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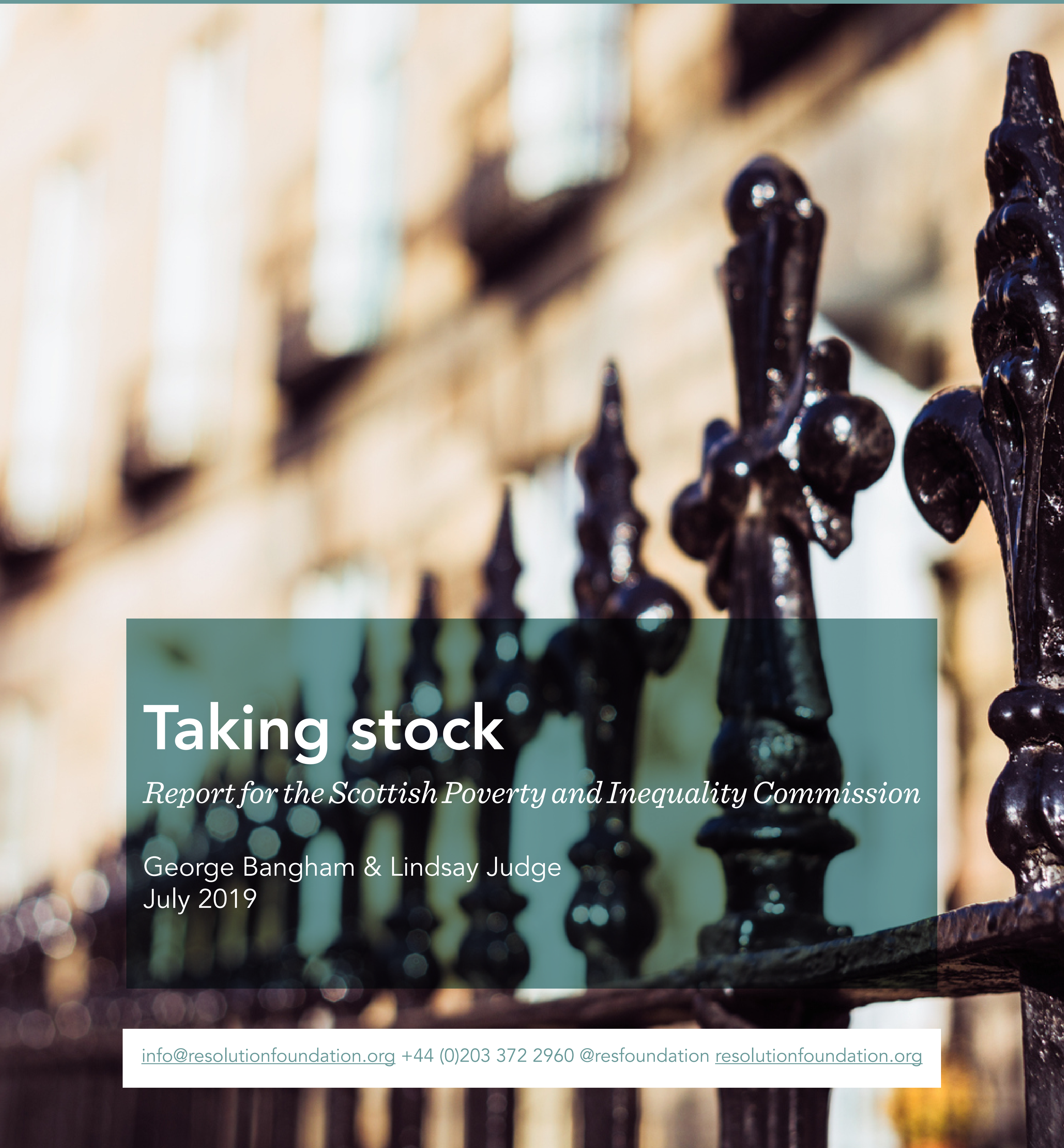

Taking stock

Report for the Scottish Poverty and Inequality Commission

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July 2019

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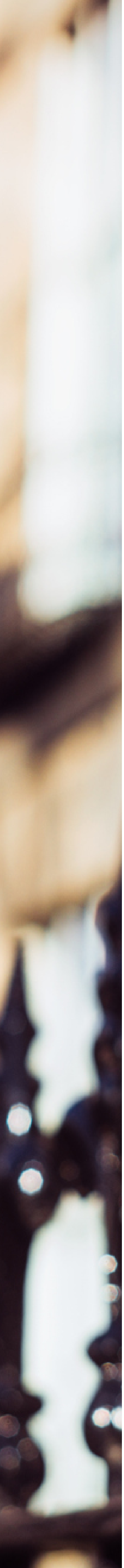


Contents

Executive Summary

There has been a growing appreciation in recent years that living standards are determined not just by income (the flow of money into a household) but also by wealth (the stock of assets a household owns). Wealth can take various forms: it can be held in financial instruments (for example, a savings account or as shares); in a private pension; or as a physical asset (for example, land, an art work or piece of jewellery). But the most visible way that households accumulate and store significant amounts of wealth is through the ownership of their (or others') homes.

Compared to income, wealth has generally been poorly measured – unsurprising given that it has only recently become the subject of serious study. As a result, erroneous or unexamined views about the topic are widespread. In this report, we bring together a wide range of data sources to take a long, hard look at both the scale and distribution of housing wealth in Scotland over time. In light of the evidence, we then reflect on a number of ways that Scottish policy makers could address the growing concerns about the scale and impact of housing wealth inequality.

On any account, Scottish housing wealth has risen sharply (albeit unevenly) over recent decades

Housing wealth (defined throughout this report as the net value of residential dwellings held by households) has grown significantly in Scotland over time. We estimate that Scottish property wealth was worth around £2.7 billion in 1968; by 2018, this figure had increased by a factor of more than 100 to an estimated £308 billion. This large nominal rise constitutes a nine-fold increase in value in real terms.

However, housing wealth has not grown smoothly over time. Instead, we distinguish four periods:

- To begin, in 1968-1980, total value increased slowly, growing at less than 1 per cent a year on average;
- Between 1980 and 2001 the pace picked up, with an average annual rate of 3.5 per cent observed;
- The years 2001-2008 are the standout: housing wealth increased at a staggering average rate of 23.4 per cent a year over this period;

- Finally, in 2008-2018, the value of Scottish housing wealth first fell but then grew once again, increasing at an average annual rate of 3.6 per cent since 2013. As a result, today we estimate the total real value of Scottish housing wealth stands just shy of the peak we observed before the financial crisis.

Housing wealth has risen due to changes in both ownership and price – but the latter effect has dominated

So what explains the dramatic growth of housing wealth over time? To begin, there are simply more residential dwellings in Scotland today than there were fifty years ago. More pertinently, however, the share of these homes held privately by households has increased significantly over this time. In 1968, we estimate that half of all residential dwellings in Scotland were in public ownership (by far the highest rate of any of the four nations); by 2018, four out of five homes were in private hands. But the change in stock is not the whole story. A look at Scottish house prices shows that the average value of a privately owned dwelling in Scotland has increased in nominal terms almost five hundred-fold over the past fifty years.

With changes in housing wealth driven by both stock and price effects, we also consider which has been stronger over time. In 1968-1980, we note that the small increase in total housing wealth was entirely driven by a rise in the value of dwellings. Between 1980 and 2001 the growing number of privately owned dwellings becomes more important - unsurprising given this was the heyday of Right to Buy. The price effect then dominates dramatically in the period 2001-2008 as house prices escalate at a rapid rate. Finally, in the most recent period 2008- 2018, the stock effect has strengthened once again but price still remains a more important determinant of Scottish housing wealth growth over this time.

Wealth is less equally distributed than income, but housing wealth is not its least equal form

Wealth is far less equally distributed than income in Scotland as elsewhere, in large part because while there are few families that have no income, there are many who hold no wealth at all. In Scotland today, for example, 35 per cent of households do not own their home (likewise, 23 per cent have no pension savings while 20 per cent hold no financial wealth). As a result, the absolute gap between high- and low-wealth families is higher for housing wealth than wealth held in either of these other forms.

However, wealth inequality is determined not just by the number of 'haves' versus 'have nots': equally important is the way that wealth is distributed within the 'have' group. Given this, we show that measured formally using the Gini coefficient, housing is not the least equal form of wealth in Scotland today by virtue of it being more evenly spread across the property owning group than financial wealth (although it is twice as unevenly distributed as income). In this regard, Scotland today looks very similar to the rest of Great Britain.

Housing wealth inequality and rates of home ownership are closely related

That has not always been the case, however. A look at housing wealth inequality over time shows that Scotland has historically recorded higher levels than England and Wales. Yet somewhat paradoxically, we observe a significant fall in the housing wealth Gini coefficient in Scotland from the mid-1990s until 2008 despite the fact that this was a period of rapid house price growth. Likewise, from 2008 to 2016, housing wealth inequality rose despite the very tepid house price inflation over this time.

For an explanation of these long-term trends we have to look less (at least in the first instance) at how prices have changed over time, and more to the ownership of private dwellings. When we do so we note that home ownership rates rose in Scotland up to 2004 (and essentially flat-lined for a few years after that), expanding the share of families who are housing 'haves' and serving to reduce housing wealth inequality in the process. Conversely, from 2008, the proportion of families who own their home began to fall, concentrating privately-held Scottish housing stock in fewer hands and driving up the Gini as a result.

Higher income families hold the lion's share of housing wealth, not least because they often own multiple properties

In 2014-16, we estimate that households in the highest income 10 per cent held around 30 per cent of all Scottish housing wealth. Of course, in many ways this is to be expected: one of the main ways a family accumulates is by saving part of its income. But critically, in recent years, we can see that those at the top of the income distribution have come to own an increasingly large slice of the housing wealth pie in Scotland. Families in the highest income decile held on average 2.5 times as much housing wealth as those in the middle in 2010-12; by 2014-16 that figure that had risen to 3.4.

One of the key reasons why higher income families hold a large share of total housing wealth is because they are far more likely than those further down the income scale to own additional property (either for their own consumption or to let out for rent). Although the ownership of properties other than the primary residence is slightly more evenly distributed in Scotland than it is in England and Wales, we note that 27 per cent of families in the top income decile have at least one additional property compared to just three per cent of those in the middle of the income distribution.

