National Audit Office

Report
by the Comptroller
and Auditor General

Department for Communities and Local Government

The Help to Buy equity loan scheme

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Key facts

12,875
households helped into home ownership by Help to Buy equity loans in the first nine months

9,600
further households approved in principle and waiting to complete their purchases

£518m
in equity loans made in the first nine months

£40,200	average equity loan against an average property price of £201,800
£8.3 million	fees paid to Help to Buy agents
£44,700	average household income of buyers using Help to Buy
1:3.4	average income-to-mortgage ratio, excluding the equity loan
1:4.4	average income-to-housing debt ratio, including the equity loan
89 per cent	percentage of completed sales that are to first-time buyers

Summary

The Help to Buy equity loan scheme

1 The Department for Communities and Local Government (the Department) published its housing strategy, *Laying the Foundations*, in November 2011.[1] In it, the government set out what it sees as the three main barriers to home ownership:

- Potential home owners cannot afford mortgage finance.
- Lenders restrict access to mortgages to buyers with big deposits.
- Developers do not build enough new homes, partly because potential buyers cannot raise a mortgage.

2 The government announced the Help to Buy scheme (the scheme) on 20 March 2013 as one of several measures to address these barriers and support the housing market. It opened the scheme to the public 12 days later, on 1 April 2013. The scheme's objectives are to turn the desire for home ownership into demand for new homes, by improving the affordability of, and access to, mortgage finance and to encourage developers to build more new homes.

3 The Department has allocated £3.7 billion to the scheme and expects to make equity loans to 74,000 households across the three years 2013-14 to 2015-16.[2] This scheme is much larger than the Department's previous home ownership support initiatives.

4 Under the scheme, the government offers buyers of newly built homes an equity loan of up to 20 per cent of the purchase price. This supplements the buyers' own deposit, which mortgage lenders normally require to be at least 5 per cent. Borrowers then raise a repayment mortgage of, typically, 75 per cent of the property's value. Mortgages that are 75 per cent or less of a property's value often have a lower interest rate and so are more affordable. To help manage the risks of negative equity and defaults, mortgage lenders limit the number of higher loan-to-property-value mortgages they make.

1 Department for Communities and Local Government, *Laying the Foundations*, November 2011, available at: www.gov.uk/government/uploads/system/uploads/attachment_data/file/7532/2033676.pdf

2 £3.5 billion was announced in the Budget and £240 million had been allocated to Firstbuy and was rolled over to the Help to Buy equity loan scheme.

5 The value of the loan at any point in time is based on a percentage of the property's value. This means that if the property's value increases, the value of the government's equity loan will also increase in proportion. It also means if their home's value rises, the buyer will have to pay back more, in cash terms, than they borrowed. For example, if when a buyer sells their home or wishes to repay part of the loan, the value has increased by 10 per cent compared to when they bought it, they will owe the government 10 per cent more, in cash terms. The reverse is also true. Participants may repay part, or all, of the equity loan at any time during their mortgage and must pay the government back after 25 years, or when the mortgage is paid back, for example if the home is sold.

6 The 20 per cent equity loan is interest-free for five years. From the start of the sixth year, borrowers pay a fee of 1.75 per cent on the outstanding loan, increasing 1 per cent above the Retail Prices Index each year. Payments of this fee do not repay the equity loan capital.

7 Homes bought through the scheme must be newly built and have a purchase price of £600,000 or less. Unlike previous government schemes, such as FirstBuy and developers' own schemes, developers do not make any equity contribution and there is no household income limit for buyers taking part in the scheme.

8 The Department provides the finance for the scheme. The Homes and Communities Agency (the Agency) administers the scheme through its network of 13 Help to Buy agents (Figure 4).

Scope of our report

9 We examine the Department's and the Agency's performance in designing and implementing the scheme to improve affordability and accessibility of homes and stimulate new housing supply. We consider whether:

- the Department used evidence and expertise to design a scheme that will seek to maximise outcomes and minimise costs and risks to the taxpayer;
- the Department and Agency are implementing the scheme effectively and efficiently; and
- the scheme increases home ownership for eligible buyers, improves affordability and accessibility of mortgage finance and increases housing supply.

We show how we assessed value for money in Appendix One and the evidence we have used to reach our conclusions in Appendix Two.

