Starting small to build more homes

A blueprint for better policymaking in the property SME market

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1. Foreword from Christian Faes

Co-Founder and CEO of LendInvest

There is public and political consensus that too few homes are being built in the UK. Successive governments have set housebuilding targets that they've failed to meet, while market share in the housebuilding sector has become too concentrated to a small group of dominant companies. Another generation of property SMEs risks disappearing from the sector as market conditions constrain their ambitions to scale up.

Small and medium sized property professionals are essential for a healthy housing market but have been in sustained decline for decades, meeting a tax and regulatory framework that distorts the market in favour of the larger housebuilders and an increasingly constrained funding environment.

The impact on communities is obvious: an undersupply of homes inflates house prices and exacerbates the gap between property owners and those who cannot find an affordable place to rent or buy.

This government has set itself the task of fixing the broken housing market with a promise to help SMEs grow. In order to deliver on this pledge, the essential role of SME property professionals investing in, building and refurbishing homes must be recognised. Government policy must support the growth of these businesses, just as it does of companies in other sectors – using tax breaks, intervention to increase competition, the dissemination of public capital through the likes of the British Business Bank and Homes and Communities Agency, as well as getting behind initiatives to arm these postcode entrepreneurs with the skills they need.

If we are to encourage new entrants to the property market, they need to know that their businesses will be treated the same as start-ups and scale-ups in other productive sectors. It is detrimental that renting premises to open a coffee shop is more attractive to the would-be business owner, than it is to build the mixed-use space in which the coffee shop will be located. Successive governments have prioritised incentives to encourage enterprise and entrepreneurialism across many sectors from retail and leisure to engineering and manufacturing. Somewhere, small property businesses have suffered, facing tougher regulation, taxation and finance issues in place of support.

The government has laid out its plans to support SMEs in its housing white paper, setting the foundations that must be built upon during this parliament to make room for SMEs to flourish across the country. Realising these ambitions will rely on an ongoing collaboration between local and national policymakers, and businesses with a stake in the development of new homes, be they builders and refurbishers, industry bodies or lenders like LendInvest. Only by advancing together to incentivise active and productive new entrants can we reconstruct the failing housing market and deliver more homes of every type.

Christian Faes
Co-Founder & Chief Executive Officer

2. Introduction

The UK is home to hundreds of thousands of small businesses. Since the financial crisis of 2008, successive governments have developed policy to help SMEs to flourish and their economic and social benefits have been celebrated.

Policies to support entrepreneurialism and the growth of SMEs have contributed towards an acceleration of start-up creation, most notably in financial services, clean energy and technology; year-on-year, the number of new business births increases, nurtured by government incentives.

Overlooked, however, are the UK's property SMEs. These are the individual, small scale landlords, investors and developers who let, renovate or build property, supplying the private rented sector (PRS) and the homebuyers' market with urgently needed housing stock. Their numbers are not insubstantial.

Four in five UK adults aspire to own a home in the next 10 years[1]; yet the country is suffering an extreme deficit of houses for its residents, let alone for them to own. Added to this, house prices in some of the most densely populated urban areas have risen to levels that put home ownership beyond the reach of many.

As owner-occupied tenure fell by roughly 185,000 between 2010 and 2014, the private rented stock grew by 675,000 units. Today, the PRS accounts for nearly 20% of all homes[2] across the UK, totalling 5.4 million dwellings. This demand for the private rented sector is not going away either: an additional 1.8 million households will be looking to rent by 2025[3].

Yet, despite constituting a crucial component of the housing sector at a critical time, these small-scale businesses are not benefitting like their counterparts in other industries from the regulatory and tax ecosystem designed to incentivise the pursuit of new UK enterprise.

There is some government support: Housing Minister Gavin Barwell acknowledges that the UK needs more homes of every type. Equally the Government concedes that it is failing to meet its own housing targets that grow every year. Last year the House of Lords Economic Affairs Committee urged government to build 300,000[4] new homes every year for the foreseeable future to address the lack of housing and expanding population.

The government's housing white paper promised to help property SMEs grow again[4], but this will require them to go further than planning reform and shifting the onus onto local authorities to free up land, as announced in the paper. It will also mean taking bolder action than funnelling money to the Homes and Communities Agency (to become Homes England).