Young people in Scotland today hold less housing wealth than the previous cohort at the same age

Just as it is unsurprising that those with higher incomes hold larger amounts of housing wealth so, too, we should expect older people to be wealthier than those in younger age groups simply by virtue of having accumulated over time. As a result, comparing young people's housing wealth with that of older people in the here and now is not revealing. What is, however, is looking at how much housing wealth different birth cohorts hold at the same point in the life course. When we do this we note that those born between 1981 and 1990 hold half the property wealth in their early 30s that those born in the previous ten-year period did at the same age.

To understand intergenerational wealth inequalities it is largely to the rates of home ownership that we must look. We show that 35 per cent of families in Scotland headed by someone born 1981-90 owned their home by the age of 30, compared to almost half of those born 1961-70 and 1971-1980 at the same age. While some of the gap between cohorts may be explained by changing norms (for example, staying in education longer or delayed family formation), it is clear that rising prices which have driven up the property wealth of older cohorts over time have also acted to lock many young people out of the housing wealth 'haves' group altogether. Moreover, we note that the likelihood of becoming a young home owner today is more strongly related to whether one's parents hold property wealth than it was 25 years ago.

Housing wealth inequalities are determined by place in two distinctive ways

A family's housing wealth is determined not just by income and age, but also by where within Scotland any property they hold is located. In Edinburgh, for example, the average residential dwelling is currently worth more than 2.5 times that in East Ayrshire. But have housing wealth inequalities between areas grown in recent years? In fact, we show that those local authorities with the highest prices in 2004 have generally not experienced higher than average house price growth over the past 14 years. As a result, while absolute housing wealth inequalities do exist between areas given the significant price differentials, in relative terms these have not increased over time.

However, there is another way we can think about housing wealth inequalities at the lower geographic level and that is vertically (within local authorities) rather than horizontally (between local authorities). Given that we know that a higher rate of home ownership is inequality-reducing (because more families are then housing wealth 'haves' rather than 'have-nots'), and higher rates of additional property ownership have the opposite effect (because housing wealth is concentrated in fewer families' hands), we identify cities such as Aberdeen, Dundee, Edinburgh and Glasgow as the places where housing wealth is likely to be least equally distributed within an area.

There is growing concern about housing wealth inequalities, and an appetite for reform

Holding wealth in any form has many benefits: those with assets are able to take more risk often leading to more reward, have higher wellbeing, and the prospect of negligible housing costs in later life. Given this, policy makers in the UK have taken a largely positive view of housing wealth accumulation over time. From Right to Buy in the 1980s, through to Help to Buy today, enabling families to become housing wealth 'haves' has been an enduring political objective.

However, in recent years, concerns about the distribution of housing wealth have increasingly come to the fore. For many, the fact that a large part of the population has made significant windfall gains from holding property sits uncomfortably alongside the struggles of others to find affordable (or indeed any) housing in Scotland today. Moreover, there is growing recognition that property taxation has not kept pace with the rise in housing wealth even though there has been action taken in Scotland on this account. So how could policy makers respond?

Action to support home ownership needs careful consideration

One obvious response from Government would be to increase the support they offer to those on lower incomes or in the younger age bracket to get on the home ownership ladder. However, policy makers should be mindful of a number of Scotland-specific factors that suggest 'catch up' to previous home ownership rates could be in sight in the absence of further policy intervention. The fall in home ownership was not as dramatic in Scotland as it was in England and Wales for example; house prices are currently falling slightly; and the Scottish population is growing so slowly that it is projected to decrease from 2049. On the other hand, the ending of Right to Buy in Scotland could act as a brake on home ownership rates (whatever one's views on the wider social implications of this policy change).

If policy makers were still mindful to take action to speed up this process and support first-time buyers in some way there are a number of issues to consider. The evidence is clear that policies such as Help to Buy potentially stimulate demand to the point where house prices are raised in some areas (and as currently designed, the programme also has significant deadweight). A better, more radical, approach to increase home ownership rates (and allocate housing stock more efficiently) would be to rebalance demand to own one's home in the interests of younger and lower income families generations through reform of the tax system.

The mismatch between the value of housing wealth and property taxation strengthens the case for reform

Council Tax has many functions: it operates as a tax on housing consumption, for example, and raises revenues for local services. But it is also the most significant property tax in terms of revenue in Scotland today; the only tax on housing paid on a recurrent basis; and, of course, it is fully devolved. Given this, it makes sense to think carefully about both its current operation, and whether there are further options for its reform.

Despite the recent changes in Scotland, Council Tax is still almost as regressive as the Poll Tax it replaced. For example, those living in Band A properties face a bill amounting to as much as 2 per cent of the value of their home each year, compared to less than 0.03 per cent of the property value levied on those in Band H. Likewise, comparing Council Tax with the average amount of income tax paid by households in each income decile is also instructive. Council Tax is remarkably flat right across the distribution, with those in the top decile paying only 2.7 times as much Council Tax as those in the bottom in cash terms.

On both efficiency and equity grounds, then, there is a strong case for further policy action when it comes to Council Tax. We consider four potential reforms, each of which has something to recommend it. Whether that is the realism of the 'revaluation' model, the simplicity of the 'flat rate' scheme, the equity of the 'fully progressive' option or the revenue raising power of the 'allowance and flat rate', there is clearly much (technical) scope to improve the current system. But would property tax reform per se drive down housing wealth inequalities?

Reforming property taxation could affect housing wealth inequalities through a number of channels

There are various channels through which a more robust property tax could operate to have this effect. To begin, raising the cost of holding property would have a downward effect on prices, reducing the absolute gap in wealth between the housing 'haves' and 'have-nots'. Likewise, the distribution of wealth held by the property owning group would change if higher value properties were taxed at a higher rate than those worth less. And critically, lower prices and more efficient stock use might make it easier for first-time buyers to purchase; if home ownership increased we would expect to see a downward effect on wealth inequality.

However, it is less clear whether those with additional properties (held either for private consumption or for rent) would respond differently from primary residence owners under any of the options we explore. This is important given that, all else being equal, additional property ownership drives up housing wealth inequalities by concentrating the stock in fewer hands. Given this, there is a logic to policy makers considering higher rates of tax on multiple properties, or increasing the surcharge levied on additional property purchases under the Land and Building Transaction Tax regime still further.

Of course, it would be wrong to underestimate the challenges that any Government would face in implementing wholesale reform of Council Tax. There would be many practical considerations: how to transition to a new system, for example, and how to protect asset-rich but cash-poor households from unreasonable bills.

Policy makers should also improve the security of those without housing wealth

There is a further way in which the Scottish Government could respond to housing wealth inequalities – and that is by taking action to ensure that the benefits of holding such wealth are also available to those who are unlikely to ever have the incomes (or parental support) to support home ownership. Recent tenancy reform has functioned to improve the security of privately renting families for example. Looking to the future, building more affordable homes could further increase the number of families with a decent home and manageable housing costs; supplementing benefits for families could tackle housing affordability from the income side; while funding the energy efficient retrofitting of housing stock could drive down energy bills as well as improve quality of life.

Of course, many programmes to improve the affordability, security and quality of housing for those without housing wealth would require substantial public investment. But as well as improving equity, property tax reform could also raise additional revenues from an undertaxed type of wealth that could be devoted to such ends. We estimate that all but the 'revenue neutral flat rate' proposal we model would generate significant amounts of new money ranging from £0.3 billion to £1.5 billion a year. While there would be many calls on new funds, reforms of this type would clearly enable the Scottish Government to spread housing wealth gains beyond the holders themselves.

Tackling housing wealth inequalities is far from simple – but the case grows increasingly clear

Analysing how housing wealth inequalities have evolved in Scotland over time is very revealing. We can see, for example, that where we are today is the product of policy choices often made many years ago (think Right to Buy) as well as long-run economic forces (the liberalisation of credit and its contraction since 2008). While many families have been (often unwitting) winners in the housing wealth stakes, others have clearly lost out as a result. And as we come to understand more fully the impact that holding housing wealth can have on living standards, action to share the benefits it brings becomes ever more appropriate.

Fundamentally, however, change remains elusive because of the political challenge faced when tackling housing wealth inequalities. Properties are rarely just assets: they are also homes with emotions and memories attached. But when the evidence shows so clearly that the huge housing wealth gains of the past fifty years have been largely unearned, that many people locked out of the wealth owning group struggle with housing costs today, and the main property tax has grown so inequitable and inefficient, the case for action is clear.

Section 1

The big picture

There has been a growing appreciation in recent years that living standards are determined not just by income (the flow of money into a household) but also by wealth (the stock of assets a household owns).[1] Wealth can take various forms: it can be held in financial instruments (for example, a savings account or as shares); in a private pension fund; or as a physical asset (for example, land, an art work or piece of jewellery). But perhaps the most visible way that households accumulate and store significant amounts of wealth is through the ownership of residential property.[2]

Compared to income, wealth has generally been poorly measured – unsurprising given that it has only recently become the subject of serious study. As a result, erroneous or unexamined views often abound. However, there is a significant amount of evidence available that can help us understand the scale and distribution of Scotland's housing wealth, both in the here and now and over time. In Box 1, we overview the data sources we draw on in this report, and highlight an important distinction between the two main approaches we use throughout.

Box 1: Understanding Scottish housing wealth

In 2008, the Office for National Statistics (ONS) took steps to improve understanding about all forms of wealth with the introduction of the Wealth and Assets Survey (WAS). Now in its fifth wave, WAS provides best evidence of the scale and distribution of housing wealth in Scotland (and the rest of Great Britain). In addition, questions about wealth have been asked in the British Household Panel Survey (BHPS) and its successor survey Understanding Society (USOC) since 1993, sources which are a useful supplement and cross-check to WAS.

However, these survey sources have their limitations. First, while they

[1] See, for example, T Piketty, *Capital in the twenty-first century*, Harvard University Press 2014 and A Atkinson, *Inequality: What can be done?*, Harvard University Press 2015.
[2] This report focuses on Scottish residential property wealth held by households. As a result, commercial property and residential property held by institutions (such as universities, pension funds or corporate bodies) are both treated as beyond the scope.

allow us to build up a picture of the past 25 years, wealth, by virtue of its accumulative nature, is often a long-run phenomenon. Second, both WAS and BHPS/USOC sample size means we can get no insight at a more granular geography. But as well as the survey data, information has been collected about both the stock and price of privately held dwellings at the national level for fifty years-plus, and at the local authority level since 2003. Using these sources, it is possible to explore Scottish housing wealth over a longer time frame and at a lower geographic level (see Annex 1 for more details on the method we have developed to bring stock and price data together).