10 We do not examine the separate Help to Buy mortgage guarantee scheme in this report.

Key findings

How well the scheme has been designed and implemented

11 **The scheme's size and design matches the Department's intention to make a substantial impact on the housing market.** The Department wanted to maximise the potential demand for the scheme to create the biggest impact possible. For this reason it set a maximum budget of £3.7 billion, much larger than previous shared equity schemes. For example, its immediate predecessor, FirstBuy, had a budget of £250 million. The Department estimates that the £3.7 billion could support 74,000 home purchases from 2013-14 to 2015-16, but how long the money lasts will depend on how many people take up the funding and how much each buyer takes. The Department chose not to target the scheme, as it had with previous equity loan initiatives, on any particular type of buyer. It also put a relatively high cap on property prices at £600,000. Around 96 per cent of all newly built properties sold between April and December 2013 cost £600,000 or less (paragraphs 1.4 to 1.5 and Figure 2).[3]

12 **Early demand for the scheme has been strong.** Some 12,875 buyers completed purchases through the scheme in its first nine months (April to December 2013). The Department made equity loans of £518 million on these purchases. At the end of December 2013, around a further 9,600 completions were in the pipeline (paragraph 2.1 and Figure 5).

13 **The Department's and the Agency's pragmatic approach got the scheme up and running quickly.** The Department introduced the scheme quickly to take advantage of the traditional Easter and summer markets. It did so successfully, and the scheme opened to the public on 1 April 2013. The scheme is similar to previous initiatives so the Department and the Agency used existing structures, such as Help to Buy agents (previously known as HomeBuy agents) that were already in place (paragraphs 2.7, 3.13-3.14).

14 **The speed of the scheme's introduction meant that there were some issues that the Department and the Agency needed to address during scheme implementation.**

- Some buyers (205, which was 1.6 per cent of completed cases at 31 December 2013) have bought a property with a deposit contribution of less than 5 per cent. This increases slightly taxpayers' exposure to costs if these properties are repossessed (paragraph 3.25).
- Implementing the scheme quickly meant the Agency did not finalise new terms and conditions for Help to Buy agents immediately. Agents therefore received £1,000 for each of 1,462 transactions, rather than the £600 they now receive (paragraph 3.15).

3 National Audit Office analysis of Land Registry data (© Crown copyright 2013).

The scheme's costs

15 **The Department expects to make back its investment in cash terms after 15 years.** In its central estimate the Department expects a gross return in cash terms of £4.8 billion by 2040-41. Once it has invested in the scheme, the Department's return will depend on market factors which it has limited ways to influence. The Department's financial modelling indicates that the scale and timing of the cash return will vary substantially based on when buyers pay off their equity loans and the value of the Department's equity loans at the time (Figure 9 and paragraph 2.11).

16 **Cash flow will vary from year to year and in some years the impact of this could be unaffordable for the Department.** The scheme will also involve income and expenditure in cash terms, which will impact the Department's and the Agency's ability to manage their budgets. Regardless of the scheme's impact on the market, it is a long-term financial commitment with uncertain returns. The Department will receive income from fees on the equity loans and from increases in the value of its equity loan. It will make losses if properties are sold for less than their purchase price. Under current accounting arrangements the Agency bears this risk on its statement of financial position. This creates a risk of over- or underspending in-year, if income is higher or lower than expected or the value of the properties remaining in the scheme changes. The Department and the Agency have used their experience of previous schemes to develop a credit-risk model to monitor this situation. The Department and the Agency have committed to monitoring this (paragraphs 2.8 to 2.11 and 3.26 to 3.28).

17 **The Department's central estimate of the scheme's economic cost is £494 million in today's terms.** The economic cost takes into account the effect of inflation and discounting, over the potential period of the loans. As with the cash flow, the eventual economic cost will depend on market factors and when buyers redeem their loans. The Department modelled a range of scenarios based on a variety of assumptions about these factors. This indicated that the economic cost could be between £16 million in the best-case scenario and £1,227 million in the worst-case scenario (paragraph 2.12 and Figure 10).