The number of small housebuilders is in continued decline, leaving the sector's output to a small number of larger companies. Where small housebuilders were responsible for 3 in 8 of the UK's new homes before 1990, they now only deliver 1 in 8 of the new homes built today. Equally as concerning is the lacking growth in the number of medium sized housebuilders. There are five times fewer SMEs now than there were in the 1980s, demonstrating a concentration of growth only at the large end of the market[6].

This rhetoric sits uncomfortably with the measures taken to curtail and reduce the population of property SMEs since 2015. The pace at which policy has been enforced to dissuade property professionals from entering or continuing in business is matched almost by the pace of policy development to encourage institutional backing of the Private Rented Sector in place of individual owners and changes to the planning and tax system that can only be weathered by the largest housebuilders.

This report seeks to further public and political understanding of what a property SME is, does and contributes socially and economically for the benefit of UK citizens, as well as identify where government could take direct action to increase the output of SME property companies.

[1] CML Press Release, October 2016
[2] Understanding the Role of Private Renting, University of Cambridge, 2016
[3] UK housing market outlook: the continuing rise of Generation Rent, PwC, 2015
[4] House of Lords Economic Affairs Committee: Building More Homes, 2016
[5] Fixing our broken housing market, Department for Communities and Local Government, 2017
[6] Reversing the decline of small housebuilders: Reinvigorating entrepreneurialism and building more homes, Home Builders Federation January 2017

3. Profiling property SMEs

We identify three types of property SMEs at work in Britain:

3.1 The SME developer: These are the small builders, developing 100 units or fewer per year on brownfield or greenfield sites. These homes may be for sale to homebuyers or buy-to-let landlords. Often they have transitioned from other professions, having spotted an opportunity to pursue self-employment in the property development market. Their numbers have been in decline for many years, correlating with the slowing delivery of new homes in the UK[7].

3.2 Small scale landlords: Making up the majority of the housing stock in the PRS, landlords diversify the tenure options in the housing market[8] for those for whom owning their own home is unaffordable or undesirable. HMRC's most recent figures report there are 1.75 million landlords operating in the UK. The small scale landlord draws his or her income primarily from their property portfolio. Their number of properties typically fluctuates as these professional landlords regularly buy and sell properties to maximise the value of their portfolio.

3.3 The property regenerator: These property investors renovate, refurbish and improve old, outdated and uninhabitable properties for resale. These could be old residential dwellings or the conversion of commercial space to homes. By bringing such properties that would struggle to secure mortgages by non-professional buyers back into the market, these investors are helping to maintain market liquidity and increase the stock of homes available across the UK.

[7] Federation of Master Builders House Builders' Survey 2016, Federation of Master Builders, September 2016
[8] Understanding the Role of Private Renting, University of Cambridge, 2016

4. Headwinds facing property professionals

Despite their role in creating and sustaining critical infrastructure in the UK, property SMEs have been subject to a number of challenges that threaten the viability of their profession.

4.1 Dominance of the large housebuilders

Output in the homebuilding market is controlled by an increasingly concentrated number of large firms in the UK. A recent House of Lords Economic Affairs Committee report highlighted the inequality of opportunity in the homebuilding market:

> *"The market has oligopolistic characteristics: the eight largest builders build more than 50 per cent of new homes and smaller builders find it difficult to operate."* [9]
>
> *House of Lords Select Committee on Economic Affairs*

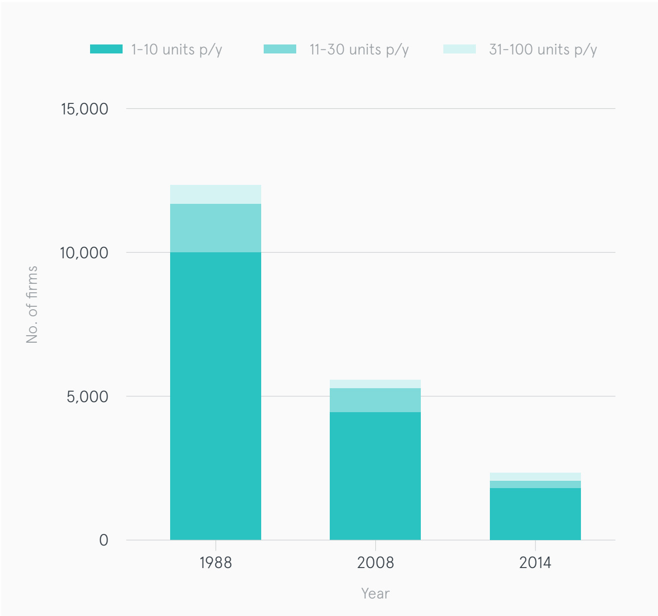
This has not always been the case. It is widely recognised that a period of post-war productivity in homebuilding correlated with plurality in the industry, or more specifically, when small homebuilders contributed a greater proportion of the housing stock across the nation.