It is important to note, however, that survey and stock-price data provide insights into two slightly different forms of Scottish housing wealth. Using WAS and BHPS/USOC allows us to explore the housing wealth of those resident in Scotland. However, some of this wealth will consist of properties located in places elsewhere (a holiday home in Spain, for example, or a private rented flat that is in another part of the UK). Conversely, the stock-price data can tell us about the housing wealth that stems from property located in Scotland. Some of the wealth identified using this method could be held by someone not resident in the nation (an absentee landlord, for example, or a Londoner with a holiday home on the Islands).

In practice, the difference between the two approaches may be small given that the vast majority of housing wealth is held in primary residences where both the property and the owner(s) will be Scotland-based. But this is a distinction that is important to keep in mind especially when we look at the additional properties (both second homes and those held for private rent) that frequently figure in our explanations of the evolution and distribution of housing wealth.

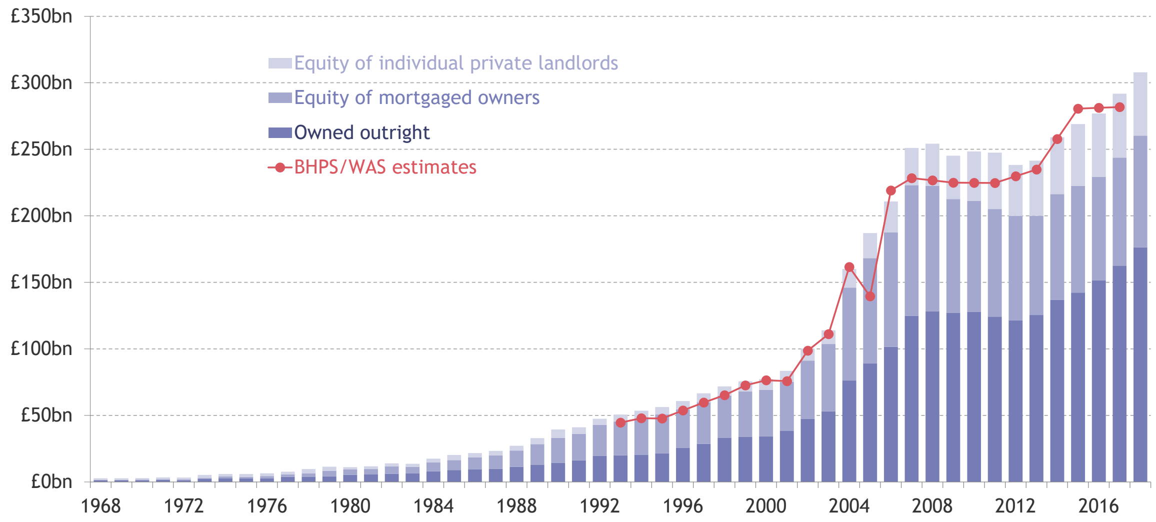
Housing wealth has grown dramatically in Scotland over the past 50 years

To assess aggregate trends it is necessary to use the stock and house price data to construct a long-run time series of net residential housing wealth in Scotland, and cross-check this against the survey sources.[3] Figure 1 presents the results of this exercise and shows how housing wealth has increased sharply over the past fifty years. We estimate that in nominal terms households owned an estimated £2.7 billion of Scottish housing wealth in 1968; by 2018 this figure had increased by a factor of more than 100 to an estimated £308 billion.

[3] See Annex 1 for a detailed discussion of the method used to construct our long run series.

Figure 1: Scottish housing wealth has increased more than one hundred-fold in 50 years

Estimated net housing wealth (nominal): Scotland, 1968-2018



Notes: See Annex 1 for details of methodology
Source: RF analysis of ONS, *Family Expenditure Survey 1961-1983; Labour Force Survey 1984-2018*; Scottish Government, *Empty property and second home web tables*; UK House Price index; ONS *Wealth and Assets Survey*; ISER *British Household Panel Survey*

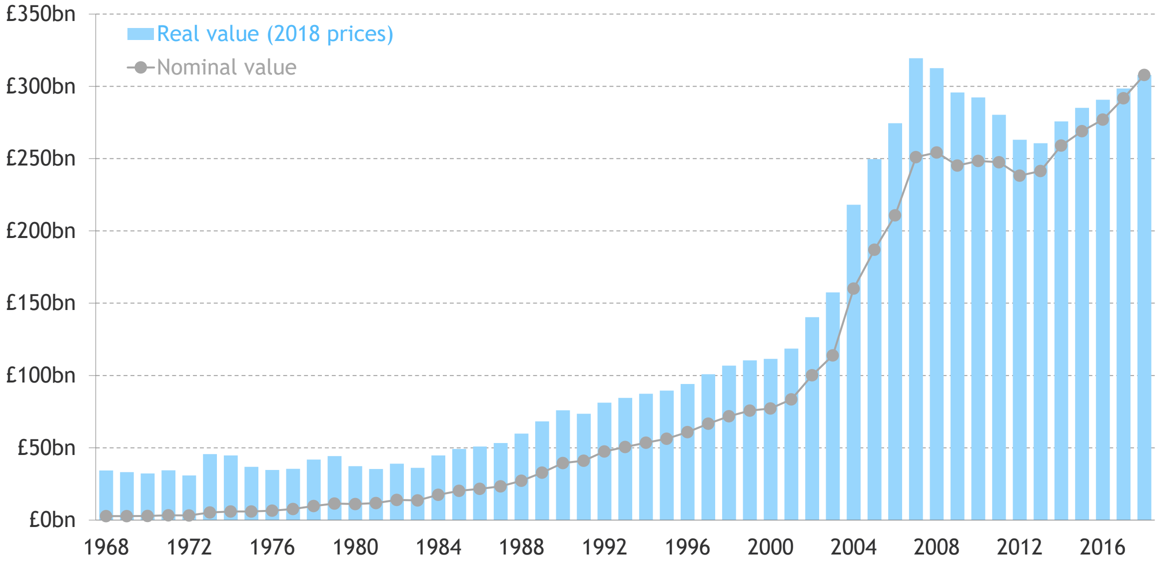
Arguably this picture over-dramatises by presenting nominal values, so in Figure 2 we measure housing wealth in 2018 price terms. On this basis, Scottish housing wealth increased nine-fold in real terms from a value of £34 billion in 1968 to over £300 billion today. Finally, given that there is limited consensus as to the best deflator to use when analysing wealth, we also present results in both share of GDP and per capita terms in Annex 2. On any of these measures, however, the dramatic increase remains a clear feature of the data.

Moreover, as both Figure 1 and Figure 2 make clear, housing wealth has not grown smoothly over the past 50 years. To begin, in 1968-1980 growth was muted, with housing wealth increasing (in real terms) at less than 1 per cent a year on average. Between 1980 and 2001 it began to grow more rapidly at an average annual rate of 3.5 per cent. However, the years 2001-2008 stand out: housing wealth increased at a staggering average rate of 23.4 per cent a year over this period. Finally, in the latest period 2008-2018 the value of Scottish housing wealth initially fell but before picking up pace once again, growing at an average annual rate of 3.6 per cent since 2013. As a result, today we estimate the total real value of Scottish housing wealth stands just shy of the peak we observed before the financial crisis.[4]

[4] The ONS *UK House Price Index* shows that Scottish house prices fell by 0.2% between April 2018 and April 2019, suggesting this rate of growth may not be sustained.

Figure 2: Expressed in real terms, the growth of Scottish housing wealth is still dramatic

Estimated net housing wealth (CPIH/CPI deflated, 2018=100): Scotland, 1968-2018



See Annex 1 for details of methodology
Source: RF analysis of ONS, *Family Expenditure Survey 1961-1983; Labour Force Survey 1984-2018*; Scottish Government, *Empty property and second home web tables*; UK House Price index; ONS *Wealth and Assets Survey*; ISER *British Household Panel Survey*

The growth in housing wealth is the product of three key trends

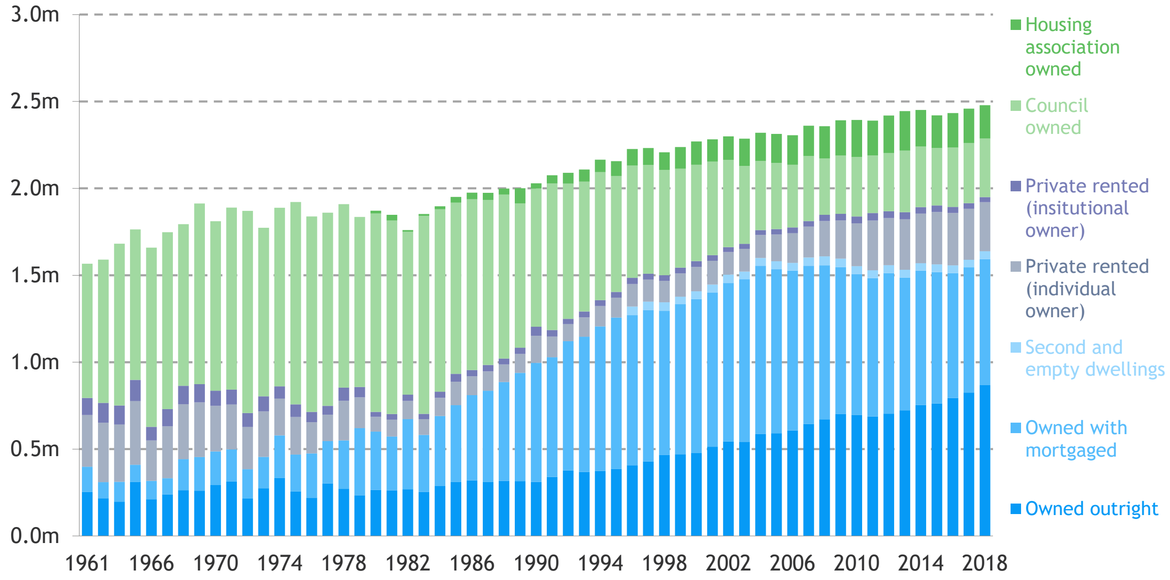
On any measure we employ, private housing wealth has clearly increased at a rapid rate in Scotland over the past half a century. So what lies behind this trend? Three factors are important. First, and most simply, there are more residential dwellings in Scotland today than there were in 1968: as Figure 3 shows, the number of units has risen from 1.8 million to almost 2.5 million over this time.