18 **The Department estimates that at least a quarter of sales through the scheme will have to result in new homes being built if economic benefits are to exceed costs.** The Department considers that between 25 and 50 per cent of sales will result in new homes being built, with associated economic benefits of £500 million and £1 billion respectively, in these scenarios. Developers report that the scheme is encouraging them to build more, more quickly, so the scheme could lead to some net increase in the supply of new homes. We cannot, however, verify the Department's figures at this stage. The Department has not evaluated previous, similar schemes' influence on home-buyers' behaviour or home building levels, to develop more robust estimates. Nor has it yet collected information from buyers or developers on what they would do, or would have done, without the scheme (paragraphs 2.5 and 2.13 to 2.14).

The scheme's impact

19 The evidence so far indicates that the scheme is helping buyers access the housing market, although we cannot say how many sales would have gone ahead anyway. So far, 89 per cent of Help to Buy equity loan sales have been to first-time buyers. By comparison, since 2005 around one-third of property sales have been to first-time buyers. Seventy per cent of Help to Buy homes are at the lower end of the price spectrum (£75,001 to £225,000) compared to 54 per cent of all newly built homes. The majority of buyers taking part in the scheme (over 98 per cent) have put down a deposit of 5 per cent or more. Most buyers (70 per cent) put down a 5 per cent deposit. In around 3 per cent of cases the buyer was able to provide a deposit of 25 per cent or more. In 2012, home buyers in the UK put down, on average, a 32 per cent deposit (paragraph 2.2).

20 The Department does not have a joined-up approach to evaluating the combined impact of its housing market initiatives. Help to Buy is part of a package of measures to stimulate the housing market and housing supply. We found in our report on the New Homes Bonus that evaluating individual schemes' contribution to broad objectives like increasing housing supply is challenging because there are several overlapping schemes with similar aims.[4] Other economic factors are likely to have an important impact. The Department has committed to reporting on the Help to Buy scheme in its 2014-15 annual report. However, it does not have an integrated evaluation plan to assess the impact of related or complementary initiatives, or a common set of measures for the different schemes (paragraphs 3.31 to 3.33).

Conclusion on value for money

21 So far, Help to Buy equity loans are improving access to mortgage finance and making mortgages more affordable to buyers, particularly first-time buyers. The Department and the Agency got the scheme up and running quickly and it is, for the most part, running smoothly. By enabling people to make purchases more easily, the scheme appears to have boosted developers' confidence.

4 Comptroller and Auditor General, *New Homes Bonus*, Session 2012-13, HC 1047, National Audit Office, March 2013. Available at: www.nao.org.uk/report/the-new-homes-bonus-2/

22 The Department expects to recover the scheme's costs in cash terms. In helping buyers invest in property, however, it is committing up to £3.7 billion as a long-term investment in the property market. This money cannot be used for other purposes until it is recovered. The cost to the taxpayer, in present value terms, is uncertain at this stage but is likely to be significant. Each new home built as a result of additional demand through the scheme will provide economic benefits but the Department cannot yet quantify robustly how many of the people accessing the scheme would have bought a home anyway, or how many additional homes will be built as a result. For these reasons, we cannot yet say whether the scheme will provide value for money. To provide value for money, the Department and the Agency need to reduce and manage the risks to taxpayers' money. This will be challenging, given the limited levers the Department has to influence the housing market once it has invested in the scheme. In addition, it should quantify the scheme's impacts through robust evaluation.

Recommendations

a **The Department should monitor the effectiveness of its actions to minimise the number of buyers accessing the scheme with a deposit of less than 5 per cent and take further action if required. It should clarify rules such as this from the outset of future similar schemes.** This will help the Department and Agency to manage and monitor the level of risk exposure for taxpayers.

b **The Department should continue to refine its financial modelling to produce more precise estimates of likely cash flows for the life of the scheme.** Potential unplanned gains or losses in any one year could create a sizeable underspend or an unaffordable overspend.

c **The Department should undertake a formal evaluation.** Its evaluation should assess how many buyers have bought a home who otherwise would not have and how many new homes have been built as a result. Quantifying the scheme's benefits is critical to assessing whether it is value for money and to deciding whether or not to continue with the scheme or pursue similar schemes.

d **The Department should urgently communicate its plans to developers, lenders and buyers concerning what will happen when the scheme ends in 2016.** This will help respective parties to decide whether to continue to participate in the scheme.