In the thirty years between 1960 and 1990, entrepreneurship in the homebuilding industry was common. SME property businesses grew at pace, some of which scaled to dominate the market as today's largest housebuilders. Indeed, three of the five largest housebuilders today were founded between 1960 and 1990, the other two operating since the 1940s.

Back in 1988, the number of small builders stood at 12,200 in the UK. That had fallen to 5,700 by 2006, and then just 2,400 by 2014, an 80% slump (see table, right).

With no single one of the top ten homebuilders today having been created after 1990, it is clear that SMEs have struggled to find their place in a market dominated by long-incumbent giants. This has been to the detriment of industry productivity, the government's ability to meet its targets, and the public's demand for homes, which has not dissipated.

Whereas the 1980s proved a decade of growth for SMEs, new entrants in recent years have struggled to scale. Matching the decline of the small-scale housebuilder, mid-size firms (building 101-2000 units per year) have failed to sustain themselves; today there are less of these businesses than in the 1980s.



Number of firms registering low volumes of housebuilding, 1988 to 2014[10]

The impact

Squeezing smaller housebuilders out of the market will result in an increasing affordability gap as larger housebuilders build the homes that deliver best value for shareholders at the expense of prospective homebuyers.

Fewer houses are being built than are required by the nation. Large housebuilders are not developing land fast enough, bottlenecking the supply of homes.

[9] Building More Homes, House of Lords Select Committee on Economic Affairs, July 2016
[10] FMB Written evidence (EHM0140), Federation of Master Builders, 2015

4.2 Regulatory and bureaucratic burden

SMEs in the property market, whether building homes or investing in them for rental or resale, operate today in an increasingly complicated business environment. Weighed down by bureaucracy and comparatively burdensome regulation, it is a difficult endeavour for SMEs to establish themselves in the market, let alone sustain a growing business.

> *"The housebuilding industry is not an easy professional endeavour"*
>
> *John Slaughter, Director of External Affairs, Home Builders Federation*

Small developers, regenerators and landlords are frequently blockaded by complex and cumbersome tax structures, difficulty in obtaining finance for their projects and constrained access to land, which is often controlled by the larger developers.

A common constraint for SMEs is the availability of and access to land for development or investment. The planning system is described by the Home Builders Federation as "working inherently against the SME"[11], with larger players able to invest in the resources to navigate and overcome hurdles arising from planning requirements.

The appetite of lenders to provide finance to SMEs is another challenge; banks and building societies were once the mainstay of housebuilding finance[12], but their share of the market has shrunk by more than 20% since 2008. For many, capital adequacy requirements mean that development finance is just too expensive to lend. For others, there is little appetite to lend capital in return for ultra slim margins.

These obstructive hurdles contribute towards an increasingly unpleasant environment in which to work and compound to disincentivise SMEs. Whether property SMEs are building, renting or selling, a selection of common regulatory hurdles and onerous bureaucracies increase the cost of business for SMEs:

- **Stamp Duty Land Tax surcharge:** On purchases of rental properties and second homes, an additional 3% rate of stamp duty was imposed from April 2016.
- **No allowance for property value depreciation:** The tax system treats income for landlords as if they were invested in a perpetual asset, without any type of depreciation allowance.

For property businesses that have not incorporated, the tax system is even more punishing:

- **Retention of capital gains tax rates:** For gains accruing from April 2016, 18% and 28% of the basic and higher rates respectively will be retained for properties that are not primary residences. This is not the case in other industries where capital gains tax was reduced to 8% and 18% respectively
- **Changes to mortgage interest tax relief:** Investors' ability to deduct interest paid on buy-to-let mortgages from taxable income has been removed. This will instead be replaced with a flat tax credit of 20% of interest paid, phased from April 2017 and will affect the smallest property businesses.
- **Letting agents' fees scrapped:** The 2016 Autumn Statement abolished letting agents' fees to tenants in a move to increase the affordability of renting. Some costs in the lettings process are essential and may be passed onto the landlord.