Second, and far more significantly, the ownership of the housing stock has shifted over the decades (Figure 3). In 1968, more than half of all dwellings in Scotland were in public hands (by far the highest rate of any of the four nations).[5] But the introduction of 'Right to Buy' in 1980, and the fact that the majority of new builds were developed for private sale from this point on, have together put downward pressure on public ownership. Indeed, by 2018, four out of five residential dwellings in Scotland were privately owned.[6]

[5] The scale of public ownership in Scotland is particularly striking: in 1968, 52 per cent of residential dwellings were publicly owned in Scotland compared to 27 per cent in England, 26 per cent in Wales and 24 per cent in Northern Ireland. In 2018, these figures had fallen to 22 per cent in Scotland, 16 per cent in England and 15 percent in both Wales and Northern Ireland.
[6] While a great deal of attention is paid to the rise of the Build to Rent sector today, only a very small number of privately owned dwellings are held by institutions rather than individuals.

Figure 3: The majority of Scottish dwellings are held privately today

Number of dwellings by ownership status: Scotland, 1968-2018

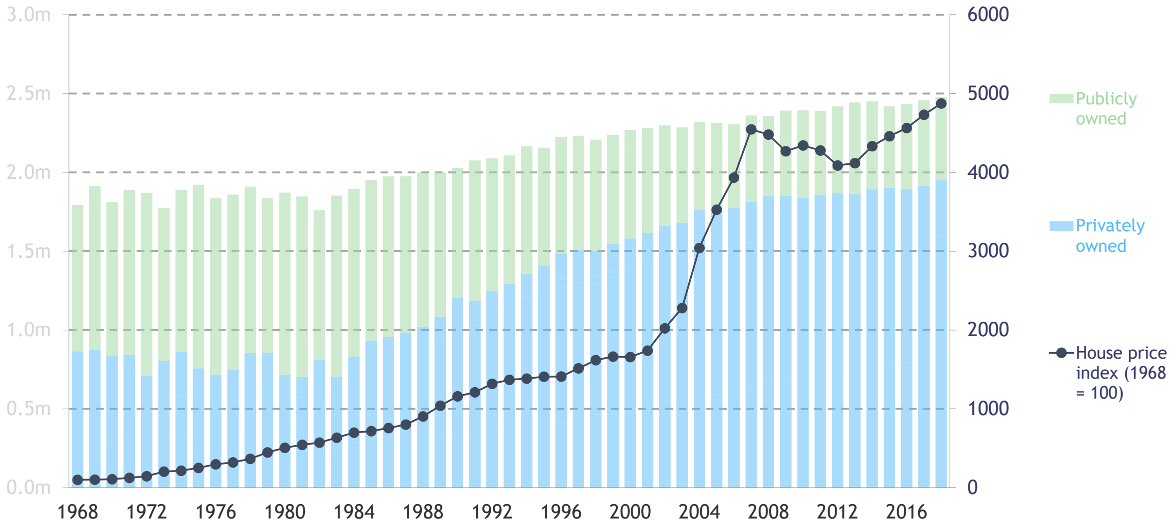


Note: Second and empty stock estimates available from 1995 only
Source: RF analysis of ONS, *Family Expenditure Survey 1961-1983*; *Labour Force Survey 1984-2018*; Scottish Government, *Empty property and second home web tables*

Third, just as the number of residential dwellings held privately has grown over the past 50 years so, too, has the average value of each unit. Figure 4 maps the trajectory of (nominal) Scottish house prices over the period onto our stock estimates. As this makes clear, the average value of a privately owned dwelling in Scotland has increased almost five hundred-fold over the past half a decade. While accounts that seek to explain house price growth often differ in emphasis, demographic change, rising incomes, expanded credit and constrained supply have each in their own way clearly played a role in driving up the value of housing wealth in Scotland over the period.

Figure 4: Scottish house prices have risen sharply over the last half decade

Nominal house price index Scotland, 1968-2018



Source: RF analysis of ONS, *Family Expenditure Survey 1961-1983*; *Labour Force Survey 1984-2018*; Scottish Government, *Empty property and second home web tables*; ONS *UK House Price Index*

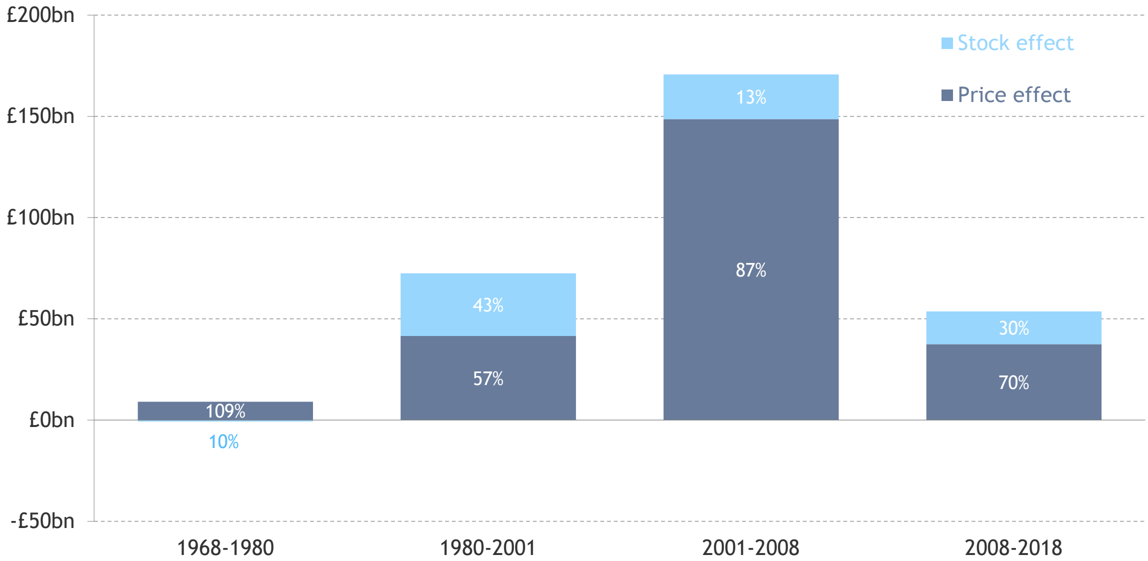
Price inflation has been the principal driver of increases in Scottish housing wealth

Taken together, then, it is the increase in the number of privately owned dwellings and the rise in unit value that account for the surge in Scottish housing wealth we have documented so far. But is one or the other of these more dominant? By decomposing the 'stock' and 'price' effects we can isolate the relative importance of each in the four periods of housing wealth growth we have identified. We set out the results of this exercise in Figure 5.

In the period 1968-1980, for example, the small amount of housing wealth growth observed is explained entirely by a rise in the value of each dwelling. Between 1980 and 2001 the growing number of privately owned dwellings becomes more important - unsurprising given this was the heyday of Right to Buy. That said, the price effect still dominates, as it does dramatically in the period 2001-2008. Finally, in the most recent period the stock effect has strengthened once again but price increases still contribute more to the growth of Scottish housing wealth between 2008 and 2018.

Figure 5: In all our periods, rising house prices explain the increases in housing wealth more than changes in stock ownership

Decomposition of nominal housing wealth growth: Scotland, 1968-2018



Source: RF analysis of ONS, *Family Expenditure Survey 1961-1983*; *Labour Force Survey 1984-2018*; Scottish Government, *Empty property and second home web tables*; ONS *UK House Price Index*

To summarise, so far we have shown that housing wealth in Scotland has grown dramatically in recent years as a result of a rising number of dwellings held privately *and* the increase in the average unit value of these homes. In the next section we move on from questions about its size and evolution of the housing wealth 'pie' in Scotland to consider its distribution: between income groups, age bands and those who hold property in different parts of the nation.

Section 2

The distribution of housing wealth in Scotland

As housing wealth has grown significantly in Scotland in recent years so have concerns about its distribution. In this section we consider how aggregate housing wealth is shared across the population, between income groups, by age and by region and how each of these has changed over time. In Box 2 we set out some of the issues we encounter when analysing housing wealth inequalities, and our preferred method of measurement.[7]

Box 2: Measuring housing wealth inequalities

Housing wealth is generally measured on a household basis, meaning data is usually presented for all the adults who reside in the same property. However, in our view this approach is not always fit for purpose. Consider, for example, a household that consists of a couple with two adult children living at home. It is not accurate to ascribe the net value of the home to all four adults given that the adult children do not own the property (although they may have an expectation of doing so in the future).

To avoid inaccuracies of this type, where possible we analyse wealth on a family unit (or benefit unit) basis. A family comprises a single adult or couple, plus any dependent children. Thus, in our example above, the household would contain three family units – the parental couple counting as one and then each adult child counting as another. We apportion all household-level housing wealth to the main family unit within that household (which in practical terms means the family containing the 'household reference person' in the data).

Finally, we then divide any housing wealth held by the main family between adults in that unit. In other words, if the property is held by a couple we assume they hold that

[7] Data limitations mean that sometimes we use a different approach to that set out in Box 2, most obviously when we turn to look at geographic inequalities. Reiterating a point we made in Section 1, it is important to be aware that results using WAS or BHPS data show the distribution of housing wealth held by residents of Scotland, while that using stock and price data tell us how the wealth that is held in property located in Scotland is shared.

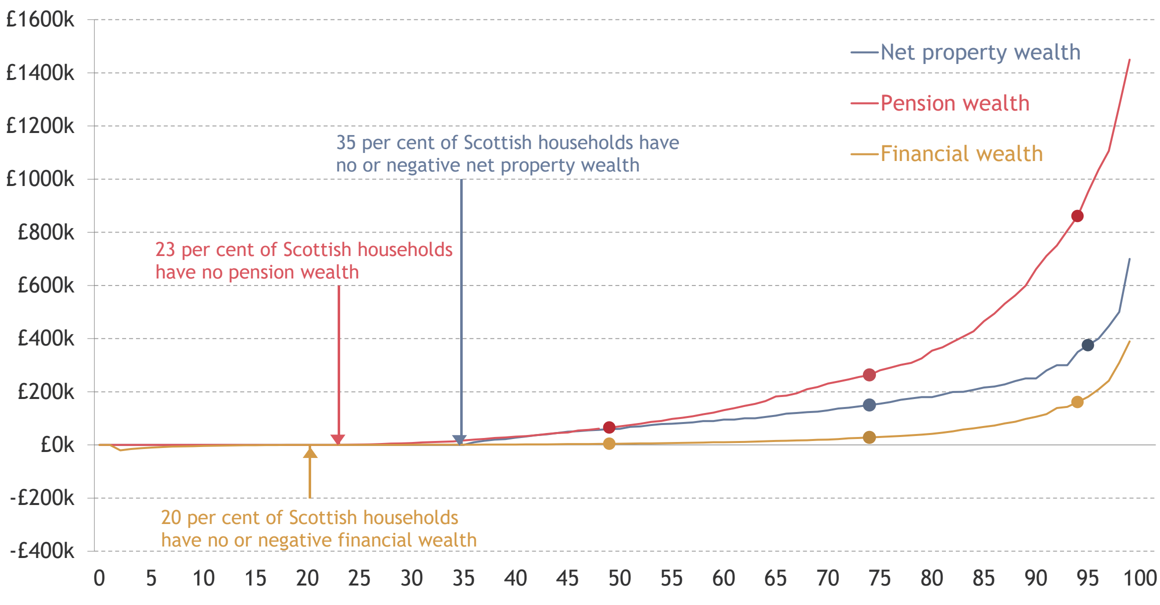
wealth in equal shares. We end, then, with a 'family unit wealth per adult' measure which in our view most accurately captures the reality of how housing wealth is distributed.

