

Why Brown is to blame if there's a property slump

PITY poor Gordon. With the IMF predicting a property slump in the UK which will see house prices dive by 40 per cent, the longest PM-in-waiting could see his premiership curtailed through external events over which he has no control.

Yes, if one believes the ministerial hand-wringing over the Northern Rock crisis, triggered by those pesky second-home owners in Florida, one could be forgiven for thinking it was entirely due to Harold Macmillan's oft-cited "events".

But that would be to deprive Brown of the responsibility and control which he exerted over the economy in his decade as Chancellor.

Superficially, the housing boom looks like a good thing: after all, 50 per cent of ordinary British people's wealth is tied up in property. The country is "irrationally exuberant" – to borrow a phrase from Alan Greenspan – when it comes to the unquestionable belief that such investment is, well, safe as houses.

Bricks and mortar will always be a solid investment, goes the mantra.

However, that is to expose oneself to ignorance of Adam Smith's belief, that it is land, rather than the buildings on it, which fuels the surge in property prices.

After all, land is a finite resource.

But there is a dangerous side to the massive boom in house prices: the Council of Mortgage Lenders predicts there will be 45,000 repossessions next year, up from 30,000 this year. Even this alarming statistic masks the very individual pain that families made homeless will feel when banks seize their assets and homes.

It will no doubt be argued that government can do little to interfere with a runaway property market. Those who have sat on their piles (excuse the pun) and enjoyed the capital growth while not even bothering with improvements will be outraged at the suggestion that a government should even think of tampering with the housing market.

But in his stealthy way, that is exactly what Brown has done: fostered the feel-good spending for the middle classes and wealthy who could draw down on the equity of their homes to buy luxury holidays and pay public school fees.

Meanwhile, those forced to rent have seen wages rise too modestly to keep up with property prices.

Brown's complicity in generating the housing boom – which if history repeats itself will be followed by recession – can firstly be examined by his tinkering with inflation.

While the Bank of England's Monetary Policy Committee has been "freed" from political interference to set its own interest rates, it has been hugely restricted by the very narrow inflation targets meted out to it by the then Chancellor.

As soon as inflation looked like leaping out of that band, Brown quickly ditched half a century of reliance on the Retail Price Index to adopt the Consumer Price Index in 2004, which showed inflation to be much lower.

Inflation would be straight off the chart if house and land prices were taken into account when measuring targets.

Secondly, housing policy is deeply flawed. Property developers and ministers have long

PM's policies while he was Chancellor have set the scene for a recession in the housing market



Gerri Peev

decided that the rise in single households means that there is a need to build more homes.

This ignores the fact that consumers have free will. They do not like being shoehorned into identikit flats, stranded on the fringes of cities, where they are reliant on cars to drive half an hour for a pint of milk.

And while there has been a rise in single households, this is not entirely composed of young 30-something women who refuse to marry and keep too many cats.

Increased life expectancy means there are now more pensioner households. But a widow is more likely to want to stay in a self-contained unit or her own family home than move into a high-rise in a commuter belt.

The glut of flat-building can be explained by the fact that for developers, it is much more lucrative to plonk 50 properties on a block of land than a cluster of houses. (Remember the 300 per cent rise in 20 years).

Fred Harrison, the director of the Land Research Trust, articulates the discrepancy between land and house prices.

He points out that in 20 years, house prices have risen 36 per cent while land prices have soared by 307 per cent over the same period. More worryingly, he has examined 400 years of economic history to demonstrate how property booms are followed by recessions. The cycle is once every 18 years, which according to projections means the market will reach its bottom in 2010. Incidentally, he made this prediction in 2005 – along with an estimate that house prices would begin to go down in 2007-8.

An additional error of judgment by Brown – while well meaning – was the decision to pump billions into subsidies for housing to be allocated to "keynote" workers such as nurses, teachers and police officers. Any non-economist understands this drives up the cost of homes for everyone – including other low-waged workers perhaps not marked out as being vital for the economy.

And what of the many areas that have not seen as huge a price rise as the South-East? While the annual growth rates between England and Scotland are narrowing, the average price of a home in Greater London is still more than twice that of a house in Scotland.

Yet Scottish homeowners are being made to pay for this through five interest rate rises since August last year. If an Englishman's overpriced home is his castle, then that same home is fast becoming a burden for the Scottish mortgage payers. Indeed, there is an argument for Scotland to set its own interest rates – but whether this level of fiscal autonomy is granted is not worth betting the house on.