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[11] Reversing the decline of small housebuilders: Reinvigorating entrepreneurialism and building more homes, Home Builders Federation January 2017

[12] UK Development Finance Review, Investment Property Forum, 2015

The impact

- Property SMEs face increasingly difficult pressures in getting their businesses off the ground and in pushing for growth. They are left at a disadvantage to the larger housebuilders, whose sheer scale and resource reduce the risk and cost of business.

- The tax position of property SMEs is poor and anti-competitive, particularly when compared to larger property organisations. Sole traders are hit by disproportionate taxation on their investments and SMEs face expensive duties that can hold back cashflow and future investment.

- SMEs are increasingly restricted in their options for finance. As mainstream lenders retreat from providing finance to these businesses, a further generation of property SMEs could risk being lost.

- Industry groups and think tanks warn against punitive taxes for the BTL sector and their effects on the market:

  – The Council of Mortgage Lenders said "there is a risk of overkill in dampening investor sentiment to the extent that the flow of available private rented property could be disrupted."[13]

  – The Institute for Fiscal Studies has said that "properties will be worth less because potential landlords and potential homeowners won't be willing to pay as much for them". As a result, there will be "less incentive to develop property."[14]

4.3 Political preference for institutional investment in the private rented sector

In a 2012 review of the barriers to institutional investment in private rented homes, the Coalition government outlined its intention to support more institutional funds to enter the private rented sector[15]. This orientation of public policy was not new and still persists, the political consensus being that operating standards are higher among institutional investors and they present a lower risk to the housing economy.

A number of distinct policies have emerged, designed to institutionalise the market:

- **Business Expansion Scheme (1988-1993):** This tax advantage incentivised investment into higher risk business start-ups, including to companies offering assured tenancies. This policy lasted until 1993 and added approximately 80,000 new homes to the PRS.

- **Housing Investment Trust Scheme (1996):** Designed to introduce pension funds into the PRS, this policy was not successful. No HITs had been initiated by 2010.

- **UK Real Estate Investment Trusts (2005):** Based on a similar scheme in the US, this legislation extended the availability of liquid and publicly available property investment schemes to a wider range of investors with a view to enhance institutional investment in commercial and private rental real estate.

While there is clearly a role for larger investments in the PRS by institutions, SME landlords play an important role in the market. SMEs consistently deliver affordable tenure in the places where supply is most needed, not necessarily where a development best satisfies planning requirements or is politically palatable. This flexibility and versatility is essential in delivering the homes communities need.

The impact

If government policy continues to prioritise large scale institutional investment in the PRS, the fundamentally important role of small businesses will be disincentivised.

[13] CML press release, January 2016
[14] Buy-to-let stampede ahead of stamp duty hikes, The Telegraph, 2015
[15] Understanding the Role of Private Renting, University of Cambridge, 2016

4.4 A problem of perception

4.4.1 The "unscrupulous" landlord

One of the most positive initiatives to stem from the Housing Act of 2004 was the introduction of housing fitness standards. Government initiatives since further focus on applying professional standards across the sector to weed out exploitative landlords offering sub-standard accommodation. Indeed, industry recognises that professionalisation in the market is a positive development.

Such moves are welcome interventions to the relatively young buy-to-let market whose status as a professional, industry is only 20 years old. The standards have not had, however, the effect of sufficiently improving the public opinion of the professional landlords investing in the private rented sector. The reputation of landlords as amateur or rogue outfits who are unprofessional and exploitative of their tenants is a lasting one, and is often too liberally applied to sector as a whole, the vast majority of which are property professionals who have excellent relationships with their tenants and uphold good levels of maintenance and service.

4.4.2 Buy-to-let's effect on rising house prices

The buy-to-let sector has proved a continually popular investment opportunity since its introduction in 1996, raising a number of concerns by public officials about the impact of private rentals by small scale landlords. A Council of Mortgage Lenders report recently noted concerns raised by a number of public officials and government representatives that investors in the buy-to-let sector may be having a crowding effect in the sector, buying up properties that would have gone to residential buyers, and worse, driving up the prices of homes as they pursue financial gain in a market dealing with fundamental infrastructure. The CML has suggested that the validity of these claims are overstated[16]. It should also be expected that the professionalisation of the sector will minimise the prevalence of irresponsible property businesses seeking to make a swift income.

