recent study suggests, though the UK approach to public finance is based on 'golden rules' for avoiding waste in fact we keep making the same mistakes.[40] The Treasury has long been wary of hare-brained schemes, and there is a long memory of projects with high-sounding aims that failed to return their investment. Furthermore the public sector is only supposed to intervene when there is clear evidence of market failure. Public sector borrowing has to be kept to the minimum to safeguard the nation's credit rating. Despite these safeguards the UK has a relatively poor record on public investment in housing. This is arguably in part due to the centralisation of local finance. Local authorities, for example, are blamed for the business rates, but only collect them on behalf of the Treasury, and an astonishingly small 17% of Council revenue is raised from local taxation compared with over half in other OECD countries.[41]

The Treasury hates what are called 'contingent liabilities' which is why it is so resistant to proposals for local Tax Increment Financing (that is borrowing against future tax proceeds). Ministers are supposed not to commit successive governments, and all propositions are carefully vetted, with open competition being used to keep costs down, and as a result projects stop and start, and the transaction costs are huge. Little difference is seen between spending public funds on housing benefits or unemployment pay, or using it to build houses. As public spending is often seen as inherently wrong, with little differentiation between investment and subsidy, it has been impossible to

39 Ed Glaeser, *The Triumph of the City*, Penguin, 2010
40 Anthony King and Sir Ivor Crewe, *The Blunders of our Governments*
41 *Cities Outlook 2014*, Centre for Cities

overcome the culture of centralisation and pooling even when the case for devolving control is strongly argued.

Grants are preferred to loans because they are easier to account for, and little use is made of tax incentives compared with the USA for similar reasons. Though increasing use is being made of Treasury guarantees the problem of deciding what projects to fund remains. Decisions are all too often taken in silos and evaluated in terms of departmental goals. This approach fails to get full value from the limited public investment that does get through the system.

The argument is often used that we are simply following the rules determined in Europe, but in fact the British have a government accounting system that is quite different from the rest of Europe. Membership of the European Union has been used as an excuse for the excessively complex and jerky way in which projects are procured, which may have resulted in the loss of our capacity to make much of the infrastructure we need, such as railway locomotives or power plant. In other countries (as we will see in the case studies in the next section) there is a much closer relationship between the state in the form of local government and the major companies who dominate the supply of infrastructure, to their mutual long-term benefit, and much less 'stop-go'.

Alternative or more creative funding ideas, such as the use of infrastructure bonds or hypothecated charges that link funding to benefits (such as toll roads) have been shunned. Suggestions that more funds might be raised locally, for example by the London Finance are easily dismissed by those wanting to maintain central control, even when the arguments are supported by masses of evidence:

Relaxing restrictions on borrowing for capital investment while retaining prudential rules and simultaneously devolving the full suite of property tax revenue streams would afford London government greater autonomy to invest in the capital. Such reforms would also increase London government's accountability to residents and businesses. Change would be achieved without affecting the financial settlements of other parts of the country.[42]

The Core Cities are also pressing for financial devolution (though some property taxes need to be redistributed, given regional and other inequalities). But perhaps the strongest arguments concern the quality of investments, and securing better returns. Excessive centralisation makes it is almost impossible to join projects up, as each government department is concerned with its own specific objectives, and does not

42 *Report of the London Finance Commission*, 2013

want to see its efforts diluted. So a rail project will be evaluated against all other rail, or perhaps transport, projects, using a simple form of cost benefit analysis that gives most weight to travel time and accidents saved. It becomes impossible to take account of the spin-off benefits from opening up land for development or boosting local enterprise, as many benefits cannot be valued objectively because of the uncertainties. Furthermore, small local projects tend to lose out to more prestigious national projects. A series of national blunders have been well documented by the media, thanks to reports from the Public Accounts Committee hearings.[43]

Even the much-trumpeted successes, like the Olympic Games, appear to follow political whims with expandable budgets rather than the careful strategic planning and rigorous analysis or deliberation we might have expected from a country with a relatively small public investment budget. When URBED brought local authorities together to compare between British and equivalent Continental cities, such as Gateshead and Gothenburg, in a research project for the Joseph Rowntree Foundation, the English marvelled at cities that seemed in control of their destinies, while the Swedes were astonished by our reliance literally on Lotteries to get major areas developed.[44]

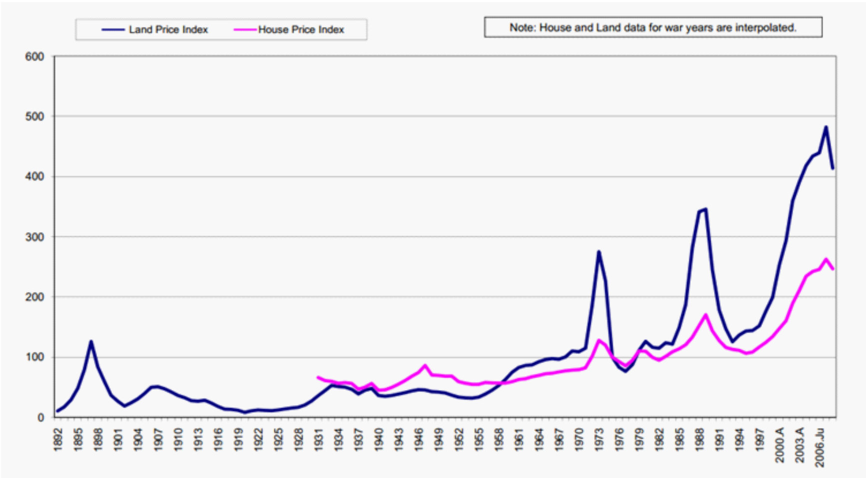
2.3 What is to blame?

Finding the true cause of excessive house price inflation in the UK is like an Agatha Christie play where all the cast could have done it. But, as Danny Dorling argues in his latest book *All That Is Solid: the great housing disaster*, the increases in unaffordability may simply be the other side of the coin of economic and spatial inequality that has bedevilled the UK for decades.[45] With so much of Britain's net wealth accounted for by housing equity, getting on the ladder has become an impossible dream for the masses, not the minority, and is the 'giant' that stands in the way of social mobility.

So while tackling the problem requires action at many levels, it also offers the best chance of rebalancing our economy so that we become more like our European competitors and less like parts of North America where inequalities have widened markedly. Much of the success of the German economy can be attributed not just to greater levels of savings, but to those savings being invested in the growth of independent businesses – the Mittelstand – rather than in house purchases. The result is a virtuous circle in which large cities grow faster than the national average, rather than lagging behind as in the UK (with the exception of London, which as a World City is a very special case).

43 Anthony King and Sir Ivor Crewe, *The blunders of our governments*, Oneworld Publications, 2013
44 *Regenerating European Cities*, URBED for Joseph Rowntree Foundation, 2008
45 Danny Dorling, *All That Is Solid: the great housing disaster*, Allen Lane, 2014

Land values reflect the effective demand for property, and are shaped by location, itself a product of local infrastructure and spending power. With little or no holding cost, they tend to ratchet upwards. Of course the Green Belt, negative planning policies, and so-called NIMBYism do not help, but they cannot take all the blame, as economists sometimes assert. But it is true that land values have escalated faster than house prices over a long period, and have taken off in the last couple of decades, as a chart from Paul Cheshire's blog shows.[46]



Of course tapping land values raises all kinds of objections. Land is different from other assets in the degree of freedom that is allowed. As Professor David Adams points out in his paper the *Potential for Urban Land Reform in Scotland*:

Even the European Convention on Human Rights, which declares that 'every natural or legal person is entitled to the peaceful enjoyment of his possessions', allows lawful interference in the public or general interest (see Allen, 2012).[47] Since property rights are socially constructed, each generation will choose to refine their disposition, adjusting the balance of rights and responsibilities to achieve what at that period is best seen to represent some conception of the public or general interest.

Adams et al examined the strategies, interests and actions of those owning land and

46 http://spatial-economics.blogspot.com/2013

47 Allen, T, 2010. "Liberalism, social democracy and the value of property under the European Convention on Human Rights" *International and Comparative Law Quarterly*, 59(4), pp. 1055- 1078.

property within 80 large redevelopment sites in four British cities.[48] They found that just over half the owners encouraged or significantly encouraged redevelopment. Another third had a neutral impact on redevelopment. Less than one fifth discouraged or significantly discouraged redevelopment. As the large sites required for urban extensions typically involve a number of owners, putting together a viable scheme becomes virtually impossible. This is why sites stay empty and derelict for so long. It is also why many independent businesses have closed down, finding it easier to sell out to developers or their rivals than to carry on. The potential uplift from assembling a site and securing planning permission are often far greater than the returns to be made from running a business.

If the UK is to hope to reach the standards achieved in the best Continental cities, whether it be in wealth creation, educational standards, or equality, it must enable cities to shape their destinies, and not be the victims of absentee landlords and investors. This means regaining control over land use and values. The shift in power that would result from a MIC could be the single most powerful force for change (accompanied, of course, by changes in the way land is valued in areas designated for development in agreed spatial plans). It would tap the underused sources of 'patient capital' owned by pensioners through properly assessed bonds. Moreover, it would then put them to work more productively without breaching the limits on public sector finance, and in the process help to narrow the inter-generational inequalities that have emerged over the last twenty years.

2.4 Breaking the barriers

There is a lot to be learned from successive attempts to build more homes and regenerate older areas in the UK. For example, the development of London Docklands, where the private investment was highly leveraged by public investment up front was only possible because the first Chief Executive went against the instructions of civil servants in funding the start of the Docklands Light Railway which opened up investment opportunities. In Milton Keynes, the Development Corporation produced one of the best returns on investment the Treasury has ever seen, as well as relieving pressures on much of the rest of Buckinghamshire. This was thanks to a dedicated full-time staff able to negotiate from strength with private house builders because they owned all the best land, and could fund the infrastructure. In Peterborough, the persuasive Chief Executive of the Development Corporation secured local backing for growth by first upgrading the existing city centre, and then building a new park at the heart of three new settlements, based on expanding existing townships.

48 David Adams, "Vacant urban land", *Town Planning Review* 73, 2002

It is not always necessary to take away responsibilities from local authorities in order to get good development done. In Manchester, where much of the central area now compares well with European cities like Bordeaux and Barcelona, the transformation is attributed to the determination of successive local political leaders. A strategy of restoring and reusing historic buildings, opening up the waterfront, and tying the city together with its suburbs through a high quality tram system, has in time generated the confidence needed for private investment, such as the superb new Spinning Fields Quarter that replaced run-down commercial buildings, or the innovative housing schemes underway in East Manchester. The private sector developer is clear it was only thanks to the drive and flexibility shown by the City Council (where the Chief Executive effectively acts as director of development as well) that the scheme could ever have proceeded, given the ups and downs of the property market.[49]

Birmingham's success in remodelling its city centre and downgrading the inner ring road was kicked off by using the great asset of the International Exhibition Centre to underpin the funding of the International Convention Centre and the area around it.[50] Leadership from the City Council has since attracted people back to live in the centre. A good example is the stylish development of Park Central, a joint venture between the City Council, whose housing was taken over by a local housing association, and redeveloped in partnership with Crest Nicholson.

Initiatives of this kind and scale would not have been possible without the active support and funding provided first by English Partnerships, (which grew out of the English Estates Corporation), and its successor the Homes and Communities Agency, which also took over the Housing Corporation. Though its budget is still relatively small in European terms, and vulnerable to short-term political swings, it has managed to make a success of a number of major public land holdings, such as the former hospital at Graylingwell on the edge of Chichester, where a contemporary looking housing scheme has been one of the first to use combined heat and power.[51] This scheme provides a good example of how to develop quality suburbs in a historic city.

By using grants flexibly, the HCA has also derisked some difficult housing schemes, such as the redevelopment of the old Ferrier Estate in Greenwich, where some £130 million was provided for decontamination works and social housing to enable the Berkeley Group to start implementing an ambitious scheme for Kidbrooke Village.[52]

49 Report of TEN Group study tour of Manchester , www.urbed.coop

50 *Partners in Urban Renaissance*, URBED for Office of the Deputy Prime Minister, ODPM, 2002

51 *Solutions: How local authorities can build sustainable urban neighbourhoods*, JRF 2008

52 Barry Munday and Nicholas Falk, *The ABC of Housing Growth and Infrastructure*, Housing Forum 2014

The key is providing enough finance up front to turn the tide of private confidence. A strong lead from the public sector is usually essential for private businesses to follow except in 'safe' situations like building office blocks in the City of London, or shopping centres let to major retailers.

However as well as the successes there are many more examples of sites that sit undeveloped for years, even when public funding has been invested on a large scale. The new town of Northstowe in Cambridge is a good example of a site that has benefitted from new rapid transit links, yet where a joint venture with the private developer failed to jell. In this case the acquisition of the former defence site from the MOD used up half the HCA's budget for the East of England, which suggests that better 'deals' could be brokered if land was not effectively auctioned off to the highest bidder. South Cambs have now given outline permission to the first phase of 1,500 homes, but have had to scale back their S106 requirements (including reducing the affordable housing to 20%), as well as skimping on the social infrastructure, and there is no guarantee that future phases will happen as originally planned.