Wealth is less equally distributed than income, but property wealth is not its least equal form

Wealth inequalities are essentially determined by two features of the distribution: the proportion of the population that has no wealth at all (the 'have-nots') and the bunching of those that do hold at least some (the 'haves'). Figure 6 shows the distribution of different types of wealth, dividing the population into percentiles according to their holdings of the three main types of wealth. As this makes clear, more adults hold some financial and/or pension wealth in Scotland today than property wealth (or put differently, there are more 'have-nots' when it comes to housing).

Figure 6: Fewer households have any housing wealth compared to pension and financial wealth

Median net family wealth per adult, by wealth percentile: Scotland, 2014-16 (nominal prices)



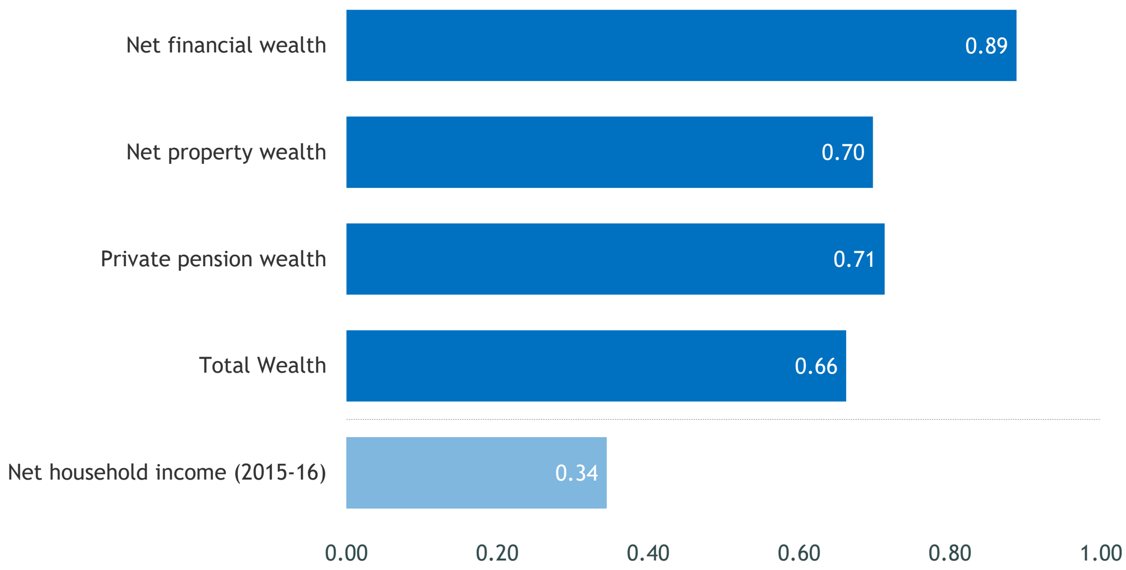
Note: Wealth percentiles are calculated separately here for each type of wealth
Source: RF analysis of ONS, *Wealth and Assets Survey*

When we look at how the wealth is shared between the various groups, however, housing wealth is less top-heavy than the other two types. At the 75th percentile, although a household at that point in the distribution has more pension wealth than property wealth, it only has 2.6 times more property wealth than the middle household, compared to 4 times more pension wealth and 6.8 times more financial wealth. These disparities are even bigger if we compare the middle household with the one that is wealthier than 95 per cent of the population: this wealthy household has 6 times the property wealth, 13.6 times the pension wealth and 41 times the financial wealth.

We express these statistics more formally in Figure 7 by presenting the Gini coefficient for each type of wealth.[8] As this makes clear, financial wealth is the least equally distributed in Scotland today (a function of both the sizeable share of the population that has negative financial wealth i.e. debt, and the concentration at the top of the distribution), while pensions wealth is most equally shared (because large numbers of those living in Scotland have a pension of some form and the value is spread relatively evenly across the 'haves'). Property wealth sits somewhere in between because, although there is a higher share of families in Scotland with no housing wealth than any other type, it is not as highly concentrated at the top as financial wealth. Finally, we note that Scottish wealth writ large is much less equally distributed than income, again in large part because although many households have zero (or negative) net wealth, almost all have some positive level of income.

Figure 7: Property wealth is shared more equally than pension wealth but less equally than financial wealth

Gini coefficient for net family wealth per adult and net household income: Scotland, 2014-2016



Source: RF analysis of ONS, *Wealth and Assets Survey* & DWP, *Households Below Average Income*

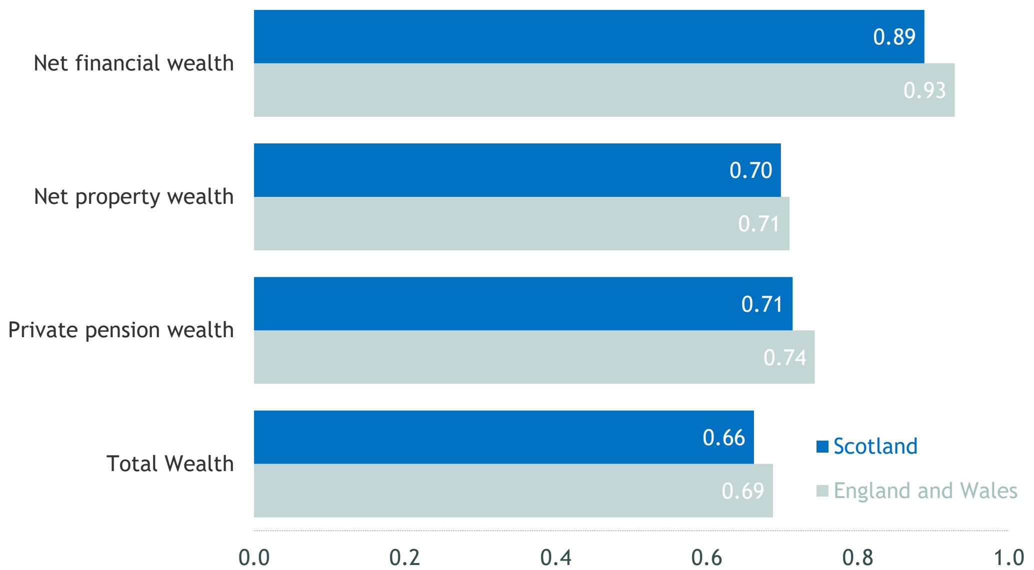
In each of these respects, Scotland does not differ considerably from England and Wales. That said, as Figure 8 shows, Scotland is marginally more equal than the rest of Great Britain when it comes to the distribution of all forms of wealth, with the difference

[8] The Gini coefficient is a long-established measure of inequality where 0 represents perfect equality and 1 perfect inequality. In making the comparisons here we note the formal difficulties with comparing Gini coefficients in order to rank different distributions as more or less equal. See, for example, A Atkinson, On the measurement of inequality, Journal of Economic Theory 2(3), 1970.

between the nations least striking when it comes to housing. Housing wealth is however much less significant as a share of overall wealth than in England and Wales, making up 30 per cent of all wealth compared to 40 per cent in England and Wales. A greater proportion of families' wealth is accounted for by pensions in Scotland (59 per cent) than in England and Wales (46 per cent). In Scotland financial wealth is relatively less important, at 11 per cent compared to 14 per cent in England and Wales.

Figure 8: Wealth is more equally spread in Scotland than in England and Wales

Gini coefficient for net family wealth per adult, Scotland and England and Wales, 2014-2016



Source: RF analysis of ONS, *Wealth and Assets Survey*

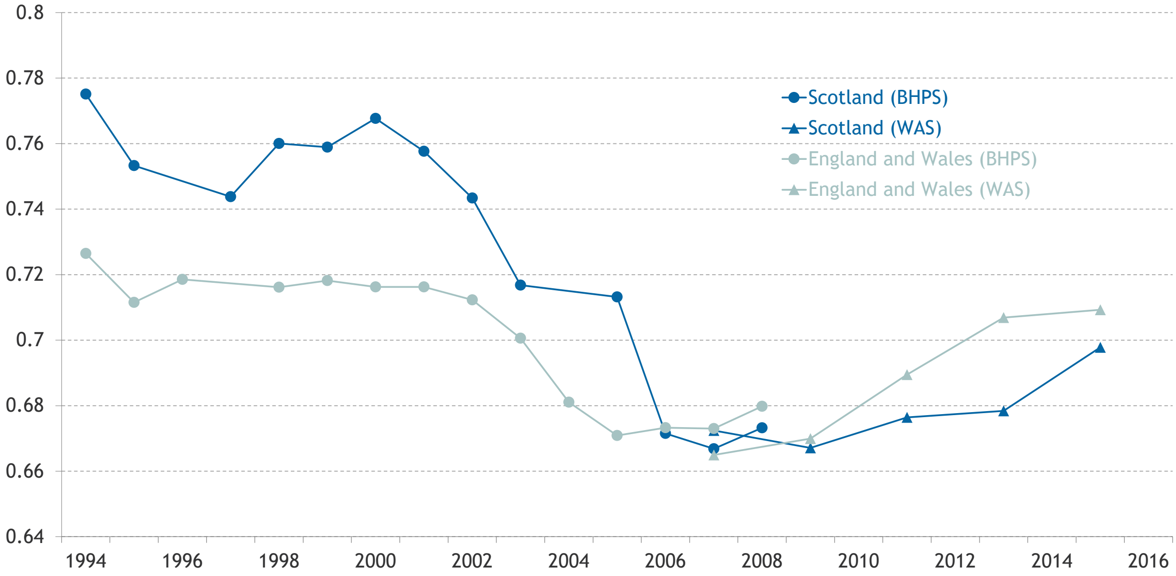
Housing wealth has become more equally distributed over time, but the tide appears to have turned

Moving beyond the snapshot picture, Figure 9 shows how housing wealth inequalities in Scotland fell significantly throughout the 1990s and 2000s, from a Gini of close to 0.78 in 1994 to 0.66 in 2007.[9] However, this positive trend now appears to have gone into reverse, with the Gini rising to 0.7 in 2014-16. In this respect Scotland is not alone, with a similar although not quite so stark pattern observed in England and Wales over the same period.