4.4.3 The pursuit of home ownership

For decades, politicians have championed the pursuit of home ownership; successive governments have designed their own versions of policy to promote and sustain a change in tenure structure, striking away from the social rental housing system that dominated the immediate post-war period.

The UK's aspiration to own is clear. 80% of adults in the UK would like to own their own home in ten years' time[17]. This ambition is part of the British psyche that distinguishes us from many other European countries, such as Germany and France, where rental housing accounts for a higher proportion of all residents' tenure choices throughout their lives.

Valuable though these ambitions are, they are out of sync with the reality of the housing market. Rising house prices, a low inflation environment and a shortage of housing are making home ownership less attainable than ever. As a consequence, more and more property SMEs orienting their business towards the rental market, where demand is growing.

Yet still, taxation policy is crafted to incentivise homeownership over renting. This fiscal favouritism extends to the selling off of public sector housing at a discount to homebuyers and preferential tax for owner-occupation. These structural biases within the tax system do not account for the changing needs of the population.

The impact

- Continued negative attitudes towards the rental sector may influence investment decisions, with property SMEs unwilling to undertake ventures that carry reputational risk. Ultimately this could limit the number of homes available in the PRS and new homes built for help-to-buy or first time buyers.
- Policy choices are geared towards home ownership through ideology, rather than economic rationalism. The risk of this is that homes of the wrong type are prioritised for development.

[16] The Profile of UK Private Landlords, CML, 2016
[17] CML Press Release, October 2016

5. A mismatch in SME growth policy

Prime Minister Theresa May has praised the "entrepreneurial spirit of the UK", lauding the role of the size and dynamism of the nation's world-leading start-up community. Most recent figures show that the UK is home to 4.5 million self employed individuals and the country saw the birth of 383,000 new businesses in 2016 alone.[18]

Regimes to encourage and nurture SMEs proliferated in the years after the 2008 financial crash, in response to a need to support jobs growth and the country's small and medium-sized enterprises - the backbone of the recuperating economy. These measures were designed to sweep away restrictive regulation, drive down the cost of business and ultimately inspire more investment in starting and growing small businesses and have supported SMEs in three areas:

Supporting SMEs to access finance to grow

- **British Business Bank:** founded in 2012 to improve access to finance for British SMEs by government, the state-backed bank supplies SMEs with credit and business advice. As of December 2016, the BBB supported over £3bn of finance to SMEs.
- **European Investment Group:** the total investment of the EIB Group (the European Investment Bank and the European Investment Fund) in the UK in 2016 was EUR 8.1 billion.

Incentivising investment through tax breaks

- **Enterprise Investment Scheme / Seed Enterprise Investment Scheme:** these tax incentives have delivered £15bn in equity finance to over 27,000 start-ups and SMEs.
- **Enterprise Zones:** these geographically defined localities designate areas of targeted growth, supported by tax incentives, which in some cases can discount business rates up to 100%.

Delivering regulatory innovation to overcome barriers

- **Regulatory sandbox:** the Financial Conduct Authority has encouraged financial services entrepreneurs to participate in its programme to support the evolution of regulation that keeps apace with innovation.
- **Enterprise Zones:** These zones can also support businesses to overcome local barriers, through simplified local planning requirements, for example.

While various frameworks have been developed to support small businesses to grow, the UK government has not backed SME property professionals building, refurbishing and leasing property to the same extent.

- Property has not been an area of interest to the British Business Bank to-date, nor does it feature in the British Business Bank's five chief investment sectors, as outlined in its 2015 performance highlights.[19] Yet, the British Business Bank's report, Small Business Finance Markets 2016/17, recognises the difficulty housebuilding SMEs have in accessing finance.[20]
- Investors in small property businesses are not eligible for equivalent tax treatment to the EIS/SEIS programmes.
- Where Enterprise Zones have been designated to encourage the establishment and growth of businesses, similar regimes have not been replicated for areas most undersupplied with homes.
- Innovations in homebuilding such as modular construction would benefit from a regulatory initiative similar to the Regulatory Sandbox to explore new innovative methods and their relationship with regulation.