Even in London, the Greenwich Peninsular made famous through the building of the Millennium Dome has remained largely undeveloped despite a public investment of some £200 million in decontamination of the old gas works, plus much more in diverting the Jubilee Line and building a new station. In both cases the waste is largely due to private owners preferring to sit on sites and wait for better times, as the holding costs are low compared with the costs and risks of building anything. In the UK there is no holding cost for sitting on land with planning permission (unlike the situation in Denmark, for example, where there is an effective system of Land Value Taxation that ensures land designated for housing gets developed without delay).

As most house building is dominated by a few volume house builders, who have their pick of sites, it will always be hard for the big inner city or urban extension sites to compete with the attractions of building on green fields that they already own or have options on. Yet in the UK they have become the only bodies with the capacity needed to put a complex scheme together, or get the backing of a government agency. Developers tend to rise and fall with each property cycle, and prefer to operate on their home turf. The fact that year after year, whatever the state of the market, private house builders produce roughly the same number of homes suggests that it is not just market demand that determines what gets built, but the interests of their shareholders, who value sites with planning permission even if nothing is built on them for years.

My report on the economic issues involved in building ecotowns sets out a series of proposals for breaking the barriers in developing exemplary new settlements, based on comparing British and Continental approaches.[53] The conclusions were also verified in an action research project funded by the Joseph Rowntree Foundation to share experience between twelve new communities in different parts of England (which informed the Joseph Rowntree Housing Trust in building Derwenthorpe in York, which has since won a lot of praise).[54] Where there have been achievements, it has usually been due to the dogged **ambition** of local actors to create somewhere better, who have been able to **broker** the necessary resources, with the **continuity** to survive the ups and downs of the business and property cycles.[55] So how could the exceptions be made the norm?

2.5 Funding associated infrastructure

The search into ways of making housing more responsive to demand in the UK has led economists such as Kate Barker to blame the planning system.[56] Paul Cheshire goes further in attacking the Greenbelts around our cities for pushing up the value of housing land, and hence house prices.[57] He compares the value of a hectare of land with planning permission for housing in Oxford of £4 million with industrial land selling for £1 million in 2011. As Paul Cheshire has shown, land values have outpaced house prices, and because there is no holding cost, tend to go ever upwards. At average house prices and densities, land accounts for a third of the price of a typical new house, more if it is detached. As agricultural land often sells for only £4,000 a hectare it is understandable why housing developers spend time securing options on land all around our cities, which they hope to profit from after numerous applications and appeals. With limited supplies and relatively few large builders, it is also easy to see why builders prefer to make sales of around one a week from each active site, and to use their standard products, even though only one in four house buyers considers buying a new home, according to market research by MORI.[58] We are stuck with a flawed system.

The value of housing sites reflects far more than costs imposed by planning. The position in the UK is in stark contrast with Germany or the Netherlands, both of which have far stronger planning systems but much lower house prices, and build much bigger homes, with a higher quality of infrastructure.[59] Some of the explanation lies in different forms of tenure, as a larger private rental sector enables new developments

53 Nicholas Falk, *Beyond Ecotowns: the economic issues*, URBED 2008

54 Michael Carley and Nicholas Falk, *How can local government build sustainable urban neighbourhoods*, JRF 2008

55 Barry Munday and Nicholas Falk, The ABC of Housing Growth and Infrastructure, The Housing Forum. 2014

56 *Barker Review of Housing Supply*, HMG 2004

57 http://blogs.lse.ac.uk/politicsandpolicy/archives/36445

58 *Report of the Future Homes Commission*, RIBA 2012

59 Sarah Monk and Christine Whtiehead, *Making Housing More Affordable: the role of intermediate tenures*, 2013

to be occupied faster (rather as has been happening through buy to let investors in some parts of London). But the differences can also be explained by the greater supply of serviced sites with planning permission in locations that are close to motorways, railway stations and rapid transit corridors. Many more builders can then compete to meet the needs of a much wider market. With plots being sold as a proportion of the expected sales value, they compete in terms of quality not price. Serviced plots are sold for 25% of the expected sales value or on a sliding scale of between 20-30%.[60]

Research into the cost of infrastructure has found that this can be greater than the new homes cost to build. The new town of Milton Keynes involved an original public investment of £700 million, which not only allowed it to 'start with a park', but also to lay down a grid of kilometre squares. This made it possible for people to drive rapidly to work (but made good public transport unviable, as the housing was too dispersed). Figures produced for English Partnerships found that the 'roof tax' or tariff of £18,500 on new homes will only yield a fifth of the total infrastructure costs. An analysis of the Milton Keynes tariff expenditure showed that transport accounted for a third followed by schools, and then landscaping, making two thirds in all. Other factors such as leisure and waste were far less important and could be lumped into a general community charge. A similar analysis by Deloitte's for the growth of Cambridge established that the infrastructure cost worked out at £55,000 per new home, of which only a third could be expected to come from the private sector. In this case 57% of the cost was for transport, 14% health, 12% for utilities, and 10% for education.[61] The programme of infrastructure investment for the period was costed at £4 billion, and the plan was to build 73,000 new homes to increase the housing stock by 40%, far more than anywhere else in the UK.

These two sets of figures are both for areas where most of the development land is in the form of green fields, usually intensively farmed, and therefore with little biodiversity. A very different set of figures should result from expanding where there already is social infrastructure, and where the scheme can piggy back on existing roads, for example by building outside a ring-road, and off an existing park and ride scheme, or by upgrading a railway line where there is currently an infrequent service. House builders would welcome building in places where there is evident demand, and agreement on both infrastructure plans, and the kinds of housing that are required. The Community Infrastructure Levy plus Section 106 contributions are resented because they add to uncertainty or risk, and have to be paid before the value is realised, which

60 Nicholas Falk, "Masterplanning and infrastructure in new communities in Europe" in Tiesdell, S and Adams, D *Urban Design and the Real Estate Development Process*, Wiley 2010
61 Deloitte, *Long Term Delivery Plan*, Cambridgeshire Horizons, 2007

is when homes are sold and occupied, and registered with the Valuation Office. The initial risks on the upfront costs are too high to make the development of strategic sites worthwhile for most British volume house builders, who prefer to pick the low hanging fruit on the edge of villages or in urban infill sites.

By raising private funds for local infrastructure and land assembly through a state investment bank, as in the examples of Vathorst in the Netherlands or Rieselfeld in Freiburg, and taking over the land at close to existing use value, developments have been able to fund superb advance infrastructure. District heating schemes or ground source heat pumps cut energy costs, and reduce carbon emissions, as do electric trams, and open spaces that encourage walking and cycling. Money that would have gone to the landowner or consultants in the UK has been invested in infrastructure that adds to the 'common wealth'. In turn private investors have probably secured higher returns on their savings. There is no shortage of funds looking for inflation proofed and property based investments, and the MIC will ensure that good projects get funded, and that risks are minimised. In turn, large scale projects should be able to use their bargaining power to attract investment into local infrastructure, as happens on the Continent.

The main energy, transport and water providers are natural monopolies, and so seek to benefit from making the most of their existing capacity, not adding to it. As a result, as power stations or railway lines age and maintenance is minimised, so the necessity of building new capacity becomes ever more urgent. In both cases the same risks as housing apply, a prolonged and unpredictable period to secure planning permission, almost certainly escalating costs with little capacity left in the UK to compete, and possibly excessive levels of profit. Investment depends on higher tariffs to recover the investment and profits that an international business with a choice of where to invest is looking for. If prices are controlled, then it is investment that suffers. The answer lies in smarter growth, that is securing local investment agreements based on plans that deliver the promised demand, not waiting for congestion or reliability to become intolerable before funds are released at the last moment.

2.6 Securing smarter growth

The bulk of long-term investment is not in fact provided by the banks but by pension funds and insurance companies. Though vast, these prefer to deal in existing assets rather than create new ones. Indeed, individual pension funds say they are too small to have any expertise in assessing potential development projects, such as building new homes, and are wary of being diverted from so-called 'safe investments'.[62] They want

62 *Local Authority Pension Funds: Investing for growth*, The Smith Institute, 2012

certainty. Only about 5% of institutional investment has traditionally been in property, and there is a marked preference for prime property in city centres that can readily be sold on, or equity stakes in development companies. The English speaking world has taken a very different approach to funding development from the rest of Europe, perhaps because of Britain's cultural and historic isolation along with the dominance of liberal as opposed to social democratic ways of thinking and acting.[63]

However, the workings of the City of London have been under fire since 2007, particularly as far as long-term investment finance is concerned. A RICS study of infrastructure funding and public private partnerships, considered Australia, Canada, India, the US and the UK.[64] The researchers found a growing demand for infrastructure finance, but dissatisfaction with Public Private Partnerships. The costs and complexities of raising private finance were seen as excessive. There was little evidence that the promised benefits have actually been secured. Government has been left with the problems of paying for expensive items like new railway lines or power stations, and picking up the pieces when private operators go bankrupt.

The RICS study recommended moving away from a project by project evaluation and taking account of the wider benefits for society. It is this 'more integrated and strategic approach' that non English speaking countries in Northern Europe have achieved since the Second World War. By centralising investment decisions in London, and by limiting the role and powers of local authorities, the UK has made it much harder for its cities to respond to economic changes, which is one reason why our recovery has lagged behind other major European countries. Our cities have not taken on the role of 'engines for growth' that their counterparts on the Continent have played, or that the Core Cities have argued for.[65] The most successful towns in economic terms have failed to expand faster than the regions, as might have been expected, and housing has lagged behind employment growth.[66] Instead our cities have become ever more polarised, as house prices rise while house building remains stuck.

When the Coalition government abolished Regional Development Agencies and Regional Spatial Strategies in the name of localism, it left a vacuum which Local Enterprise Partnerships are not able to fill. Yet an earlier Conservative Party Paper had recognised the 'lack of house-building enabling infrastructure. It is no accident that investment in housing is among the lowest in the developed world'.[67] The Heseltine

63 Robert Skidelsky *Keynes: the return of the master*, Penguin 2009

64 *The Global Infrastructure Challenge: the role of PPP in a new economic and financial paradigm*, RICS October 2013

65 Michael Parkinson et al, *Competitive European Cities where do Core cities stand?* ODPM, 2004

66 *From Austerity to Prosperity: seven priorities for the long term*, McKinaey Global Institute, November 2010

67 *Control Shift: returning power to local people*, Conservative Party, 2008

Report *No Stone Unturned* stressed the importance of local authorities playing a more proactive role, and there could well be all party support for the resurgence of local leadership and combined authorities.

The idea of strategic planning is also resurfacing as local authorities in metropolitan conurbations start to join forces and combine some of their staff. They are motivated by the consequences of financial cutbacks in the name of austerity, and the need to attract new sources of funding to close the North South divide. Starting with the Association of Greater Manchester Authorities, but extending to other places that had once been organised as Metropolitan Counties, the Core Cities are starting to fight back. There are also initiatives from authorities such as Woking and Southampton, who have led the way in investing in local energy systems. The imperative to boost local growth, if only to maintain current levels of services, could produce the breakthroughs in planning that are long overdue.

2.7 Tapping pension funds

The parlous state of public finance in the UK makes it essential to find better ways of shifting private long-term or institutional finance into building new homes and related infrastructure, and not just buying existing ones. The British pension funds have come under criticism for offering low returns to investors. Those reaching retirement age find their 'pension pots' are not as large as expected, with much swallowed up in fees, and annuities are much less attractive than they used to be. As a result those living on fixed incomes are likely to welcome the opportunity to invest in bonds that share in the rise in land values as a result of housing developments and new infrastructure.

As windfall profits from land speculation are widely criticised, there should be popular support for measures to use the proceeds to help fund the essential infrastructure that underpins what people are prepared to pay for housing in the right location – that is a safe neighbourhood, with easy access to jobs and services, and the advantages of good schools and open spaces. However, the economics of development vary greatly between London and well-connected parts of the South East, including growing cities in other parts of the country, and the old industrial areas that have lost jobs, and where people have moved away from the cities. Huge amounts have to be invested to overcome the effects of long periods of decline. There is consequently a conflict between the local authority pension funds that are under pressure to invest in regeneration, and the places that offer the best prospects for growth.

The Pensions Infrastructure Platform was launched in 2012 to raise an initial £2billion for infrastructure projects. However this will favour the kinds of national projects that the government is willing to underwrite, such as power stations and intercity railway lines. At the same time the LGA's work on a Municipal Bonds Agency is more concerned with cutting funding costs, than with channelling finance into projects that boost local growth. There are consequently major gaps to be filled in creating viable projects in both growth and regeneration areas, as research into the economics of new housing has established.[68]

In growth areas, the best solution is to share in the uplift in land values when a change of use is permitted on a major site, say one large enough for a thousand homes, or 100 acres. In regeneration areas, where property values are lower and reclamation costs higher, major government grants will still be needed. As case studies of recent major housing schemes show, projects in low value areas such as South East London still require considerable public pump-priming, while attracting families to live in an area like New Islington in Manchester costs even more, such as investing in a new secondary school.[69]

The answer for land with negative value lies in setting up Development Corporations with public funding for their management costs, and the ability to take over land at close to existing use value (as was done in successes like Milton Keynes and Peterborough). They would not need much in the way of public funding, provided they were able to pool public expenditure within a sub-region through drawing up a Local Investment Agreement. This would then secure much greater public benefits than any one project alone, such as a new tram line, school, hospital or park could secure. It is what economists call 'agglomeration effects'. This holds the key to turning areas around through pooling investment, as Germany has done so well in regeneration areas such as Emscher Park in the Ruhrgebiet.