[9] This trend is in keeping with the long-term fall in UK wealth inequality observed from the 1920s onwards. See J Hills & F Bastagli, 'Trends in the Distribution of Wealth in Britain', in J Hills et al., *Wealth in the UK: Distribution, Accumulation and Policy*, Oxford University Press, 2013 for further details.

Figure 9: Housing wealth inequality fell in Scotland between the mid-1990s and financial crisis, but has risen since

Gini coefficient of net family property wealth per adult: Scotland, 1994 to 2014-16



Source: RF analysis of ISER, *British Household Panel Survey*; ONS, *Wealth and Assets Survey*

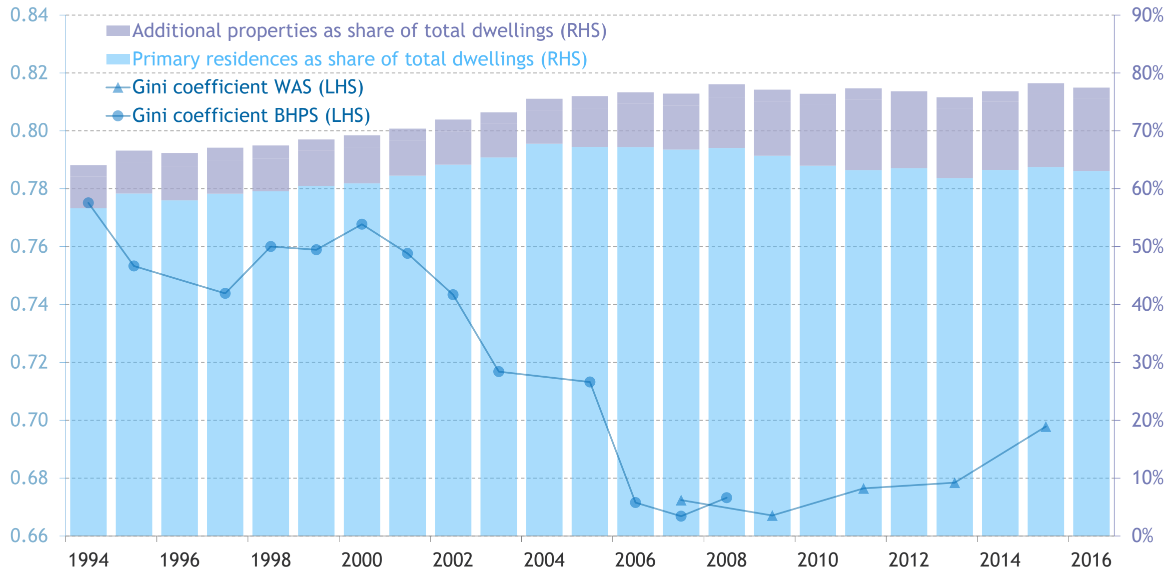
It is worth reflecting carefully on what sits behind this picture. It may seem paradoxical that the Gini coefficient fell during an era of rapidly rising house prices, a trend which on its own should have driven up housing wealth inequality. Just as surprisingly, the Gini began to rise post-2008 despite the fact that house prices first fell and then grew only slowly in Scotland after this point. In fact, for an explanation of housing wealth inequalities over time it seems we have to look less to price trends, and more at the ownership of private housing stock.

In Figure 10 we set the Gini coefficient against the share of all dwellings in Scotland that are in private hands. Critically, we distinguish between the stock held as the primary residence and that which is additional property.[10] This shows that in 1994, 56 per cent of all dwellings in Scotland were primary residences, a figure that rose to a peak of 67 per cent by 2008 as home ownership rates in Scotland expanded. By reducing the share of families who have no property wealth at all, rising home ownership had an equalising effect on the distribution of housing wealth. From 2008 onwards, however, the picture changes. By 2015 a larger part of housing stock was held as additional properties. By concentrating ownership, this trend acts to drive up housing wealth inequalities.

[10] We use the expression 'additional property' throughout this report to indicate any dwelling that is held by a family unit which is not the primary residence. This therefore includes any second or additional homes used for the family's sole use, a dwelling rented out privately to other family units, and the hybrid category of properties held for both own use but also sometimes let out to others on a short term basis. It would not include, however, the short-term let of the primary residence.

Figure 10: Additional property ownership has increased since 2008, driving up housing wealth inequality

Gini coefficient of net family housing wealth per adult over time & composition of private housing stock: Scotland, 1994-2016



Source: RF analysis of ISER, *British Household Panel Survey*; ONS, *Wealth and Assets Survey;* ONS, Labour Force Survey 1994-2018; Scottish Government, Empty property and second home web tables.

Put differently, and in the same terms we employed in Section 1, when it comes to explaining why housing wealth inequalities have changed over time the stock effect looks to be more important than the price effect (the opposite, of course, to what we found to be the case when we looked at the growth of overall housing wealth).

Those in the top income decile hold an increasingly large share of Scottish housing wealth

It is unsurprising that a household's level of wealth should correlate with their level of income; after all, one of the main ways in which a household accumulates wealth is by saving part of their income over a period of time. It is nonetheless striking that housing wealth per adult should vary so considerably by household income. Figure 11 splits all families in Scotland into ten evenly-sized deciles according to their income in 2014-16. This exercise shows that the top 10 per cent have around 3.4 times as much housing wealth as those in the middle of the distribution, holding in total 30 per cent of all housing wealth in Scotland today. Moreover, comparing the median and mean within deciles is also instructive as this shows that wealth within each decile is also top-loaded.

Figure 11: Housing wealth is skewed towards the highest-income households

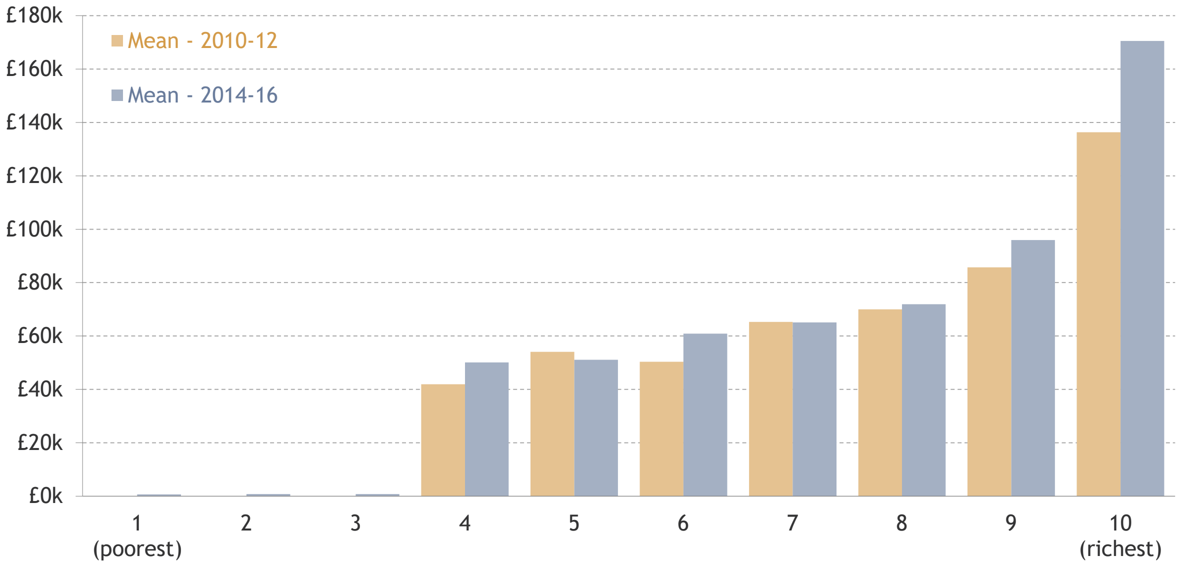
Average net family housing wealth per adult, by Scottish household net income decile: Scotland, 2014-16 (CPIH-adjusted to 2018-19 prices)

Source: RF analysis of ONS, *Wealth and Assets Survey*

In Figure 12 we look at how the distribution of housing wealth by income deciles has changed over time. In just a short period we can see how more housing wealth has come to be held by those at the very top of the income distribution. In 2010-12 those in the top decile held on average 2.5 times as much wealth as those in decile 5, compared to the 3.4 times we have noted in 2014-16.

Figure 12: The distribution of housing wealth has become more top-heavy over time

Average family net property wealth per adult, by Scottish net income decile over time: Scotland (CPIH-adjusted to 2018-19 prices)



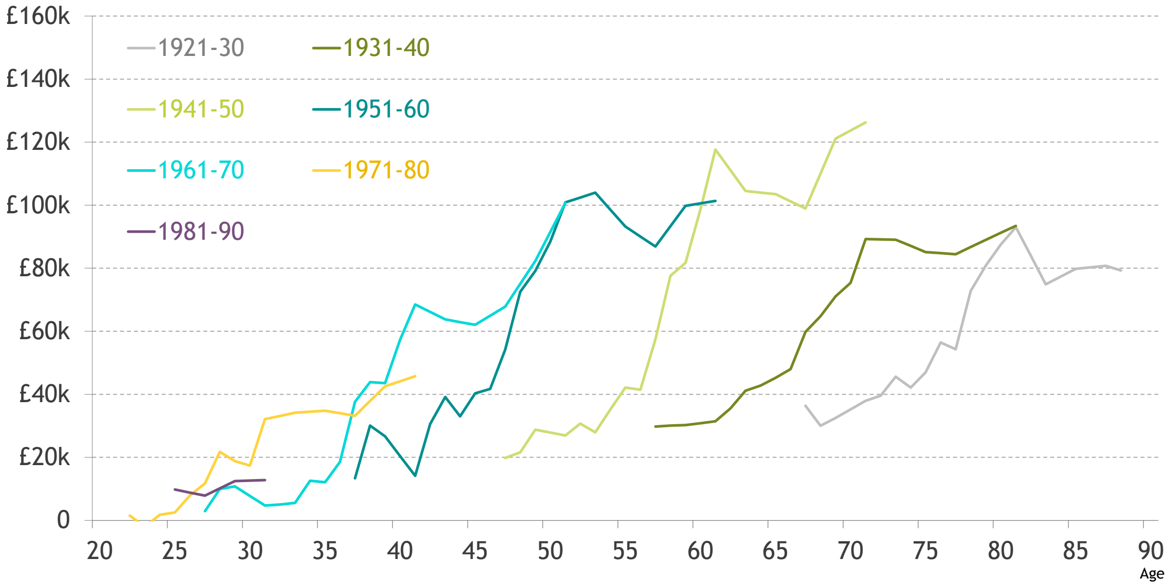
Source: RF analysis of ONS, *Wealth and Assets Survey*

Young people today hold less housing wealth at the age of 30 than their predecessors

Just as it is unsurprising that those with higher incomes hold larger amounts of housing wealth so, too, it is to be expected that older people will be wealthier simply by virtue of having accumulated wealth over time. Comparing young people's housing wealth with that of older people in the here and now is not very revealing. What is, however, is looking at how much housing wealth different birth cohorts hold at the same point over the life course, a picture we present in Figure 13. This shows us that today's young people (here defined as those born between 1981 and 1990) hold significantly less property wealth at the age of 30 than those born in the previous ten-year period did at the same age.

