

Are Government Policies Destroying the UK Property Market?

*The plethora of government policies will hurt the UK property market, says **Godwin Okri***

The free-market economist, Friedrich Hayek once opined that the free market is not just the most efficient way to organise economic activity but also a guarantor of personal liberty. Most free market economists (including monetarists, Keynesian and neoclassical economists) agree that intense and regular **State** intervention in the free market could be destructive. So, how "free" is the UK property market?

The housing shortage and affordability crisis have been identified by the Government as key problems in the UK property market. As a result, the Government has introduced a plethora of policies as panacea to cure the (alleged) ills of the property market, which are the following:

Firstly, the Government has introduced the Housing & Planning Bill. This Bill heralds the intention of the Government to build affordable homes for first time buyers (FTB) and to speed up the planning process with a view to delivering more housing.

Secondly, the Government introduced the Help-to-Buy Scheme to encourage FTB access the property ladder. Under this Scheme, FTB can get interest-free loan of up to 40% of the property value provided the FTB has 5% deposit.

The Help-to-Buy ISA was also introduced to give FTB the opportunity to receive 25% top up payment from the government when they save £200 a month in a dedicated ISA. This would enable FTB raise the deposit required to purchase a home.

Furthermore, the government announced that anyone buying a second home would pay a higher rate of stamp duty. This was introduced in order to keep a tight rein on Buy-to-Let investors (BTL),

Fifthly, as part of the Finance Act 2015, BTL landlords will be prevented from deducting their mortgage interest costs from their rental income when calculating taxable profit.

Lastly, as part of the Immigration Act 2014, all BTL landlords in England are required to check the ID of new tenants before the commencement of their tenancy to ensure they are legally entitled to live in this country. A fine of £3,000 is payable for any breach of this rule.

Are all these laws and policies necessary in a free market economy? Have these policies gone too far so as to have 'crossed the Rubicon'?

Whilst there is economic benefit for building more affordable homes, it is difficult to see how all the other laws and policies are justified in a country of free enterprise. Firstly, the Help to Buy Scheme and ISA is premised on the false assumption that owning a house is good for everyone, even if they cannot afford it. The Scheme is a government loan for five years. What happens after the expiration of five years or if the mortgage rate is hiked? This will cause a flood of repossession, the very thing that caused the 2008 financial crisis.

The desire to increase the number of homeowners above the 'natural' market rate is likely to lead to a lot of economic pain. This is a form of "creative destruction". In his book "*The Financial Crisis and the Free Market Cure*", John Allison refers to actions of this kind as a misallocation of resources which is destructive to the free market. As Paul Ormerod (author of "*The Death of Economics*") would say: "When the **State** attempts to take on that role, it can have the opposite effect to the one intended, making people depend on the **State** and unable to help themselves."

Another destructive policy by the government is increasing the stamp duty rate for second homes. From 1 April 2016, anyone buying a second home will pay higher rate of stamp duty. This will lead to unintended consequences which will be destructive to the housing market.

For a start, some BTL investors may transfer the increased expense to their tenants in the form of higher rents. This is destructive to the market as it will lead to cost-push rent inflation, which is counterproductive in economic terms. Secondly, the fundamental error in raising stamp duty on residential property may limit the supply of affordable homes: increasing stamp duty makes property purchase more expensive, which may drive down demand. As demand falls, developers may be reluctant to risk building more affordable homes, with the result leading to fewer affordable homes being built. It is important to note that developers assess their equity multiples when considering whether to build homes. The equity multiple is a ratio that compares equity with leverage. Dampening demand by increasing stamp duty will affect this ratio.

Furthermore, the policy by the government preventing BTL landlords from deducting their mortgage interest costs from their rental income when calculating taxable profit goes against established accounting principles. The usual accounting rule is that cost is deducted from income in order to arrive at a profit. Treating gross income as profit runs contrary to this principle and is illogical. The policy is also counterproductive because BTL investors may increase their rent(s) to take account of this illogical policy. The government has failed to factor in human nature; eventually the laws of human nature are what drive all economic activities.

Lastly, the requirement that all BTL landlords check the ID of all new tenants before the commencement of the tenancy is simply adding more layer of bureaucracy and red tape on them. For instance, there are many unanswered questions: Are EEA or EU prospective tenants entitled to live in this country? Would BTL landlords be responsible to checking whether the documents are forged? Where a landlord engages a managing agent, who would be liable for breaches of this rule? Further, the additional expense the majority of the 2 million BTL landlords may incur, as a result of this illogical policy, may have to be borne by innocent tenants.

In sum, the plethora of Government policies will hurt the UK property market. The key message here is this: the Government should not interfere in the market process. A free enterprise society creates an environment of freedom upon which creativity flourish. This guarantees "the greatest happiness of the greatest number".

Godwin Okri

Author of the book

"Investing in Property with Strategy"

£6.99 Amazon

Godwin Okri is the CEO at Menvo Limited

His email address is: godwin@menvold.com

He can be reached on +44 (0)7774 639435