In turn the Development Corporation, with a multi-disciplinary team of expert staff and full political support, can provide private investors with the confidence they need to support long-term projects in the face of inevitable ups and downs and reverses. Just as Peterborough Development Corporation won the support of local politicians by upgrading the main shopping centre, and creating a new park at the heart of the new settlements, so a new breed of development corporations can fill both a funding and management capacity gap. The TCPA has usefully proposed how the legislation could

68 I have drawn on figures produced by Pete Redman, based on experience with a range of housing developments and statistics on the costs of infrastructure.
69 Nicholas Falk and Barry Munday, *The ABC of Housing Growth and Infrastructure*, The Housing Forum 2014

be updated to reflect current concerns for community engagement and sustainability, and instead of being imposed, these could be offered to local authorities prepared to take up the challenge of reshaping their communities.

2.8 The case for a state investment bank

Many have argued for radical change following the deep and prolonged recession, which is blamed on financial short-termism and misjudgement of the risks involved in bundling up investments.[70] The first statements by the new Governor of the Bank of England warned of the dangers of another housing bubble. Calls for a major reform of access to and provision of finance for investment led to proposals for a 'British Investment Bank' in a report from Nicholas Tott for the Labour Party and also by the think-tank IPPR for the Trades Union Congress.[71] Both drew heavily on the example of KfW in Germany. Proposals for some kind of BIB from both the left and the right suggest a degree of consensus on fixing a financial system that is no longer fit for purpose as far as long-term investment is concerned.[72]

A start has been made on a small scale in Vince Cable's Green Investment Bank with its £3 billion of capital but very restrictive conditions on what it can invest in, and it is not allowed to raise more finance. Sadly there has been no serious attempt to link extra investment in housing with the tasks of upgrading our infrastructure and rebalancing our economy, or with providing pensioners with a better income, and this is where the best long-term returns will come from.

With very limited public finance, it is crucial to concentrate efforts in mobilising private finance where it will have the best effects. A BIB would use the incentive of making funds available to persuade unlikely bedfellows to work together across sectoral and professional boundaries in developing viable projects. It can also fill the long-term gaps. Investment finance is blamed for where the UK has gone wrong over the last few decades, and the collapse of the banks was fuelled by what some have called 'casino capitalism'. Far more money is made through mergers and acquisitions and closing down capacity than in financing new ventures. Money is made in the USA and UK by moving it around, a system highlighted by the 'bonus' culture that has hit the headlines.

70 Graham Turner, *No Way to Run an Economy: why the system failed and how to put it right*, Pluto Press, 2009

71 *The case for a British investment bank*, Nicholas Tott, Labour Party Policy Review, 2012; *Investing for the future: Why we need a British investment bank*, Tony Dolphin and David Nash, IPPR September 2012

72 See for example Faisal Islam, *The Default Line: the inside story of people, banks and entire nations on the edge*, Head of Zeus Ltd, 2013

Criticisms have also been made of the pensions industry for seeking short term returns through excessive 'churn' and inflated management fees which are not in ordinary pensioners' best interests.[73] This has resulted in a pent up demand for better returns on the part of private savers that could be invested in longer-term projects, such as building new homes. According to Key Network Solutions, the value tied up in older people's housing amounts to some £800 billion, and a report from Demos suggests that 60% would consider downsizing provided better options were available near at hand.[74] This alone would release some 3 million family homes. Building homes that appealed to older people would provide a larger and often leaky home with a garden for a young family to improve and enjoy, and probably bring down prices in the process.[75]

A state investment bank can also help fill the infrastructure gaps that cause people to oppose development, such as local congestion on the roads and railways. While almost everyone agrees on the imperatives of both building much more and better housing, and upgrading Britain's worn out energy and transport infrastructure, the financial obstacles so far are proving insuperable.[76] Despite hosting one the world's main financial centres the UK often struggles to channel large amounts of funding seeking a fixed return into the many smaller projects that pay off over the longer term. The UK has relied too much on Public Private Partnerships schemes that were not true partnerships. The Policy Exchange report on infrastructure criticised the Private Finance Initiative for raising the costs of finance.[77] Instead it proposed an infrastructure bank based on practices in Australia and Ireland as well as Germany, (which suggests that both right and left could be in agreement). Their proposal was to merge the Public Works Loan Board (established as long ago as 1793) with Labour's creations of the Treasury Infrastructure Finance Unit, and Partnerships (now Infrastructure) UK, and to focus the bank on funding large projects. Such a proposal would also tie in with Sir John Armitt's proposals for an Infrastructure Commission to help make choices on the really big projects.[78]

A state investment bank would focus on securing better returns from joining up development and infrastructure in ways that improve total returns. For example, the cost of improving home efficiency is put at £2 billion and total energy efficiency at £21 billion, compared with £136 billion on renewables.[77] Similarly the total cost of building

73 See criticisms by Lord Lawson and the Pensions Minister Steve Webb reported in the media
74 Demos, *The Top of the Ladder*, 2014
75 Nicholas Falk, *Lifelong Neighbourhoods: how older people can add value*, Housing Learning and Improvement Network, 2013
76 See for example the Barker Review of Housing Supply 2004
77 Dieter Helm, *Delivering a 21st Century Infrastructure for Britain*, Policy Exchange 2009
78 Sir John Armitt's *Independent Infrastructure Review.* 2012

another 100, 000 homes a year is unlikely to be more than £5-10 billion, or a fifth of the spending said to be required for infrastructure. Most of the extra new housing needs to come from schemes of over 1500 units, which will be large enough to support a primary school at its heart plus some commercial facilities and open space. Yet in urban extensions, new housing developments could piggyback on existing or proposed infrastructure, and incorporate energy saving measures as a bonus, thus reducing the need for extra utility capacity or new roads.

Finally a state investment bank can help ensure a better flow of good investment opportunities. Though there have been calls for quick solutions, such as local authority pension funds filling the funding gap, research for the Smith Institute found that the potential for releasing pension fund investment in housing was likely to be in the millions rather than billions. A major obstacle to growth seemed to be the lack of viable propositions and insufficient scale.[79] Similarly Housing Forum seminars that brought together developers, financiers and local authorities to discuss the obstacles to funding housing infrastructure concluded that the real obstacles lay not so much in the availability of finance, but in devising viable schemes on the scale investors require.[80] The funds want projects that are 'oven ready', with risks that are easy to assess. Speakers from the Caisse des Depots in France and earlier from Kommuninvest in Sweden explained how their system worked better in supporting high quality and affordable housing built to the higher environment standards. For example the Caisse des Depots funded building 133,000 new social housing units in 2011, which is almost as many as the UK built altogether. As we shall see in the next section, almost all European countries have long standing state investment banks that supplement the roles played by private financial institutions, working closely with local authorities, and that finance housing and local infrastructure as well as SME's.[81]

Conclusions

The urgency of both building many more homes and restoring a worn-out infrastructure provides, like war time, the circumstances when radical change should cut across the forces of inertia and privilege. It should no longer be acceptable to rely on rising house prices to pay off housing debts of those fortunate enough to get on the housing ladder, while the rest look on with envy. By focussing development on locations with existing or planned infrastructure, we could overcome the barriers that have stopped supply responding to changes in demand.

79 CLES, *Local Authority Pension Funds.: investing for growth,* Smith Institute 2013
80 Nicholas Falk and Barry Munday *The ABC of Housing Growth and Infrastructure* 2014
81 Barry Munday and Stephen Hill, *Infrastructure: the key to unlocking housing development?* Housing Forum 2012

The short life of public bodies like the Regional Development Agencies shows the dangers of relying on new institutions to rebalance the economy which are then overturned by the next government. So a solution must be found that can appeal to all sides of the debate. A **municipal investment corporation** would help make the numbers add up by channelling private finance into building local infrastructure and affordable homes rather than into further inflation in house prices or credit card fuelled spending. This would also be one of the best ways of supporting SME's and achieving real devolution or localism. It therefore fits well within both the Labour Party's commitment to establishing a BIB and Lord Heseltine's proposals for getting the economy moving through local growth, and should therefore survive political shifts.

If a BIB is going to add value to what exists, satisfactory answers are needed to the following questions:

- which projects should be funded and on what scale
- where are the funds going to come from?
- how will they be allocated?
- what can be done to control the risks, and avoid waste or corruption?
- and how will resistance from entrenched interests be overcome?

To answer these questions, we would do well to look and learn from what has worked so well in other European countries.

Section 3

What can we learn from the rest of Europe?

What can we learn from the rest of Europe?

We need to learn from successful cities abroad… the evidence suggests that where cities are given more freedom and resources they have responded by being more proactive, entrepreneurial and successful.

State of the Cities report[82]

The solution to the funding chasm calls for new models. This section first considers the need to look abroad, before introducing three case studies of major developments to show how the system works in the very different countries of France, Germany and the Netherlands, and why a state investment bank is also required in the UK.

3.1 The need for better models

The task of collaboration is paradoxically hardest in the very areas of the country where the pressures for growth are strongest, such as in Oxfordshire or on the edge of London. However in Cambridge one of the wealthier colleges and the local authority pension funds have joined forces to launch a new bank, while in Manchester the pension funds are pooling their efforts. These emerging collaborative arrangements offer hope, providing that development and infrastructure decisions and funding are also joined up. Precedents are also set by devolution to Scotland. Local government reorganisation in Scotland in 1996 did away with the regional tier, resulting in 32 single tier local authorities. Devolution of some powers to the Scottish Assembly has certainly helped to strengthen national identity. A National Planning Framework has been adopted which provides a model for English city regions, with similar populations and economies. There is much more sharing of good practice.

As English local authorities look into what further cuts can be made, planning and regeneration departments have been the first to lose out. But just as leeches rarely brought sick patients back to health, so cutting services further will do little to enable cities respond to the new demands. Instead some far-sighted authorities are starting to consider how new financial mechanisms can be used to rebalance their cities as well as local economies. City Deals in some 28 authorities are being used to negotiate greater freedoms, with Manchester leading the way in retaining business rates from development. Integrated strategic plans and adequately resourced delivery agencies are also likely to win business support from Local Enterprise Partnerships, as they start to commission Growth Plans.

A few are also looking abroad to discover what other approaches are possible.

82 Michael Parkinson et al, *State of the Cities report for the ODPM*, 2006

Significantly the Local Government Association has commissioned advice from the founder of the Swedish Kommuninvest on setting up a Municipal Bonds Agency to reduce the cost of borrowing.[83] The initiative is backed by twenty local authorities, and was launched in January 2014. Kommuninvest was set up as recently as 1986, but a similar approach has been in use much longer in a number of other European countries that have built more and better housing than the UK.

As Britain faces similar challenges to much of North West Europe, it is time to learn from what works so well there.[84] In particular we need to discover again how to mobilise land, draw up effective masterplans and development frameworks, and fund upfront infrastructure. Regrettably the post-war Labour Government was unable to bring in real land reform, and became mired in a spirit of austerity which lost it power.[85] Subsequent efforts to benefit from betterment have failed. However New Towns like Milton Keynes did build enough housing to fund high levels of community facilities, such as parks, and pay off Treasury loans, and the residents are now able to reach jobs without spending hours commuting.[86] This was largely thanks to acquiring agricultural land at close to its existing use value, so that the 'land value uplift' could be reinvested in local infrastructure. The Act is still on the Statute Book.

Unfortunately the 1947 Town and Country Planning Act did not resolve the problem of land valuation, as it was reformed after only five years, and successive rulings have enshrined the idea that landowners should secure most of the uplift from public investment in infrastructure once planning permission is given. Yet it seems only fair that some of what Ebenezer Howard called the 'unearned increment' resulting from public investment in infrastructure should be ploughed back into facilities that benefit the wider community, and this can be done without infringing human rights, given the necessary political will. It is particularly relevant in places that are going to benefit from public investment in upgrading rail and road links.

European cities and countries have done much better in recovering or avoiding the crises and fluctuations that have dogged the UK. The situation in much of North West Europe is comparable in terms of both cultural history and densities, except that since the last war, real power has been devolved to cities and city regions. Previous research by Nicholas Tott and the IPPR established the key roles played by state investment

83 LGA Press Release 20th January 2014 LGA appoints lead advisor to finalise bonds business case, and Municipal Bonds Agency: revised business case summary, March 2014, LGA
84 Peter Hall with Nicholas Falk *Good Cities, Better Lives: How Europe rediscovered the lost art of urbanism*, Routledge 2013
85 David Kynaston, *Austerity Britain*, 1945-51, Bloomsbury 2007
86 Anthony Alexander, *Britain's New Towns: from garden cities to sustainable communities*

banks such as KfW in Germany in reaching the parts that private financial institutions tend to ignore.[87] They operate on a substantial scale, investing together with local authorities, as well as under-pinning the investments made by other banks.