Figure 13: Cohorts born since the 1950s are falling behind their predecessors in terms of property wealth holdings

Mean real family net property wealth per adult, by 10 year birth cohort: Scotland, 1993-2016 (CPIH-adjusted to 2018-19 prices)



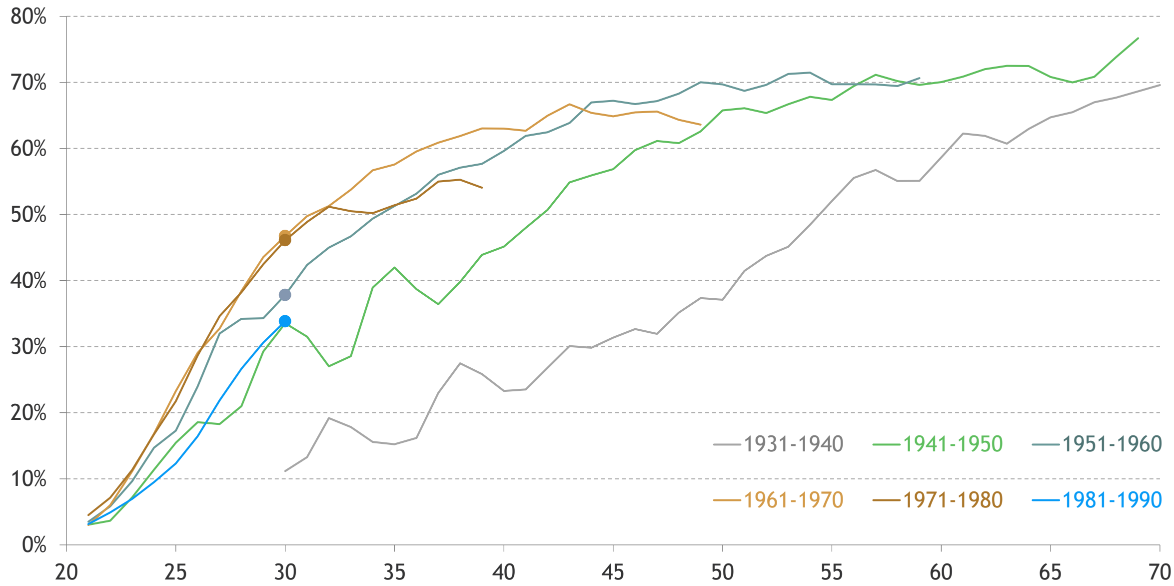
Source: RF analysis of ISER, *British Household Panel Survey*, *Understanding Society;* ONS, *Wealth and Assets Survey*

That said, Figure 13 also shows that it is not only younger people who hold less property wealth in Scotland today than their predecessors did at the same age: the inflation-adjusted value of the housing held by those born between 1971-80 and 1961-70 has dipped below that of the earlier birth cohort for example. The sharp downturn in housing wealth that we can see all cohorts have experienced is clearly linked to Scottish house price trends since 2008. But for a full explanation of intergenerational housing wealth inequalities we once again need to look at how property ownership has changed over time.

In Figure 14 we set out the home ownership rates of families by birth cohort and age. As this makes clear, 35 per cent of families headed by someone born 1981-90 owned their home by the age of 30, compared to almost half of those born 1961-70 and 1971-1980 at the same age. While some of the gap between cohorts may be explained by changing norms (for example, young people today stay in education longer, partner more often and have children later than previous generations, all of which could change the preferences for home ownership), it is also patently clear that rising house prices which have driven up property wealth over time have also acted to lock many young people out of home ownership.[11]

Figure 14: Millennials born in the 1980s have fallen behind their predecessors when it comes to home ownership

Proportion of family units owning a primary residence, by 10 year birth cohort 1961-2018



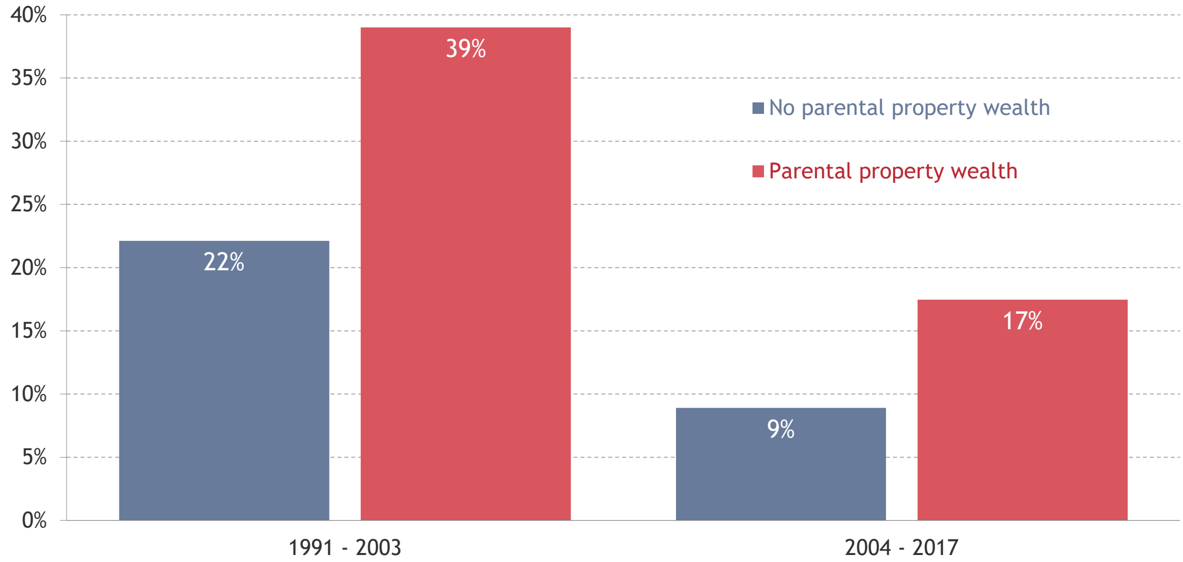
Source: RF analysis of ONS, *Family Expenditure Survey 1961-1983*; *Labour Force Survey 1984-2018*

There is one other way in which it is interesting to think about intergenerational housing wealth inequalities, and that is to consider how parental wealth is linked to younger people's prospects of becoming property owners. At the UK level, previous Resolution Foundation work has shown that help from family to purchase one's first home has become more important over time, even when we control for personal characteristics, such as income and education.[12] While data constraints mean we cannot repeat the exercise fully for Scotland only, Figure 15 suggests that, while young people without the back-up of parental property wealth have always been less likely to become home owners themselves in Scotland, today their chances are somewhat slimmer compared to their more fortunate peers.

[11] In A Corlett and L Judge, Home affront: housing across the generations, Resolution Foundation September 2017 we estimate that changing preferences explain around one third of the difference we observe between the UK home ownership rates of 30 year olds in 1984 and 2016, leaving us to ascribe two-thirds of the gap to the growing unaffordability of a first home.
[12] S Clarke & J Wood, House of the rising son (or daughter): the impact of parental wealth on their children's homeownership, Resolution Foundation December 2018.

Figure 15: Young people's probability of home ownership has become more closely correlated over time with their parents' property wealth

Home ownership rates of people aged 30, by parental property wealth: Scotland, 1991-2017



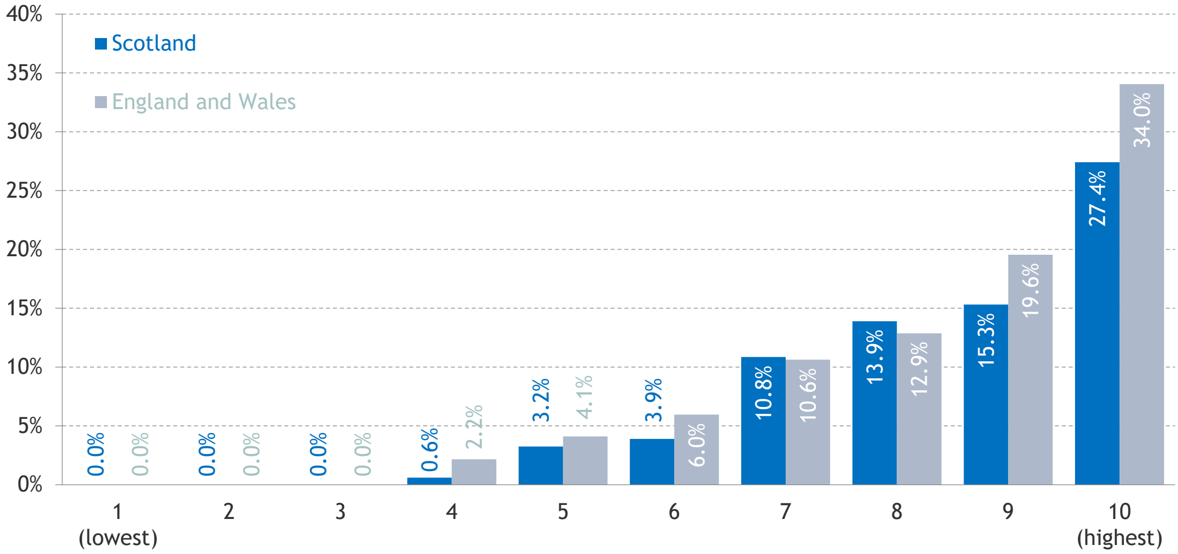
Source: RF analysis of ISER, *British Household Panel Survey and Understanding Society*

Additional properties are overwhelmingly the preserve of high-income families in Scotland

It is worth looking closely at the age and income profile of those who hold additional homes given the important role the growing number of such properties has had in driving up overall wealth inequality. In Figure 16 we set out the proportion of adults in each income decile who have some additional property wealth, comparing the distribution across families in Scotland with that of families in England and Wales. As one would expect, the likelihood of having (an) additional home(s) vastly increases as income rises. Additional property ownership in the top fifth of the household income distribution is higher in England and Wales than it is in Scotland.