It is clear that as policy development to support SMEs to grow in other industries continues, the same cannot be said for small scale property businesses. For these individuals and small businesses, the overall tax and regulatory environment is more obstructive than conducive.

[18] Business Statistics, House of Commons Library, 2016
[19] British Business Bank Performance Highlights, 2015
[20] Small Business Finance Markets 2016/17, British Business Bank, 2017

6. A case study: disparity in cost and opportunity between SMEs

The case study shown below demonstrates the very different positions for two UK small business owners with regard to getting a project off the ground.

Situation: A small developer purchases an old semi-commercial unit in a degenerated area of a town centre. The building has been vacant for some time and the developer obtains planning permission to refurbish it and establish a commercial space on the ground floor and two small flats on the first floor. The developer plans to sell the flats, and hold and lease the commercial space to a first-time coffee shop owner.

Property SME

Getting started

- Redevelopment costs for a project are likely to exceed £500,000, including the purchase of the property, planning and labour costs.
- Finance opportunities are constrained:

  - the developer is not able to find financing through mainstream lenders.

  - to-date, developers have not had the same access to finance from the British Business Bank or European Investment Group as other small businesses.
- The developer has to navigate the planning process to acquire permissions for proposed structural changes and change of use.

Impact

- The developer generates work for a number of local workers, including a team of construction workers, planners, legal consultants and contractors to name a few. In any case, work is generated for over 15 individuals.
- Development of the unit adds residential housing stock to the private rented sector.
- The economic contribution made by the developer is significant. Property taxation is high. Those doing business in the property sector pay more in tax than other businesses because of stamp duty costs and capital gains rules on top of their corporation tax bill.

State support

- Some SMEs are eligible to apply for the government-administered £3bn Home Building Fund. This particular case is not eligible as it is a two-unit development (the minimum is five).

Retail SME

Getting started

• The average start-up cafe needs £50,000 to get off the ground.[21]

• Financing opportunities are many:

- mainstream lenders offer a number of business loan products.

- the business can apply for finance from the British Business Bank or may be eligible for European finance from the European Investment Group.

- equity crowdfunding exists as a less traditional finance route.

- start-ups can receive investment from private investors that are granted significant tax benefits for investing, such as the Seed EIS and EIS schemes. These schemes make this funding a very real prospect for start-ups.

Impact

- The cafe, depending on size, will create jobs for a handful of people.
- Cafes are known to increase footfall and encourage the presence of other retailers in their local areas.

State support

- State backed funding options such as the BBB and access to European Investment Group funds.
- Business investors may be eligible for SEIS/EIS relief on tax.
- The coffee shop may be able to claim business rates relief.
- The business may benefit from discounted business rates if it falls within a designated Enterprise Zone.

[21] How to start a coffee shop, Limini Coffee, Accessed January 2017

Simply put, disparity exists in the opportunity to build and sustain property businesses in the UK. Beset by challenges in regulation, tax treatment and access to start-up capital, property SMEs are not given the same support as other businesses to grow, despite the nation's need for increased home supply.

The economic and social benefits of new enterprise in all sectors are significant, yet getting businesses off the ground can be a challenge. State-backed SME funding schemes have been formed as a policy response to the financial crisis, supporting the growth of flourishing industries across the UK. The impact of these initiatives on investment in property business has been limited, an area remains an underserved industry by public financing, or in the supply of capital from mainstream lenders.

Small property firms must also navigate a more onerous regulatory framework than companies in other sectors. Where larger firms are better resourced to overcome regulatory challenges, knockbacks as a result of the planning system and other regulations can mean the success or failure of projects and directly affect the pace at which the company grows.

The UK has the highest property taxes in the developed world.[22] As a result, property is an expensive business investment and smaller businesses can be priced out as they struggle to operate on margins squeezed by various taxes. While taxes have been simplified and discounted for SMEs across other sectors, the same cannot be said for SME property companies.

[22] OECD Revenue Statistics - United Kingdom, OECD, 2016

7. The real contribution of property SMEs

A study conducted by the Home Builders Federation[23] showed that post-war housing supply peaked at the same time that entrepreneurial property companies were flourishing. If we were to return to the same level of market plurality as in 2007 even, we could build 25,000 more homes every year.