While much of their funding goes into support for Small and Medium Sized Enterprises (SMEs), state investment banks also play a fundamental role in building new communities and applying sustainable development principles, such as funding renewable energy systems that cut emissions and consumption. As we shall see the roles played by the state investment banks help explain the lead that European countries have had over their English speaking counterparts, along with differences in the way that land for development is treated, and strategic planning operates.

The case for using a state investment bank to fund advance infrastructure and affordable housing was first set out in a report into learning from exemplary European housing schemes. Britain has not been short of ambitious policies and plans, as the saga of Ecotowns in 2008 or the Sustainable Communities Plan in 2003 illustrate. But the test is not the size of the targets but what is actually built. A collaborative research project to find out why other countries were building better new housing developments than in the UK, discovered a variety of designs, but a surprising similarity in approach.[88] *Beyond Ecotowns* analysed a set of six exemplary large scale housing projects in four different countries – Amersfoort in The Netherlands, Germany (Kronsberg in Hanover, Vauban and Rieselfeld in Freiburg and Hafen City in Hamburg) plus Adamstown near Dublin in the Republic of Ireland, and Hammarby Sjostad in Sweden.

It turned out that though reaching agreement still took time, innovative schemes had then been built five times faster than in the UK, and catered for a much broader range of residents. This was largely due to the local authority, or a public private partnership, drawing up the masterplan, assembling and decontaminating the land, installing the basic infrastructure including some utilities, and then selling off sites within briefs to a wide range of builder developers, including cohousing or building groups. Further probing into the economics of the process discovered that one of the secret lays in being able to borrow large sums of finance up front at relatively low rates of interest from banks whose purpose was to serve the public interest.[89] A large professionally managed private rental sector also helped people move in much faster, at a time when buying a home was still risky. There were also measures to ensure that the public realm was well managed, with greater use made of collaborative arrangements such as sports associations.

87 Nick Tott op cit, IPPR op cit
88 *Beyond Eco-towns: applying the lessons from Europe*, PRP, URBED and Design for Homes, 2008
89 Nicholas Falk, *Beyond Eco-towns: the economic issues*, URBED, 2008

Sustainable development takes time

Stage	Led by	Duration
1. Land assembly/ strategic planning	National/ regional/ local government	2-4 years
2. Masterplanning	Local authority	1-2 years
3. Physical infrastructure	Local authority	Staged with masterplan
4. Social infrastructure	Local authority	In advance of housing
5. Housing construction	Builders/ coops	1-2 years per phase, 5 years in all
6. Management	Local authority plus neighbourhoods	Ongoing

Repeated study tours by British groups from local authorities to some of the best models, such as Rieselfeld in Freiburg in South West Germany or Vathorst in Amersfoort near Utrecht in the Netherlands, concluded that the lessons from success could be transferred, provided the process was led by a proactive local authority or public agency, and not through a centralised and top-down form of intervention or leaving the running to private developers.[90] In addition a new source of finance was needed to prepare the sites for sale, and thus open up much greater competition between house builders, with a greater choice for households as a result. Here we summarise case studies from three leading countries to show how funding can be made to work in different situations, first a large central site in a run-down part of the French capital, then a major area of industrial decline in the German Ruhrgebeit, and finally an urban extension to a medium sized Dutch city in the centre of Holland.

3.2 Learning from France

The Caisse des Depots in France provides funding to public private partnerships to implement agreed spatial plans. Founded in 1816, the French state investment bank Caisse des Depots et Consignations, to use its full name, plays a key role in supporting local authorities and other public bodies in developing their cities. Unusually it manages savings accounts, including deposits for house purchases, and forty seven pension funds with 7.4 million contributors. Since 2009 it has managed nine new government investment programmes totalling 7 billion Euros, such as 'The City of Tomorrow'.[91] The four priorities set out in its strategic plan *Élan 2020* are housing and cities; universities and the knowledge based economy; SMEs and sustainable development and indicate the range of its interests. In 2011 it financed 133,000 social housing units, a third of the housing built in France at the time. In total it made 16 billion euros of loans for social housing and urban development in 2010.

The bank invests in property projects and infrastructure alongside local authorities, providing them with 35 year loans. It has consolidated assets of 262 billion Euros and equity of 20.2 billion Euros. There are 37,000 employees in the Caisse des Depots Group in 25 regional offices, and 102,000 worldwide including its transport subsidiary Veolia Transdev, so it has all the expertise needed to assess projects as well as borrowers. As well as the regional offices, there are head office departments covering real estate; transportation engineering and infrastructure, knowledge-based industry, insurance, digital technology, tourism and leisure, sustainable development, and local economic development.

90 See, for example, **Learning from the Netherlands: report of the Dutch study tour**, URBED for JRF 2012, www.urbed.coop

91 Source: Presentation by Frank Hovorka, Caisse des Depots, to the Housing Forum seminar on Financing Infrastructure, July 2012

A modal shift away from car dependence to public transport, cycling and walking as in France has taken many decades to bring off thanks to sustained public investment in infrastructure. . The UK lags far behind the rest of Europe in investing in local transport as the following figures illustrate:

	Tram systems	Metros
UK	5 (+1 under construction)	4
France	23 (+4 under construction)	5
Germany 54	54	16

France now has five times more light rail systems than the UK and ten times the length whereas in 1980 both countries were equal.[92] In turn their provincial cities have outpaced Paris in economic growth over the last thirty years, and their quality of life has also been transformed, as any regular visitor will confirm.[93] So investment in local infrastructure meets a number of policy goals simultaneously, but takes much longer than any politician's lifespan.

A TEN Group study tour to Paris in 2012 examined the huge development over the railway lines into Gare de l' Austerlitz, a development some three times the size of Kings Cross, which provides a good example of how the French planning and development system works for strategic projects.[94] In situations such as Paris Rive Gauche, where huge upfront investment is required but where the demand should eventually be strong, the municipality sets up a publicly owned development agency (société d'economie mixte) that can operate with the flexibility of a private company, but without its loans being counted as public debt.

SEMAPA was set up in 1985 and was selected, as 'a responsible urban developer' whose 'primary concern is to cater to general interest' in 1991 to carry out the Paris Rive Gauche programme. This is one of a number of mixed development zones (Zone d' Aménagement Concertée or ZAC). The original finance came from the Caisse des Depots, who have also financed several office buildings on the site. SEMAPA has an option on all the land, which means it, does not pay for the sites until they are developed, and can compulsorily acquire adjoining sites if required. Originally SNCF were a joint partner with the two adjoining local authorities, but had to drop out because of EU rules.

92 Unpublished research by Reg Harman and Nicholas Falk
93 Urbanrail.net
94 *Learning from Paris, report of the TEN Group 2012 European study tour*, www.urbed.coop,

The company provides continuity while avoiding burdening the Councils with liabilities, and is described as a 'tool of the City' that can act entrepreneurially. It will take some 25 years to build the projected 2.5 million sq metres of space, and currently the scheme is about three quarters complete. So far the Deputy Director, who is an architect, has outlived three mayors. The company employs some 40 professionals, with a full range of disciplines. As well as controlling what happens on Paris Rive Gauche, SEMAPA also taken on other development projects, such as one in Paris Nord Est, an area which is like London Docklands in having lost much of its economic base.[95]

Figures in a SEMAPA presentation showed that the initial investment in assembling, planning and preparing land was recouped by selling off development rights (which is sometimes known in the UK as 'land value capture'). Thus in 2008, over 20 years after the start, SEMAPA had invested over 3 billion Euros in the purchase of land and provision of infrastructure, and recovered 73% of that from selling off serviced plots, largely to private companies. Infrastructure accounted for 38% of expenditure, and includes a district heating system.

The French development system produces a higher investment in infrastructure, possibly thanks to a lower land cost. It delivers growth faster because there is less time spent dealing with opposition or bidding for funds. It benefits from being able to package funds, for example, through the Versement Transport, a hypothecated local charge in major cities on the payrolls of those employing more than ten staff.[96] The planning process is surprisingly straightforward compared with the British system.[97] For example local authorities secure funding for feasibility studies once proposals have been approved as part of the regional spatial plan, which means they can then work out the costs of different options knowing that the scheme would secure planning approval.

3.3 Learning from Germany

The German state investment bank KfW was set up in 1948 to support economic reconstruction, but its role has changed over the decades into tackling environmental issues. It now employs around 5,000 staff, half of whom are in Frankfurt. KfW made investments in 2010 of 28.5 billion Euros for SMEs compared with 4 billion for social and municipal infrastructure (or around 8% of its total investments). KfW boosts the capacity of cities to work up viable development projects, and effectively 'reinsures'

95 The source is a presentation by Frank Horovka at an RICS/Housing Forum seminar on financing infrastructure for housing.
96 Peter Hall, *Good Cities, Better Lives: how Europe discovered the lost art of urbanism*, Routledge 2013
97 *Healing Fractured Cities: a tale of suburbs in London and Paris*, URBED 2013

local commercial banks by sharing the risks, and taking a longer-term perspective. Thus in 2012 the KfW banking group invested 73 billion Euros of which 40% went into environmental projects and climate protection. There are seven main areas of investment of which one is municipalities and regional development banks.

The KfW Banking Group now describes itself as 'a bank of responsibility', and operates internationally.[98] Along with the Dutch BNG Group it is rated as one of the two soundest banks in the world, which means it can raise finance at relatively low rates of interest.[99] German cities are some of the most successful in Europe, even where, as in the case of Leipzig for example, they lost 90% of their manufacturing jobs after reunification. Much of the success is often attributed to a relatively localised financial system, with a plethora of savings banks or 'sparkasse' (municipal mutual banks) that have invested in the local economy of medium sized enterprises (Mittelstand). Intriguingly in 2010 43% of the loans to German SMES came from Sparkassen and Landesbanken (regional banks), and only 14% from the big commercial banks.[100] But these in turn have benefited from the resources and expertise of KfW and the regional investment banks, along with regional planning, and proactive city governments, have supported much higher levels of public investment than in the UK.

When West Germany was reorganised after 1945 power was carefully divided so that the Federal State could not tell the regions what to do, and the regions had to respect the cities. The functions are carefully allocated so that, for example, the regions are responsible for health, education and intercity transport, and also for economic development and regeneration. But though the regional development agency has much greater financial resources than the cities, it can only respond to projects and proposals put forward by the cities themselves.

This makes the role of the City Mayors very important indeed, as it is they that both negotiate with higher tiers of government and also coordinate the investment made by different state departments.

A number of visits to growing German cities such as Berlin, Hamburg, Hanover and Freiburg have discovered how funds are invested in local economic development and infrastructure, including house building, rather than in home ownership. Making housing much more affordable and neighbourhoods more liveable than in the UK,

98 KfW at a Glance: Facts and Figures, www.KfW.de
99 Global Finance
100 Gregg McClymont and Andrew Tarrant, *German: a banking ecology that supports the real economy*, Policy Network 2011

has given cities a boost, and for example, the historic city of Freiburg has expanded through planned urban extensions so that people can live close to work, and travel by tram or bike.[101] URBED's most recent study tour was to Emscher Park in the Ruhrgebeit, an area which has suffered from 'shrinking cities'.[102] Where land values are negative, they are of little interest to private developers, and require sustained and coordinated investment over many decades if they are to change direction. The area around the River Emscher in the Ruhr has not only lost most of its old iron and coal industries, but faced huge problems from contamination of the water system, creating even greater problems than in Yorkshire or the West Midlands.

An International Building Competition (IBA) was launched in the late 1980s to promote ideas and demonstration projects for the sub-region. The Emscher Landscape Park is one of over twenty programmes where the different local authorities that make up the Ruhrgebiet work together for the common good. Collaboration at first was not easy, as it involved 11 districts with a combined population of 5.1 million, in 53 towns and cities and an area the size of Greater London. Implementation started in 1992 under the theme of 'nature for people'. The Ruhr, which had been Germany's main heavy industrial centre, had a very poor image, and the River Emscher served as a sewer.

The original target was to secure high levels of investment- 5 billion marks but with no new money, so the initial impact depended on joining-up existing budgets. More than 400 project proposals were submitted under the six different fields, which were evaluated against quality, social and environmental criteria. 100 projects, which were all locally driven, were then implemented. 80% of funding came from the state government (North Rhine Westphalia) and 20% from the cities. Money from the equivalent of the British Environment Agency was used to build new bridges, and six new bridges were built through competitions, which provided symbols of change. The IBA only ran for ten years in order to avoid local resistance to people coming in from outside and taking over. 30 staff were employed, half in public relations, and the other 15 were planners. The core staff ran the process in collaboration with the city districts, though considerable use was made of consultants, (and for example Norman Foster won the competition to masterplan Duisburg Inner Harbour, and subsequently the rest of the old city).

One result of the IBA has been a network of people who work together well. Thus the Mayors of each city meet once a month to discuss the three most important issues.

101 Nicholas Falk, *Masterplanning and Infrastructure in New Communities in Europe*, in Teisdell, S and Adams , D, Urban Design and the Real Estate Development Process, Wiley , 2011
102 *Learning from Emscher Park*, report of TEN Group Study tour, URBED 2013

Officers from each city collaborate beforehand to draw up the agenda and briefing papers. The process is undoubtedly helped by the fact that all but two are members of the Social Democratic Party, and by the division of powers in the Federal German Republic, which puts the responsibilities and powers clearly on the lowest level of government. After the Park achieved its main objectives, the regional state agency decided to carry on and used a new slogan Concept Ruhr. Instead of disbanding the original teams and laying off experienced staff, as has happened in the UK, the teams have been incorporated in new bodies, and the budgets for the Emscher Park itself maintained (after considerable politicking!)

The agency sets out to promote projects in a number of different fields of competence e.g. design, health care, tourism. There are seven regional green corridors in which neighbours work together and the new masterplan extends them into the cities. The focus has shifted to promoting a 'knowledge region', as all the remaining coal mines are scheduled to close by 2018. The problem is seen as no longer converting sites, but converting brains to work in the new economy.

The concern is with sustainability in the widest sense under the theme **Ruhr 2020**. Surveys show that 30 per cent or people now recognise the value of the park even though the land is in thousands of ownerships. The current masterplan was only adopted in 2004 after over a hundred meetings, and some 600 people had been working together from 17 different cities.

Strategic planning and development are now coordinated by **NRW Urban LEG**, which stands for North Rhine Westphalia Landes Entwicklung Geselshaft. This regional development and housing agency reports to the Regional Parliament and works though development agencies in each city. For example in Dortmund, after the main steel works closed, NRW backed the Mayor's plan, and took on the funding of a new lake around which high quality housing has been developed. This allowed the steel company to concentrate on upgrading its works in Duisburg on the River Rhine. NRW is able to package funding from a range of sources, including KfW and the European Union, as well as any special federal programmes. As in the UK, the aim is to invest in projects that cover their costs and stimulate private investment, but with a much longer-term time horizon.

Because of KfW's reputation and expertise, their support for municipal projects has been the trigger behind much more local investment, and has enabled local authorities to take over land for regeneration and growth at close to existing use value. Knowledge of the prospects for a local economy is considered important in evaluating locations for new housing, as borrowers are said to overstate the prospects for economic growth. Furthermore, as the IPPR report points out, as most of their investment is channelled through commercial and local savings banks, they do not have to assess all the projects themselves.

This case study illustrates the role of investment banks in supporting local initiatives to promote regeneration. Much of Germany's post war success can be attributed to the quality of their regional planning, the way that local cities work together and with their universities and research institutes, assisted by regional development agencies. This in turn has been greatly helped by a system that joins up different forms of investment. KfW and the regional housing and development agencies like NRW Urban LEG have provided a strong incentive for city councils to promote projects that provide long-term benefits, and are helping Germany to retain its lead in designing and manufacturing transport and energy systems. It has also been greatly helped by the German system for developing unused land as set out in the box below.

German policy for unused land (Städtebauliche Entwicklungsmaßnahme)
Under the German Building Codes 165-171 the urban planning law enables the speedy procurement of unused land. It is used to mobilise land for development and to finance municipal development costs in situations where there is an increasing demand for housing, workspace, or public facilities. The measure is financed from the uplift in land values following development.

The municipality buys land at existing use value, and then sells the land when it has been planned and serviced for the price of undeveloped plots. The difference is used to fund social infrastructure such as schools, parking and green areas, and other costs involved in planning and development. Owners can fend off the purchase if they are willing to carry out development in accordance with the plan, in which case the municipality gets compensation.

The policy is used to freeze the price in areas designated by the local authority for development, such as in Vauban in Freiburg. It helps simplify the process which would otherwise result in complex and time-consuming negotiation over Section 106 or the Community Infrastructure Levy.

Source: Wulf Daseking and the City of Freiburg

3.4 Learning from the Netherlands
In the Netherlands, which offers the best lessons of all, the state investment bank BNG

Bank (Bank Nederlandse Gemeenten) was set up as far back as 1914. Since then it has played a key role in enabling housing plans to be implemented. Its web site states:

BNG Bank is the bank of and for local authorities and public sector institutions in the Netherlands. Half of the bank's share capital is held by the Dutch State and the other half by municipalities, provinces and a district water board. BNG Bank's clients are primarily comprised of local authorities and public sector institutions in the areas of housing, healthcare, education and public utilities. BNG Bank provides customized financial services ranging from loans and advances, payment services and electronic banking to consultancy and asset management. BNG Bank also participates in public-private partnerships. BNG Bank's specialized financial services help to minimize the cost of social provisions to the public.[103]

As in the UK a major priority has been to expand the housing stock in sustainable locations, with the difference that the Dutch have achieved what we only managed to talk about. The ten year housing plan, which is the mechanism for this remarkable building programme, is called VINEX. It produced over 450,000 homes in some 90 sustainable urban extensions, with very little public funding.50 of the suburbs have been in the conurbation known as the Randstad. With a population estimated at between 7.5m and 10m, a high level of commuter traffic, a strong cultural preference for houses rather than flats, and a natural vulnerability to flooding, the area bears strong resemblances to Greater London and much of the South East of England. Moreover, the population density of the Netherlands as a whole is comparable to, if not greater than, the South East of England.

The VINEX plan increased the housing stock by 7.6% in a decade largely through urban extensions in nearly a hundred cities with populations of over 100,000, and 30% of the units were affordable. Academics and practitioners agree that the Netherlands provides the best model of all for housing development in situations quite similar to those facing British cities.[104] This is because of the synergy between transport and city development.[105] Also their social housing is not stigmatised, and housing associations account for half the new homes built.[106] Success has been widely attributed to the deep-rooted partnership approach among government agencies and developers,

103 Capital Markets, BNG December 2013

104 E.g. Peter Hall, *Good Cities, Better Lives: How Europe discovered the lost art of urbanism*, Routledge 2013

105 Article by Hugo Priemus in *Investing in Better Places: international perspectives*, ed Sharon Chisholm, Smith Institute , 2011

106 Ed Julie Cowans and Professor Duncan Maclennan, *Vision for Social Housing: international perspectives*, Smith Institute 2008; Ed Katherine Scanlon and Christine Whitehead, *Social Housing in Europe: a review of policies and outcomes* 11, LSE 2008

combined with the so-called 'Polder mentality' which forces different interests to face common problems, as a result of half of Holland being below sea level. As in the Netherlands, the main growth opportunities lie on the edges of city regions and in the medium sized towns around London and in the greater South East. If we matched what the Dutch achieved through their ten year VINEX housing plan we would need some 400 sites, rather than a handful of new towns, or say five in each district of over 100,000 population (to leave out the smaller rural authorities).

Our case study features the prosperous town Amersfoort, which has a population of around 150,000, and is close to the City of Utrecht on the intersection of two motorways. It is now regarded as one of the 'greenest' towns in the country, and the city council has promoted three urban extensions, two of which form part of the VINEX programme. The latest, Vathorst, consists of some 11,000 homes plus shopping facilities, business and community facilities, and is over half completed. The process started in 1998, when the municipality and the government drew up an agreement on the size of the extension, the contribution they would make to reclaiming contaminated land, and how the settlement would be connected to the two motorways it adjoins.

The Vathorst Development Company (OBV) was then set up as a 50:50 joint venture between the local authority and a consortium of private landowners and developers, who pooled their land holdings. The private sector included those who had bought land in the area but also those who the city wanted to be involved as a result of their track record. The Vathorst Development Company is responsible for land acquisition, urban planning, engineering, commissioning infrastructure, allocating sites and economic and cultural development. It employs a small staff of fewer than 15 with a Chief Executive from the private sector and a Chairman appointed by the municipality.

Financing the company's budget for the development of 11,000 homes, a shopping centre and business park amounted to €772 million, of which half goes into infrastructure and the public realm. The government provided only 6% of the total investment in the VINEX programme (according to an estimate by URBED). At the start OBV raised €250m through loans from BNG Bank repayable over 15 years at an interest rate of 5%. The 500 hectares of former agricultural land was acquired for €192m, or €380 000 per hectare (€175,000 an acre). There was then a further investment in infrastructure and the public realm of €384m. The company expects to realise €590m from the sale of housing plots, and €150m from offices and amenities.

The borrowings are repaid out of the proceeds from land sales, and the company has built up a 'buffer', which allows it to act entrepreneurially. For example, it funded the railway company to open a station several years before the population justified it, and it underwrote an entrepreneur to open a restaurant to provide a new neighbourhood with a place where residents could meet. The underlying risks are taken by the shareholders and ultimately possibly by the local authority, who benefitted from the social housing that was built, and therefore provided the necessary leadership. Each shareholder/developer carries out the detailed architectural work for the area it has been allocated. The company then provides the services and infrastructure. When these are ready, the site is sold to the developer to construct within an agreed and binding programme. The value of housing plots is based on the estimated sales proceeds. Each housing plot realises around €50,000, or around 28% of the value of the completed house. Sites for social housing are transferred to the local authority, (which provides them with a major incentive to exercise leadership), and a proportion are sold to occupiers on low incomes at a discount, with an agreement that on resale a proportion of the uplift comes back to the local authority.

The deal works because the public private partnership acquires unimproved land at close to agricultural value. Also as OBV borrows at lower rates than a private company (5% vs. 7.5%); it is able to fund advance infrastructure and take many of the risks out of development. OBV say they can exert influence on developers because they know best what the community wants, and because they have provided the infrastructure at a lower cost than developers would have incurred. The process also works because most of the developers and house-builders are members of the company (as well as two social housing companies). The joint venture company approach provides the flexibility of a private company with the social acceptability of a public enterprise, without being snarled up in some of the EU procurement rules. The Dutch approach of joint venture companies provides a particularly useful model for smaller district councils in areas facing growth pressures as it shows how to combine the expertise and resources of the public and private sectors to good effect.

Conclusions

These three contrasting examples in different countries in fact have a lot in common, as all benefitted from the support of a state investment bank in the early stages, and would never have happened under the British system where the private sector is expected to take the lead, or where limited grants are available for land preparation and social housing, but little else. As an excellent series of case studies on urban regeneration in Europe points out:

The existence of stable, semi-independent sources of funds in France, Germany and increasingly in other continental examples, works as a conduit for investment because *it is left alone, indeed encouraged, for this purpose, by finance ministries and is not raided as a source of further capital by the private and commercial sectors.*[107]

In assessing the benefits that would come from having an equivalent British state investment bank, with a remit that includes supporting local authority plans for broadening the housing stock, the following eight features stand out:

1. An asset base and independent status allows support for long-term projects that are in the public interest and enables finance to be raised at relatively low cost

2. A board with diverse ownership and expertise makes it relatively free of political bias and capable of boosting investment in projects that support local growth and regeneration

3. Investment funds are channelled into projects that boost local capacity, not frittered away on 'bridges to nowhere', through the ability to say no as well as the capacity to spread good practice

4. Investment in local infrastructure, including land assembly, masterplanning, roads and basic utilities helps the growth of SMEs as it opens up sites for small builders, thus improving choice and competition, and boosting the supply chain

5. Land values become more realistic when they are no longer driven by speculative developers, and housing becomes more affordable without excessive financing charges and profit margins

6. The capacity to assess and support major housing developments makes it a good agency for innovative government programmes, for example to save energy by promoting renewable energy solutions (as KfW does so well)

7. By accessing low cost sources of finance, due to its stability, it can be an ideal financial partner working alongside local authorities to help them implement growth plans

8. Ultimately it will strengthen private sector capacity, by removing some of the upfront risk on major schemes, as well as reducing the cost of capital for infrastructure investment that cuts energy consumption and unnecessary car use through the growth of the 'green economy'.

107 Charles Fraser in ed. Chris Couch et al, *Urban Regeneration in Europe*, Blackwell, 2003

Section 4

4. What roles would a British investment bank play

What roles would a British investment bank play

But it should be obvious that mere abstinence is not enough by itself to build cities or drain fens

John Maynard Keynes

To understand how a state investment bank could play a role in overcoming the barriers to building more homes, upgrading local infrastructure, and supporting economic growth outside London, we need to know how the development process works at present, and how it would change once there was a clear and substantial source of development finance for designated areas and qualifying projects. This section sets out how a Municipal Investment Corporation - the housing and local infrastructure arm of the new bank - could be established, and the benefits it should bring. I show how it would operate by running through the stages a major urban extension such as on the edge of Oxford or York might go through under the current planning and development system, and how the system could be changed at minimum cost and effort.

4.1 Establishing the organisation

Setting up a new organisation takes time, and inevitably raises many questions about structure, staffing, and funding, and indeed whether a new body is needed at all. Enough answers have been suggested in previous papers from both the left and the right to indicate that some form of state investment bank would be both desirable and feasible.[108] There have also been well-argued reports on the merits of British local authorities issuing bonds, as American cities do, and not simply relying on the Public Works Loans Board.[109] The Smith Institute has already investigated the potential for tapping local authority pension funds through some form of clearing house, and it appears that a very small part of their investment (under 2%) is in local infrastructure.[110] An initiative by Local Partnerships UK supported by the LGA may well lead to setting up a Municipal Bonds Agency to reduce funding costs by tapping into pension funds.