7.1 Supplying the homes that communities need

The housebuilding sector is dominated by a concentrated number of larger housebuilders who do not build the homes that the nation needs, but rather, those that are more profitable for their shareholders. The Centre for Policy Studies says that this clutch of major firms "tend to build what they believe people will accept".[24]

7.1.1 Putting old homes back into the system

Property renovators and refurbishers regularly take uninhabitable properties, that are unlikely to be approved for mainstream mortgages to homebuyers, and invest in their restoration, often adding kitchens, bathrooms or central heating. They either go on to sell the regenerated property to homebuyers or investors, or refinance to add it into the rental system.

7.1.2 Converting old commercial units into homes

As demand for homes in inner city and urban neighbourhoods increases, property entrepreneurs are unlocking housing opportunities by investing in property previously used for commercial and retail purposes. Converting shops and office blocks into apartments and houses contributes towards the improvement of communities and rejuvenation of existing infrastructure.

7.1.3 Creating new homes from the ground up

The 80% slump in SME housebuilders since 1988 has been to the detriment of both the industry and the nation at large. Despite this drop in number, small scale builders continue to deliver growth in the UK's regional economies, often developing land more swiftly than their larger competitors.

Many developers, both large and small, struggle to obtain finance for their development projects, unless they can demonstrate a number of pre-sales. Property investors make up a significant proportion of this, buying speculative projects and providing the security for the project to go ahead. Changes to taxation rules for the property investors could destabilise this process, with investors unable or unwilling to make financial commitments of this kind. Without their investment, the buildings won't go up.

7.1.4 Challenging convention and pushing forward innovation

> *"We simply need to build more homes...It means encouraging new technologies that will help us to get more houses built faster"*
>
> *Rt Hon Theresa May, Prime Minister[25]*

Pre-made, factory-built homes known as modular housing are fast gaining favour with the UK government, garnering praise from the Prime Minister at her first party conference.

It is the small-scale property developers who are leading in this innovation, experimenting with modular technology for residential property and constructing homes 30% faster

[23] Reversing the decline of small housebuilders: Reinvigorating entrepreneurialism and building more homes, Home Builders Federation, January 2017
[24] Housing: now is the time to seize the opportunity, Centre for Policy Studies, January 2017
[25] Prime Minister: The good that Government can do, Conservative Campaign Headquarters, 2016

than traditional methods. Property developers such as Pocket Living and Urban Splash are delivering on modular projects across the UK, setting the standard for off-site built property construction that can be cost-effective; providing efficient solutions for social housing; and catching us up with European countries where modular building is an increasingly commonplace solution for high demand urban areas.

Similarly, the proliferation of development of houses in multiple occupation, especially in inner city areas is increasing the availability of affordable tenure for students and young professionals.

7.1.5 Contributing to local economies

Entrepreneurial property SMEs are all around us. These businesses do not cluster in designated hubs, but instead contribute to every postcode or constituency around the country.

Most private landlords and developers own or build property in their local or neighbouring areas. They are delivering housing in their regional communities as affordability for home-ownership and the availability of social rental tenure drops.[26]

Their economic contribution is not limited to locally retained tax receipts or the availability of housing, but also in creating employment for the range of industry players: for instance, property professionals including planners, surveyors, project managers and solicitors, as well as construction workers and building material suppliers. In 2016, LendInvest's development finance borrowers alone borrowed in excess of £50 million and created employment for approximately 750 local people.

Small developers also deliver greater diversity in the types and styles of builds, which could be attractive for town planning, especially when breaking up larger sites. SMEs can create the garden towns designed for living and working and can support a more organic growth of communities, allaying the fears of opponents to new development.

7.1.6 Employing and upskilling young talent

The Home Builders Federation has noted the crucial role that small scale housebuilders play in upskilling workers in the construction industry, providing a training environment for young trainees. Plurality in the housebuilding sector is essential in challenging the skills gap in the construction sector.

7.2 Providing flexible tenure choice

The demand for private renting is increasing as UK socio-demographic trends change.[27] A report by Rugg and Rhodes (2008)[28] identified the most important factors generating the demand for private renting. They were:

- growing student numbers;
- increased inward migration;
- higher levels of relationship breakdown;
- increased demand that would otherwise have been catered for in the social rented sector;
- growth in the numbers of younger tenants renting for 'lifestyle' reasons; and
- worsening affordability problems for those wanting to access home ownership.