As highlighted in the previous section the Dutch model of BNG Bank, (or Bank Nederlandsche Gemeenten, which means Dutch municipal bank) offers the best guide to such a bank or corporation might work in the UK. The initiative would need to

108 Dieter Helm, James Wardlaw, Ben Caldecott, *Delivering a 21st Century Infrastructure for Britain*, Policy Exchange, 2009; Nicholas Tott, *The Case for a British Investment Bank*, Labour Party Policy Review, 2012; Tony Dolphin and David Nash, *Why We Need a British Investment Bank*, IPPR, September 2012

109 Tom Symons, *Capital Futures: Local capital financial options in an age of recovery*, Local Government Research Network, 2011

110 CLES et al, *Local Authority Pension Funds: Investing for growth*, The Smith Institute, 2012

be supported by the Local Government Association, and leading city regions such as Manchester and Birmingham, and by counties in Cambridgeshire and Oxfordshire as well as by London to overcome understandable Treasury opposition. In short the benefits are that it would fill an important gap in the expertise to assess both projects and borrowers, thus providing an important check on madcap schemes. It would reinforce commitments to both localism, through a devolution of real power. would be in line with the desire of many local authorities to assume more control over their futures, and to reduce dependence on central government grants. It would also be an investment for future generations, by building homes that younger people so desperately need.

Given that it would have wider functions than a bank it is referred to as the MIC and hereafter as 'the Corporation'. It might be organised as a separate subsidiary of the BIB, with a carefully chosen Board of Directors who really understood housing finance and property development, and were committed to 'breaking the mould' like the Housing Finance Corporation (THFC), which provides another good model. This is already channelling an estimated £5 billion of funding into housing associations into housing associations. However what is proposed here would operate on a much wider scale, and in markets that are not underpinned by housing benefit. The investments are therefore potentially much riskier but also offer greater rewards if land can be acquired at the right price, (an issue that is taken up in 3.2 below).The challenge of building communities fit for the 21st century will almost certainly provide a strong pool of applicants to join the management team, including some of those who have taken early retirement from agencies such as English Partnerships and the Regional Development Agencies.

Like the European models, the new Corporation would supplement the finance that goes into individual mortgages with a mechanism for promoting sustainable local growth through investment in local infrastructure, using private bonds (see 3.5) It would take advantage of the considerable funds seeking inflation-proofed and asset backed returns that are currently under-invested. The Corporation would deal directly with both local authorities and the larger housing associations that act as developers, who in turn may enter into joint ventures with private development companies, or employ builders directly. It would therefore be acting in the public interest and supporting, not restricting, competition. It could also be a major force in the growth of a professionally managed private rental sector (as recommended in the Montague Review[111]) as well as in energy saving forms of local infrastructure (thus meeting some

111 *Montague Review of the Barriers to Institutional Investment in private rented homes*, DCLG 2012

of the Policy Network's concerns). It would also seek to work closely with the Housing Finance Corporation.

The new body will function as a 'public corporation' in European terms so that the funds it raises should not count as part of Public Sector Borrowing, Most of its funds would come from private investors, but central and local government would provide the equity needed at the start as part of its commitment to a BIB or regional banks. It should not be seen as an arm of central government, who would only choose a minority of directors.

As with the French Caisse Des Depots, the bank could also act as an agent for certain government regeneration programmes where a financial return is expected, and charge an appropriate management fee to add to the commission it receives for organising major loans. In this way it will in a better position to package funding, and indeed to leverage any grants or 'soft loans' that may be available, for example from the European Union and the European Investment Bank. It would seek to provide a much needed source of funds for innovative forms of housing such as Custom Building and Cohousing in the crucial period before these qualify for individual mortgages from banks and building societies.

Another source of funds would be to pool funds from local authorities Housing Revenue Accounts and sources such as City Deals, thus providing a valuable 'smoothing' function. There is even a possibility that it could work with the banks that local authorities are starting to set up, such as in Salford, Cambridge and Hampshire. Here the potential for providing funds for local initiatives that are making better use of under-used Council properties, such as surplus buildings or car parks, again demonstrates the potential for 'joining up' investment and development, and getting much better value from public assets. Crucially it would employ the knowhow that is now lacking, and enable local authorities to learn from each other, as the Housing and Communities Agency formerly did before the cutbacks.

Investing in housing and local infrastructure, or sustainable urban growth, is very different from supporting Small and Medium Sized Enterprises (SMEs), which is the primary role for a BIB, and will involve different people with different skills and experience. However, as with the European models, there will be a number of advantages in combining the two functions:

- The corporation would fill gaps in long-term funding and not displace the commercial banks who specialise in short-term loans and mortgages to individuals and small firms that are often property backed. Instead it will provide a clear source of funding for the innovative types of project, such as cohousing or custom build, that banks tend to turn down. Investment in housing and local infrastructure should support local economic growth, and therefore knowledge of local potential is essential. An important section will deal with local and regional economics and market information, and there is considerable scope to improve the way strategic development sites are identified.

- It might recruit some of its staff from bodies like the European Bank for Reconstruction and Development (EBRD) or the European Investment Bank that have relevant experience in project and programme assessment. It would also employ some of those who have experience of packaging complex schemes, but have taken early retirement
- It would develop relationships with key local authorities, who are committed to ensuring that enough suitable sites with planning permission are available. Hence it will need to operate on a regional and sub-regional basis, often through arrangements with other financial bodies (rather as the Green Investment Bank has been doing). There should be economies of scale in covering the country, as the Corporation can develop expertise in different forms of housing investment, for example estate renewal versus building on greenfield sites, and the relevant costs and returns from different forms of development
- It would also maintain close relationships with institutional investors, some of whom are becoming interested in the opportunities for developing the equivalent of new towns, but complain of the difficulties of finding good projects to invest in. One example is Legal and General, who say they are planning to spend up to £5 billion on five new towns over the next ten years.[112] It is likely that some of the relationships will have been brokered at Infrastructure UK, who might well become part of the new organisation.

While it can be argued that the capital market ought to provide the funds that are needed without any government intervention, there are at least five good practical reasons for not leaving too much to the markets and chance. The first relates to redressing market failure. Private property investment or 'irrational exuberance' not only brought the US and UK economies down, with side effects round the world, but are one of the main causes of growing inequality. Since around the mid-1970s non-homeowners have been left further behind. As land values and house prices in many areas have far outpaced general inflation or economic growth those with an asset have seen their wealth increase rapidly in ways which many see as unfair.[113] The land market

112 Interview with L&G Chief Executive in the Sunday Times, January 19th, 2014
113 Paul Cheshire et al *Urban Economics and Urban Policy*, Edward Elgar, 2014; Thomas Picketty, *Twenty-First Century*, Harvard University Press, 2014

operates very differently from other markets, and cannot be treated in the same way.

Second the number of capable developers and building component suppliers has shrunk. Simply splitting up the existing banks or separating the retail and investment functions will do little to rebuild the foundations that are urgently required. Instead the Corporation needs to help smaller builders and developers to grow, not just support the best established. It should have a particular interest in new bodies such as Community Land Trusts that offer a different model for providing affordable housing long-term, and that currently have no source of finance to turn to. The Corporation can support the Treasury's desire to make property markets work better.

The third reason relates to changing institutional 'mind sets' or values. With the majority of wealth tied up in housing, inequalities have widened, and getting a foot on the property ladder has not only involved taking on excessive debts, but has also created expectations of home ownership as the best form of investment. This may in part explain why the UK economy has continues to have a productivity problem, as continual house price inflation has fuelled land speculation which in turn has diverted investment away from the 'real economy' into chasing short-term profits.

The Corporation would follow a different set of values from those forged either in the market place or the civil service, inspired perhaps by the municipal corporations that transformed Victorian cities, for example by bringing water from Wales into Birmingham or the Development Corporations that built the New Towns, such as Peterborough.[114] The Corporation, like KfW, will be an agent of 'responsible capitalism'; and will 'build for posterity not austerity.'

The fourth reason for creating a new body is to ensure good and innovative projects are devised and that funds are invested where they will produce long-term returns. It is vitally important that increased investment is matched by increased saving, which means raising productivity, for example by enabling places with untapped growth potential such as Bristol or York to expand. Local investment needs to be carefully targeted so that it releases capacity constraints, and does not simply provide politicians with opportunities to cut ribbons or avoid painful decisions. Rather than letting local authorities (or national governments) take on debts they cannot expect to repay, the Corporation would vet both the projects and the borrowers. Just as the Private Finance Initiative turned out to be an expensive way of delivering upfront funding, so too could government guarantees, even though the Public Works Loan Board seems to offer

114 Tristram Hunt, *Building Jerusalem: the rise and fall of the Victorian city*, 2005, Metropolitan Books

relatively cheap money. The Corporation should minimise the number of blunders!

Finally too much of the talk of new towns has been wishful thinking. It will take time to build new communities which usually involves surviving at least one turn of the business cycle. Calling them Garden Cities does not solve the basic problem of channelling demand into a new location. An examination of the relative costs of the different options reinforces the common sense view that is only by extending medium sized towns with growth potential as well as by densifying some existing built up areas (such as Council estates) that private investment can be made to pay off.[115] Places like Ebbsflett on High Speed One are quite exceptional. As so much needs to be invested upfront in land assembly and basic infrastructure, mechanisms are needed to avoid all the value going to 'free riders', which means being able to share in the uplift of land values as a result of both planning permission and investment in related infrastructure.

Here the German land valuation model provides one practical answer as we will shortly see. But reaching agreement is not just about powers, but also requires securing the trust and commitment of local authorities, which will be a further core skill for the Corporation as it takes on the role of building capacity, rather as the HCA once tried to do with design. In order to see where the BIB and the MIC would add value over existing arrangements or other options, we now need to consider what currently happens as far as major sites are concerned, and what needs to change.

4.2 Designating development sites

The first stage process should be to agree where development should take place. This is often prolonged, with local authorities reviewing 'Issues and Options', responding to both proposals from developers and local consultations, before issuing a core strategy. Even when this is approved after many years, it can still lead to unwelcome applications, often decided on Appeal, and authorities may choose to refuse or defer decisions on unpopular sites to evade responsibility. Little distinction is made between regeneration areas with low property values and high remediation costs, as in many Northern cities and Eastern parts of London and some Southern cities, and growth areas in much of the South East and in the rural fringes of some Northern cities.

To establish costs and values for promising opportunities, the Corporation could provide funding for feasibility studies, as happens in the French development system, once there was an agreed plan for the City Region or development corridor that identified where most housing and employment expansion was expected. The planning

115 These arguments and the supporting evidence are set out in URBED's submission for the Wolfson Garden City Essay prize

work budget could be managed by the Homes and Community Agency, as has been happening in examples like growth around Didcot, or delegated to authorities that were large enough to employ relevant expertise, either by themselves of in combination with others. This is likely to require reemploying some of the experienced staff that have been let go as a result of cutbacks, rather than relying excessively on private consultants.

A further change is to stop speculation in land values on strategic sites where planning permission might be granted (so-called Hope Value) by applying the German system for 'freezing' land values in designated sites, and capturing part of the uplift to fund the infrastructure needed for growth (see 3.3). Such a policy needs only apply to large schemes of say 1000 units or more, and so would only affect a small minority of housing sites and hence should not arouse too much opposition once the arguments for tapping 'betterment' are spelt out. But the policy would account for the majority of the extra homes that are planned, and the huge differences between agricultural and housing land values, especially in the Greater South East, must be tapped if public funds are as limited as they are. The measure would be combined with policies that enabled Compulsory Purchase, if the owner failed to undertake the agreed plan within a specified time (which the HCA can already do). Another option is a system of land taxation such as in Denmark which would charge owners of large sites with planning permission as if the land had been developed for the approved use. This would please economists by imposing a 'holding cost' on doing nothing. It might come out of a review of the Rating system, such as introducing extra bands at the top.

4.3 Approving planning frameworks

Once sites have been designated (which had started to happen under the Communities Plan and through the efforts of 'delivery bodies' such as the Gloucester Urban Renaissance Company) funding would be made available for working up masterplans or development frameworks. Under the current system, these are usually worked up by private developers or landowners using private consultants. The problem is that most of the work is wasted if the scheme does not go ahead. It also leads to inflexibility and time-wasting conflicts, as local authorities seek to tie everything down. Furthermore where, as often happens, land is several ownerships, it can be hard to agree who should fund the necessary planning work, which can easily amount to several million pounds for a scheme of 5,000 homes, with possibly as much as half going on the Environment Impact Analysis required under European Regulations. The finance that should go into ground works are used in the UK to commission studies and fight planning battles. A fraction of all that effort and cost would produce agreed development frameworks so long as there was proper local leadership to 'sell' the benefits.

Research suggests that European cities have grown faster and better because their local authorities are supported by a planning system that links planning and development, and with local politicians who act as leaders, not government employees. In France, for example, there is a seven stage process, which starts with a City Contract or Contrat de Ville between government and the municipality and leads on to a development agreement for the land in question with a Declaration of Public Utility.[116] A key element is the idea of Zones d'Aménagement Concerte (ZACs) or Comprehensive Action Zones. The existence of the Corporation would incentivise local authorities to undertake or commission the basic work needed to prepare a development framework for larger sites. The framework would set the basic parameters in terms of key factors such as:

- Size of development in terms of ground area and numbers of units
- Plot coverage and densities (along with simple rules or Codes explaining the underlying principles)
- Proportion of affordable or social homes to be provided
- Levels of commercial units
- Social facilities
- Environmental policies, for example with regard to nature and water

The work would include consultations with local interests to ensure that legitimate concerns were met through mitigation, for example by improving public transport or road measures to relieve anticipated congestion. Consideration should also be given to changing the Compensation system, perhaps following French practice, in order to 'buy off' landowners who might otherwise mount strong opposition. However we should not expect universal support, as there are always many who benefit from the current system and indeed may profit from continuing shortages.

An approved planning framework for large or strategic sites could enable the cost of land to be contained at no more than 25% more than its current value, and as a reserve would make use of the CPO powers and expertise that the Homes and Community Agency has been given. This would overcome the lack of experience and resources on the part of local authorities, and enable them to avoid local criticisms when other services are being cut. This is far simpler than some of the 'auction' systems that economists have promoted, where, as in the French phrase, 'the best is the enemy of the good.' The added value of the BIB is to increase what are currently very limited resources for upfront investment by taking a 20-30 year perspective on land development (thus smoothing out the peaks and troughs of the property cycle). The underlying

116 See for example Charles Fraser in ed. Chris Couch, *Urban Regeneration in Europe*, Blackwell Publishing, 2003

financial information can be readily made available to reach agreement, once it is clear that government stands behind the agreed plans.

4.4 Working up feasible schemes

In situations where there is a strong land market, such as in the South East, it will be relatively easy to attract house builders. However many district councils are too small to have a full range of expertise and many of the most experienced staff have taken early retirement. Where the local authority already manages a large stock of social housing, the process can be improved by the use of joint venture companies, as in the case of the agreement between Oxford City Council and Grosvenor Developments for Barton Park. In areas where the risks are much greater, and demand is less predictable, some kind of roving Development Corporation at a County or Metropolitan area level could bring together the expertise needed to procure development, and the necessary technical studies.

A combined development agency could be set up under existing legislation, through agreement between adjoining local authorities, who might second some of the staff to help keep costs down. Indeed there are already a number of authorities that are combining planning and development staff, such as in Cambridge City and South Cambridgeshire. Where there is not agreement a Development Corporation would need government approval (and the TCPA has published a valuable update of the legislation which could cover a range of situations). A Development Corporation or joint venture would need to be set up for at least 20 years to attract the calibre of staff needed to make a difference, and to raise the finance needed to prepare land for development and benefit from some of the uplift in land values once the area 'takes off'. We must not repeat the mistakes of the previous crop of 'local delivery vehicles' that were closed down before they had much time to prove themselves.

One of the values of the Corporation will be to ensure that public funds are used to greater effect by avoiding wasteful remediation works or excessive advance infrastructure (which is encouraged by short-term grant regimes), as in Greenwich Peninsula for example. It would instead provide low cost long term loans that can be repaid out of the proceeds from selling off serviced sites with planning briefs that offer planning permission on compliance. At present the Homes and Communities Agency has been instructed to maximise the revenue it gets from selling off public land, and quality is being downplayed. Yet as Planning Minister Nick Boles MP said at a Berkeley Group event on February 4th 'The existing house builders are never going to build the number of homes that are needed … Quality is the key to unlocking quantity'.

Replenishing the capacity of our building industry is going to require public land to be used as equity, and giving small builders a better chance to compete. As in Holland, for example, the price or value of large sites could be set as a proportion of the expected selling price of the units, using an approved scale. This would allow developers to be selected on the quality of their proposals and capacity to implement the agreement swiftly, rather than on the size of their bid. The value would be set in order to provide the required return on the finance borrowed, after allowing for expected site remediation and local infrastructure works. Payment would be made when sales are made and the real value is determined. This in turn will affect what the original owner earns, with the option of being paid off early at existing use land value plus say 25%, or staying with the project, and receiving a ground rent, plus a proportion of what is secured once development has taken place, and units have been sold and occupied. Such an approach will almost certainly provide better value than selling sites to the highest builder, only for them to negotiate the specification down, which in turn intensifies opposition to all development.

One good way of incentivising local authorities to play a proactive role in allocating land for development and assembling sites is to give them a proportion of the affordable housing to allocate as they want in return for making land available in appropriate locations. This works well in the Netherlands, where a proportion of the affordable housing is then sold to owner occupiers at a discount from market prices under a system in which the local authority retains some equity and benefits as and when the unit is resold in due course. The MIC should have a commitment to both balanced and sustainable communities written into its mission statement, as this, of course, will guarantee long-term value.

4.5 Raising development finance

The real problem many involved in the financial markets argue is not lack of finance, but lack of enough good projects. In recent times house builders, who are largely public companies, have raised large sums of capital on the strength of balance sheets that are buoyed up by the value of the sites they have acquired for development. Housing associations then buy sites off house builders, and compete for both sites and grants. Larger housing associations have raised large capital sums by issuing bonds, which are secured against the rental income on all their properties. Local authorities that have retained their properties now have greater freedoms under the reformed Housing Revenue Account regime and can already raise finance at relatively low costs through the Public Works Loan Board. Some, like Islington, are starting their own developments while others may prefer to enter into partnerships with established house builders.

The problem is that even when land is provided as equity, house builders have to cover both their funding costs and profit objectives in situations which are intrinsically risky, and involve huge upfront costs. Developers have told me that they need to up their profit margin from 25% to 30% to cover the risks in the British market. The major Swedish construction firm Scanska withdrew after a brief foray into the British market because the returns were not high enough. The public sector pays much less for the money it borrows. However local authorities have been capped in what they can borrow because of Treasury concerns over the public funding deficit, which seems to override all the arguments for prudential local investment. When Britain moves to the European system of the General Government Finance Deficit, (as they are required to do) British authorities should once again secure the freedoms of their Continental counterparts, with some real benefits.

One solution is not counting the 'public corporations' against government borrowing, so that good investment is distinguished from expenditure to maintain current levels of consumption.[117] Another is making sure that projects work as planned.

Added value should come from providing long-term capital for projects in areas where there is an agreed development framework and Local Investment Agreement, as the risks and costs of housing development are then both reduced. The Corporation will undertake the appraisals needed of both the borrower and the project to assure investors that they will get their money back, and should provide a much more cost-effective approach than going round the City of London. This should also satisfy the Treasury's concerns to avoid the UK getting a bad reputation, as it would enable loans to be monitored.[118]

As an example the cost of the 250 million Euros provided by BNG in the Netherlands for the development of Vathorst was 5% repayable over 15 years, compared with the 7% or more that a private builder would expect to pay there. The BIB's knowledge of local economic as well as housing prospects, through being involved in funding SMEs (as with KfW in Germany), should help reduce risks on bad loans to projects that do not work out as expected. It will link housing investment to areas where new jobs are most likely to be created. A new source of long-term private funding should also enable embryonic financial centres to grow, such as in Leeds, Manchester or Birmingham, and

117 CIH and Coopers and Lybrand, *Challenging the Conventions: Public Borrowing Rules and Housing Investment*, 1995; John Parry, *Treating Council Housing Fairly: how changed borrowing rules can build more homes and boost the local economy*, National Federation of ALMOs, 2013
118 John Perry, *Let's Get Building: the case for local authority authority investment in rented housing to help drive economic growth*, for the LGA and others, 2012

thus help their economies to rebuild their foundations, as the costs of infrastructure there will be significantly less than in growth areas in the South East.

As much of the funding will come from pension funds that are already tax exempt, there should be no need for further legislation. What is more, such a system will satisfy the appetite of pension funds looking to make larger investments of around £5 million a time in funds that are large enough to allow an exit without having to close the fund. Bankers have told me a bond needs to raise around £100 million to make its issue worthwhile, as evaluations have to be produced for both the project and the borrower. As examples, some 28 bond issues were made by housing associations since January 2011, typically for terms of around 30 years, and over half were for nominal amounts of over £250 million.[119] The cost of funds was typically around 5% or two percentage points above gilts, with loans secured against the assets they were used to acquire, and five banks handled the bulk of the business. But maintaining the supply of private funds requires a good supply of investment projects to choose from, plus some level of security, such as a charge over the land. It also requires a long term planning horizon of at least 20 years to allow for the ups and downs of the business cycle.

The Corporation will score over both private banks and government departments that inevitably have much shorter time spans and narrower perspectives, and should also benefit from reduced transaction costs. Thus the Department of Transport is primarily concerned to cut travel times and improve safety, and ranks projects accordingly; it does not see its role as supporting developments that create new employment and homes in places where walking and cycling will predominate, even though these may cut congestion and carbon emissions. Grand projects such as High Speed 2 are not fully integrated with developments around their terminals or along rapid transit networks that would produce a real modal shift away from cars.

The MIC would specialise in a new generation of 21st century Garden Cities or Expanded Towns that are built around high quality local transport and energy systems, and thus help the UK to catch up with the rest of Northern Europe.

One further innovation that would both satisfy the calls for a return to regional or local banks, and that would also tap additional sources of saving will be to enable subscriptions in bonds for innovative developments to be sold through local offices, thus generating greater interest in ambitious development projects that people can see for themselves. One possibility that has been suggested is to adapt the current system

119 Andrew Heywood, *Investing in Social Housing*, The Housing Finance Corporation, 2013

of National Savings to provide for a bond that was dedicated to building new homes, or investing in energy saving measures. Another would reinforce links with the provision of mortgages for house purchase by working through Building Societies. The remaining Mutuals such as Nationwide or the Peterborough Building Society will almost certainly be interested, and could help channel funds into local projects in areas known to be in high demand. They may well also support projects such as Cohousing and other forms of 'Custom self-build' as well as the growing number of Community Land Trusts, as they start to show their viability, and even some Passive Houses.

Some would suggest that all that is needed is for municipalities to have the freedom to borrow against the prospective increase in their business rate base. Certainly the American model of municipalities raising bond finance for projects that have won popular support in referenda has much to commend it. Portland, Oregon, which is regarded as the one of the most sustainable cities in the USA because of its tram system MAX (the Metropolitan Area Express) provides a particularly inspiring example, as a bond for extending the tram line to the main railway station was funded from the expected property tax income from higher density housing schemes around the station. However warnings from cities such as Detroit that have ended up being unable to service loans illustrates the downside. This is a further reason for a Corporation having the expertise to assess both the project and the borrower. This will give confidence to other investors, such as pension funds, that lack their own expertise, and thus raise far more than would otherwise be possible from private investors.

Infrastructure bonds to mobilise investment

The Observer on 12th April carried an editorial headed "Prepare for the great pensions crash" which offered the following recommendation:

(Employees) need more reliable places to invest, now that confidence in private sector final products is so low. The government should turn its part-ownership of the banking sector to that end. It could , for example , create a national bank for economic reconstruction dedicated to financing infrastructure, renewable energy, social housing. It would issue bonds that would make an attractive and safe investment vehicle for ordinary savers – citizens lending money to help fix a broken economy and getting it back with interest on retirement. But there is no sign that Labour has sufficient will or imagination for such a scheme. It also looks unlikely even to address openly the pension problem.

The Policy Exchange report *Delivering a 21st Century Infrastructure for Britain* proposes to resolve the problem of raising huge sums at low costs through what is known as the

Regulatory Asset Base or RAB. Once approved by the Regulator, this enables utilities to raise funds knowing that a contract to purchase their products will be honoured. In turn utilities are incentivised to invest in order to boost their profits. However the uncertainties created by government policy, or lack of policy, has increased the risks and therefore the funding costs to the point that major players like RWE, the German electricity company, is withdrawing from the UK to concentrate on more stable markets. So unless the Treasury is weaned away from its fixation with competition, costs will rise as infrastructure wears out and revenue falls. Yet as the report says 'Infrastructure bonds could become a normal and substantial part of the portfolios of the wider population'. As in Germany, for example, it would become smarter to invest in society's 'common wealth', and less important to focus on amassing individual wealth in the form of borrowing as much as possible to gamble on the housing market.

Bonds that raise infrastructure funding for local projects will have a wide appeal, and could help solve the growing pension crisis. They can be promoted to local authority pension funds and wealthy individuals with an interest in a particular growth area. Tax incentives could be used and the Policy Exchange proposes extending the use of ISAs for this purpose, but they are probably unnecessary. At this moment, with interest rates so low, a bond that offered a couple of interest points above inflation would be very appealing to those thinking about their old age! Such an innovation would be in line with current government thinking, as the 2009 Budget statement referred to experimenting with Accelerated Development Zones, but would make it work. The Conservative Party's policy paper *Control Shift* praised the use of bonds (but did not make it possible for local authorities to assist their issue). Labour could fulfil its commitments without leaving everything to chance.