CML predicts that by 2025, 1.8 million more households will be looking to rent, rather than buy. SMEs delivering new rental tenure need to be supported to meet this demand.

[26] The Profile of UK Private Landlords, CML, 2016
[27] Understanding the Role of Private Renting, University of Cambridge, 2016
[28] The Private Rented Sector: Its Role and Potential, University of York, 2008

8. A blueprint for government to support property SMEs

A whole-of-market approach by government to address the housing crisis should consider the following interventions:

- **Priority sale of public land to SMEs:** Government should introduce apportion a quota of public land for sale only to SMEs to get land into the hands of the property businesses most incentivised to develop housing swiftly.

- **Reform of the property tax environment to support growth of SMEs:** Simplification of the the property tax environment and a review of its stifling impact on SMEs should be considered in a review immediately. Reducing the tax burden on property SMEs will remove barriers to growth as they are able to reinvest capital back into development. Possible measures for consideration include:

  - Cutting the stamp duty bill for downsizers, or those bringing disused or uninhabitable property back into the housing system.

  - Reviewing incentives for investment in property, for example capital gains rules.

- **Investment in access to finance for SMEs:** State-backed finance programmes must increasingly provide capital to upstarting property businesses. Vehicles like the British Business Bank and the Homes and Communities Agency are appropriate, but action must be taken to ensure that their intervention addresses the needs of SMEs:

  - The British Business Bank should apportion funding specifically for property development.

  - The £3bn of finance for housebuilding designated by government to the Homes and Communities Agency (HCA) is a welcome recognition that public finance must back SME developers. However, the Home Building Fund must administer £55.6m a month to SMEs if it is to meet its target of 25,000 homes by 2021. To-date, the HCA has committed over £500m of funding but will need to act on recommendations of the Tailored Review and consider working with intermediaries to ensure that committed finance is put in the hands of SME housebuilders without delay.[29]

  - The HCA should promote new entrants to the property development market by revising down delivery criteria for the Home Building Fund. Currently, developers must build a minimum of five units per project in order to qualify for funding, but many SME property businesses begin by developing smaller units before scaling up.

- **Introduce a house building competition strategy:** Addressing the clutch of dominant housebuilders will require impetus from government to increase competition in the sector. This could be achieved by a joint strategy by the Small Business Minister and Housing Minister to support the professionalisation of SMEs.

- **Promote industry skills initiatives:** Arming aspiring property professionals with the tools to get their projects off the ground is a priority for many in the industry. Government should promote skills initiatives in the sector to increase the number of new entrants and drive public awareness of the valuable contribution these small businesses make to communities.

[29] Tailored Review of the Homes and Communities Agency, Department for Communities and Local Government, November 2016

9. Conclusion

More than ever, the nation needs SME housebuilders, property regenerators and landlords in every community investing time, capital and expertise in the generation of affordable housing stock.

Should conditions remain as they currently are for property SMEs, the UK risks losing another generation of enterprising investors. What has been an attractive and honest means of self-employment stands to become financially inviable, at the same time that entrepreneurship is celebrated and supported in other sectors.

The onward impact on local economies could be enormous. Fewer houses coming into circulation to buy or rent will starve communities of space and mobility; run-down properties will remain eyesores in neighbourhoods; and fewer members of the construction industry will be contracted to work on or supply services to small-scale local projects.

Punitive taxes and fiscal favouritism for other tenure options is undermining the position of these property investors, despite their ubiquity across the nation. The UK simply cannot afford to lose these postcode entrepreneurs, whose presence extends to every part of the country but could be reduced if they continue to lack similar support to that given to SMEs in other sectors.

This urgency must be addressed as the UK pursues its first industrial strategy in a generation and combats the worst housing crisis in half a century. As government pursues an ambitious agenda to increase capacity in housing supply, the contribution of all industry members should be explored and policymakers must challenge the barriers locking property SMEs out of the market.

As industry, policymakers and the public coalesce in their appetite for bold solutions to the housing crisis, safeguarding the continued and consistent contribution of small-scale property businesses could not be more valuable.

10. Acknowledgements

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