The key to a successful bond issue is to provide an inflation proof investment that covers the annual payments (which might be through sources like parking revenue or a service charge on energy supplies, or sales of serviced plots). It is also essential to be able to repay the bond investors either progressively or at the end of 20 years or so, and provide some kind of bonus, which conveniently should extend beyond the normal business and property cycles. Repayment at the end could come through the sale of land purchased at the beginning, and perhaps rented out for an interim uses such as park and ride sites, or for growing food, which would provide a greater incentive to await maturity. The key of course is that by the time the bond matures, the value of the land will have increased hugely as a result of quality development, natural urban growth and inflation.

Bonds issued by joint venture companies or County and Unitary Authorities could also tap investments from local authority pension funds, (as for example, URBED did when we set up the London Small Business Property Trust with CIPFA.). Some of the funds may need to be under-pinned by having recourse to local tax revenues in order to raise funds at the lowest possible cost, and to allow for the risks of the scheme not working out as planned. This is where Tax Increment Finance or the concept of Accelerated Development Zones referred to in the 2009 Budget would help. But the real appeal will be through local authorities committing to providing the necessary large housing sites with planning permission that makes development viable, along with the timely provision of related infrastructure.

4.6 Funding hard infrastructure

Many of the largest housing schemes depend on 'piggybacking' off existing infrastructure in areas on urban fringes. These may well be in sensitive areas designated as Green Belt' or where new infrastructure is required, such as a road linking several main roads (as in Houghton Regis or the A34/A40 link in Oxford) or bypassing a major town (as in Bedford or Ashford). The early garden cities were only feasible because Letchworth was located on the Great Northern Railway line to Cambridge, while Hampstead Garden Suburb was developed because the Northern Line was being extended up to Golders Green.

The greatest potential uplift in land values will come from places that have not previously been considered for development, such as in the Green Belt or Metropolitan Open Space. The process for Green Belt Review is controversial and protracted, and faces well organised opposition from bodies such as the CPRE and media such as the Daily Telegraph. It can only be justified in situations where demand is so strong (measured for example by house prices in relation to average household incomes), and where there equal commitments to new extensions or improvements to the Green Belt. One measure that might work would be to ensure that Development Frameworks require an overall increase in the level of biodiversity and access to open space, taking advantage of Green Infrastructure plans such as the Green Grid in East London. Great care will be needed to avoid creating another 'developers' charter'.

Where new infrastructure is being provided there is no standard way of recovering a proportion of the costs, other than through Section 106 provisions or the Community Infrastructure Levy. Both systems are flawed, with for example large amounts of money provided by developers going unspent, while adjoining land owners benefit as 'free riders'. Joining up development and infrastructure is fundamental to the idea of Smarter Growth through a set of principles that would meet the arguments of some of the most effective opponents of development. We badly need not only a much simpler system, but also one that avoids unnecessary uncertainties and obstacles to the costs of development. Furthermore CIL will only raise at best around a third of the cost of the infrastructure needed, according to studies in both Milton Keynes and Cambridgeshire. Hence it does not solve the basic problem of rebuilding our worn-out infrastructure, yet is complicated to administer.

So instead of considering each infrastructure project in isolation and in comparison with other similar projects across the country, we need to make the decisions at a sub-regional level to ensure that we get best value for any major public commitment, which requires changes in the way planning and property taxation works. One easy way is to make use of the requirements from Europe for 'smart investment' under the Territorial Cohesion proposals. This could be done by all the stakeholders such as transport and education providers signing up to Local Investment Agreements to firm up proposals, particularly with regard to timing. The Treasury has already agreed the principle of Earn Back in the City Deal negotiated with the local authorities around Manchester and something similar for Cambridge. But there is as yet no general solution for places that are to benefit from City Deals.

As an example in Oxford, with the least affordable housing in the country, where housing costs some eleven times average earnings, £80 million is being spent on a new rail link to London via Bicester. And a great deal more is being invested in electrification, resignalling and a new station. A commitment has been made in Oxford for an initial £50 million, with apparently the promise of £300 million more. £15 million is being offered to join up two roads where there is currently congestion. But at present there is no agreed plan for where all the new housing is to go, with long-standing conflicts between Oxford City Council and the adjoining districts, who see themselves as largely rural. Local people are pressing for an Oxford Futures Commission to recommend how Central Oxfordshire could achieve smarter growth.[120]

By ensuring that the public sector captures the majority of the uplift in real land values that should follow on from relieving capacity constraints almost everyone should be satisfied. A **Local Investment Agreement** would signal what might also be called a 'quality deal'. Changes in the way public investment projects are approved while projects are being aligned should not cause any further delays – after all Crossrail took several decades to agree – as the funding sources will be much more predictable, and less subject to upsets from opponents. We could learn a great deal from how the French manage to achieve what we find almost impossible through local leadership.

120 *Oxford Futures: achieving smarter growth*, Oxford Civic Society 2014

One aspect of leadership is being able to explain both the costs and returns to a cynical and often hostile electorate. There is currently a major gap in both knowledge and understanding of the relationship between infrastructure investment, development and property values, which the new Corporation could readily fill though the interest it takes in major projects, as well as from research it might commission. There is a wealth of information available through the Valuation Office, and also through making use of Geographical Information Systems to supplement the existing Investment Plans that have already been drawn up in most local authorities. Extraordinarily the information series on Land Values was abandoned by the Coalition Government apparently to save £50,000!

We need to pool knowledge on both the costs of different forms of infrastructure and their impact, and to publish the outcomes. Huge amounts of research were commissioned by the Regional Development Agencies, for example into the best location for a new town in the East of England, much of which is still relevant, and which might be extracted from the archives. Commitments to related hard and soft infrastructure should be a precondition for making loans available, which would incentivise collaboration between the stakeholders in finalising spatial or territorial agreements, and not arguing for ever.

4.7 Funding soft infrastructure

Just as important to house values and demand is the quality of the local environment, and facilities such as schools, and places where people can meet each other. Much of the extra housing to be built will be in locations that are not currently preferred as places to live, in part because of understandable fears about children's prospects. Yet educational standards can be improved over time, as successes in Inner London illustrate. The key is often making it possible for upwardly mobile people to stay and invest in their communities and a good example is the decision to set up an Academy in New Islington in Manchester backed by Manchester Grammar. At present the excessive cost of housing forces such people to move further away, and to spend long hours (and money) commuting to work and taking their children to school.

By ensuring that the 'social capital' needed to build healthy communities is available from the start, for example by providing good schools and open spaces, the new community will develop much faster, which will in turn provide better financial returns for the investors. This principle is already well understood by some of the most successful house builders, such as the Berkeley Group.[121] Instead of complex and

121 Tim Dixon, *Creating Strong Communities*, Berkeley Group, 2014

inflexible agreements to compel private developers to step outside their comfort zones, or building soulless housing estates with few amenities, social infrastructure should be seen as essential as roads and utilities. This can most readily be achieved through projects led by charitable housing associations, as exemplified by innovative projects such as Lightmoor by the Bournville Village Trust or Derwenthorpe by the Joseph Rowntree Housing Trust.[122] It can also be achieved through asset based development trusts, as in the examples of Caterham Village or Grayling Park, both developed by Linden Homes, or Coin Street Community Builders in London.

The Corporation could provide a 'one stop shop' for community based trusts that are trying to develop social capital in both new and existing residential areas. In this way the number of successful community enterprises will grow rapidly. Funds would be made available to those that can produce the business plans to show how, with a package of grants and loans, investors who are willing to provide 'patient capital' can be repaid, and how the project will support local growth. Many of these projects are also like to apply innovative energy saving measures, and may well be tapping into low cost loans from the Green Investment Bank or European Investment Bank through appropriate intermediaries, such as the Low Carbon Hubs that have been set up in cities such as Manchester, Oxford and Bristol. In this way the examples set by advanced cities such as Freiburg, the so-called Solar Capital of Europe, can be transferred to the British situation, and we can start to rebuild our worn-out infrastructure through local initiatives.

4.8 Managing the common parts

The biggest criticisms that have been made of new housing schemes in the UK is not the houses themselves (though they are attacked for being much smaller than in the rest of Europe), but the public realm. Provision for parking has generally been inadequate, with cars parked all over the place as a result.[123] Walking and cycling are unpleasant if not dangerous. At the same time requirements that new developments hold rain water on site have led to expensive and sometimes unsatisfactory Sustainable Urban Drainage Schemes, while flooding is potentially a problem for many areas that have not been developed for housing in the past. Despite a wealth of good advice in the form of compendia and toolkits, a system based on house builders promoting development schemes does not seem to work very well, at least as far as larger communities are concerned.

However once a joint venture company or development corporation is in a position to

122 Michael Carley and Nicholas Falk, *How can local government build sustainable urban neighbourhoods*, JRF, 2012
123 *Space to Park*, URBED with Design for Homes, 2014

lay out a site, and install the basic services, a number of other possibilities are opened up. First an Energy Services Company (ESCO) can be set up, or even one providing a range of utilities, (MUSCO) and this can not only result in better looking developments but also ones that are cheaper to build and maintain. For example a common service duct can avoid the need to continually dig up the roads. Such a company could be owned by the new community, or the local authority, and provide an ongoing source of income to help maintain social and environmental services needed to maintain the neighbourhood in good health.

A second alternative is some form of development trust, and there are plenty of good examples in most parts of the country, the pioneer being Coin Street Community Builders on London's South Bank. There are also good examples of environmental conservation trusts taking on the open spaces, and maintaining them to high standards, as in Cambridge for example. The key in both options is to plan how the community is to be managed from the very start, and to provide the necessary funding and agreements, for example with regard to service charges and what they cover.[124] As innovative projects such as Vauban in Freiburg have demonstrated, a combination of financial incentives and good urban design will persuade people to give up having private cars, which in turn releases land for other and better uses than storing cars.

The Corporation should ensure that before making funds available for strategic developments, principles have been agreed for how the scheme is to be managed and maintained, and who will pay for way. This will avoid endless arguments over adopting roads, or making schools available for community use after hours, which lead to waste and conflict. An endowment in the form of some land or homes for rent or an interest in providing energy or running community transport can ensure that long-term stewardship is exercised without putting a further strain on overstretched local authorities.

In turn by enabling a mix or balance of people of all ages, incomes and social classes to achieve a better life together, some of the original aims of the first 'garden cities' can be achieved. In the process those with disposable wealth will have a much better choice of investments, and a major barrier to the growth of the British economy will be removed.

Conclusion

A BIB, with an arm modelled on the Dutch BNG Bank with the involvement of both central and local government, and focused on assisting housing delivery and local

124 *Managing Mixed Communities*, URBED and the University of Westminster for English Partnerships and the Housing Corporation , 2008, www.urbed.coop

infrastructure would be the single best way of planning for posterity not austerity. It will also go a long way to overcoming the banking failings that have brought so much discredit to the UK in recent years. In summary it would offer the following benefits:

1. taking a longer-term perspective, for example giving more weight to investments that reduce energy consumption and hence fuel bills (and carbon emissions) than a private investor would
2. de-risking complex projects, for example only lending money where local authorities are committed to allocating appropriate sites, and providing the necessary soft infrastructure, such as schools
3. distinguishing the good projects from the bad ones, and channelling more investment into locations where the conditions for long-term economic growth are right
4. mobilising private sector investment by demonstrating commitment and providing guidance on where development is to take place (and where it is not welcome)
5. crossing boundaries, for example by joining up public investments in local transport with related developments
6. encouraging collaboration between adjoining local authorities and utilities by supporting sound and agreed long-term local investment plans
7. avoiding political swings, and building the capacity to think and act for the longer term
8. and ultimately raising our levels of growth and wellbeing to those of comparable European cities.

No solution can be found to the persistent housing crisis without addressing the root causes. As KPMG recommend in theur comprehensive report for Shelter,[125] intervention in the land market is an essential first step. They propose designating New Homes Zones for special treatment, as well as new Garden Cities. They also back the idea of a National Housing Investment Bank on the Dutch model. Such proposals should win all party support.

Thomas Piketty's masterwork *Capital in the Twenty-First Century*[126] brings out the wider importance of the value of the housing stock to the wealth and wellbeing of any country. What reviews of the book may have missed is that the French have 50% more invested in infrastructure that the UK, which underlies the superior quality of

125 KPMG *Building the homes we need A programme for the 2015 government*, Shelter, 2014
126 Thomas Picketty, *Twenty-First Century*, Harvard University Press, 2014

life in most of their cities. By investing in building better neighbourhoods, we could not only rebalance our cities, but also achieve a fairer and less wasteful pattern of 'smarter growth' that would reduce regional inequalities and boost economic and social growth without 'costing the earth'.

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If you would like to know more about the Smith Institute please write to:

The Smith Institute
Somerset House
South Wing
Strand
London
WC2R 1LA

Telephone +44 (0)20 7845 5845
Email info@smith-institute.org.uk
Website www.smith-institute.org.uk

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