Figure 16: In Scotland, additional property wealth holdings are less clustered among the highest-income households than in England and Wales

Proportion of adults living in family with additional property wealth, by Scottish and English/Welsh household income deciles, 2014-16



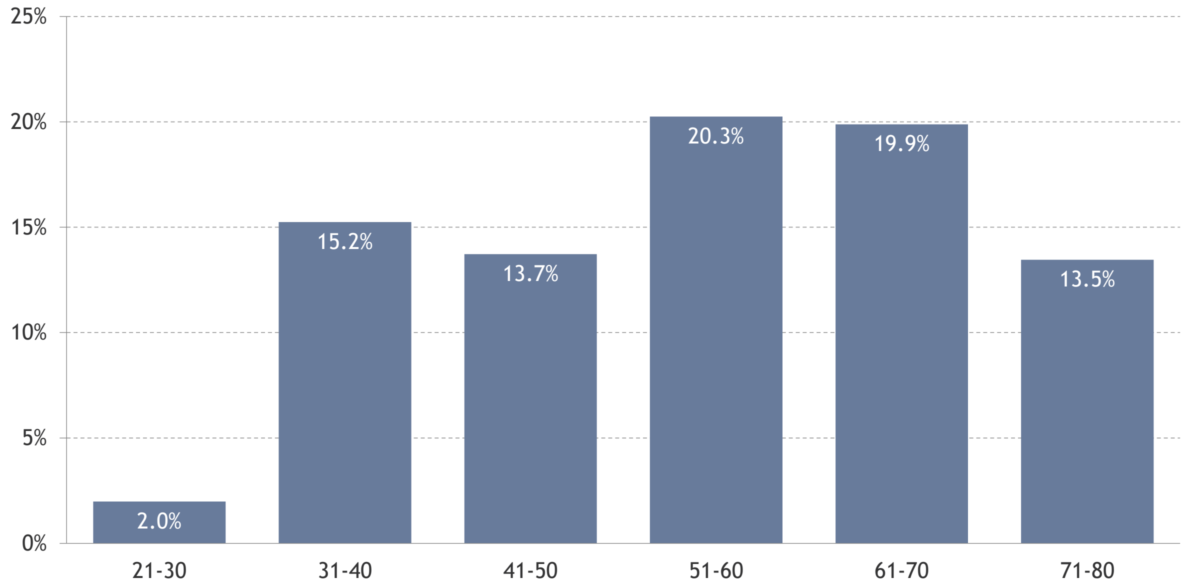
Source: RF analysis of ONS, *Wealth and Assets Survey*

An interesting follow-up question to ask is how far the distribution of additional properties across the income spectrum arises because higher income people are likely to be older and hence to have had more time to acquire additional properties? Figure 17 suggests that the distribution of additional properties is less skewed by age than one might expect. In 2014-16, in Scotland, those aged between 51-60 were most likely to own additional property, with those aged 61-70 close behind. But younger age bands do not lag that far behind. Indeed, the conclusion from recent analysis of Britain-wide trends is that wealthier members of younger cohorts are matching their predecessors' levels of additional property ownership, even as their levels of main home ownership have fallen.[13] At age 29, for example, 37 per cent of British people born in the 1980s owned some property wealth, compared to 50 per cent among people born in the 1960s at the same age. But the rate of additional property ownership, by contrast, was the same for both groups, at 7 per cent.

[13] G Bangham, Game of Homes: the rise of multiple property ownership in Great Britain, Resolution Foundation, June 2019.

Figure 17: Additional property ownership is highest among people aged in their 50s

Proportion of adults living in family with additional property wealth, by age group: Scotland, 2014-16



Source: RF analysis of ONS, *Wealth and Assets Survey*

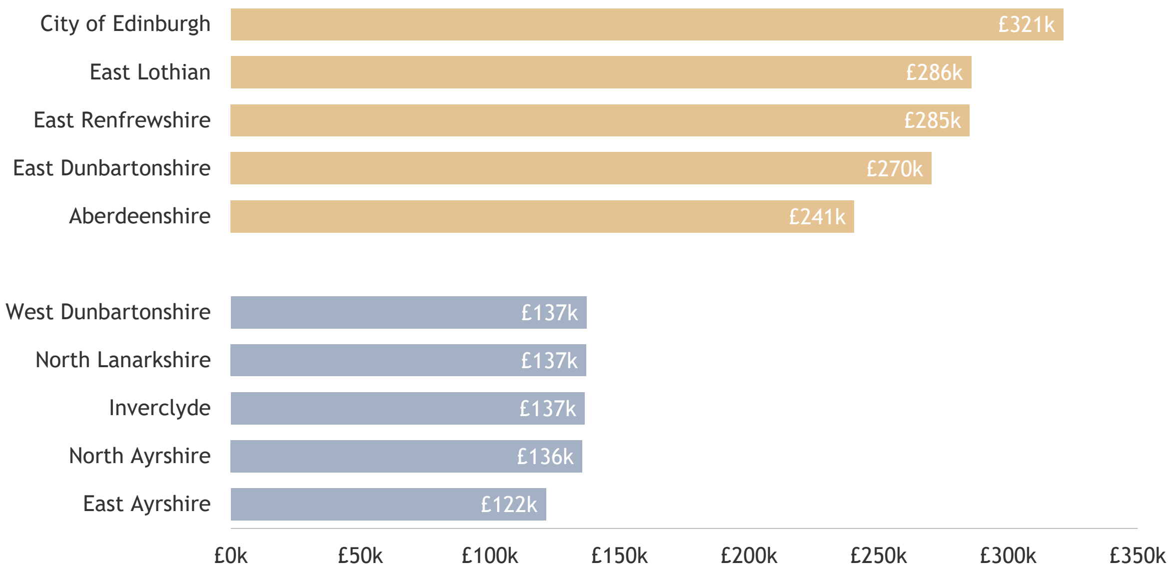
Housing wealth inequalities between different parts of Scotland are substantial, but have declined in recent years

A family's housing wealth is determined not just by income and age, but also by where within Scotland any property they hold is located. In Figure 18 we show how large a difference this can make by presenting the average value of a residential dwelling in the five local authorities in Scotland with the highest house prices, and the five with the lowest.[14] Unsurprisingly, Edinburgh is where the most valuable housing stock is located: the average unit is worth more than 2.5 times as much in the capital as in East Ayrshire.

[14] Due to data limitations, the values we present here are gross.

Figure 18: Significant house price differentials exist across Scottish local authorities

Top and bottom five local authorities by gross value of average residential dwelling, 2018



Source: RF analysis of ONS, *UK House Price Index*

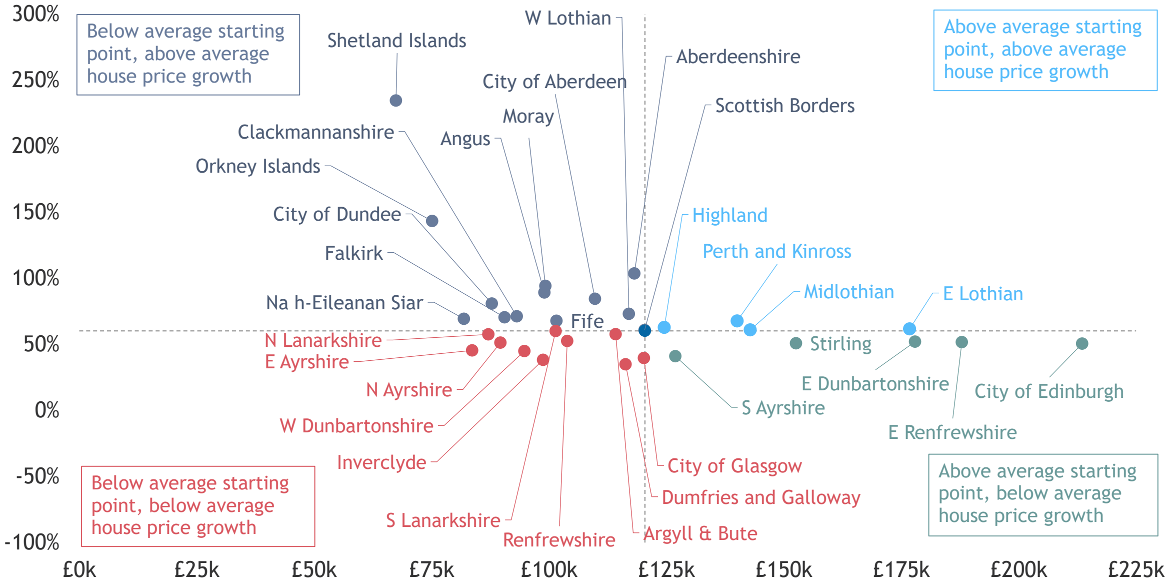
Of course, in higher value areas families may need to take out larger mortgages to be able to become property owners, and their net housing wealth will be affected accordingly. However, house price inflation will increase the equity held in a property, thereby improving the net wealth position of a family even if heavily leveraged. As a result, we would expect housing wealth inequalities between local authorities to increase over time if high value areas experience faster house price growth than areas where the housing stock is cheaper. So has this indeed been the case in Scotland in recent years?

In Figure 19 we plot 2004 house prices against the rate of house price change observed up to 2018 for every local authority in Scotland to explore this point.[15] In fact, as the chart shows, higher value areas (in 2004 prices) were largely not the areas to experience higher than average house price growth over the past 14 years. Indeed, with the exception of some runaway local authorities, such as the Shetland and Orkney Islands (and to a lesser extent, Aberdeenshire), there has been less deviation of house prices from the Scottish average than perhaps popular accounts lead one to expect. As a result, while it is clear that housing wealth inequalities exist between areas given the large differentials in unit value, we conclude that the price effect at least has not driven these up in recent years.

[15] House price data is not currently available at local authority level in Scotland before 2004.

Figure 19: Lower priced areas have played 'catch up' with higher priced areas over time

Average house price (2004 values) and rate of growth (2004-2018) by local authority

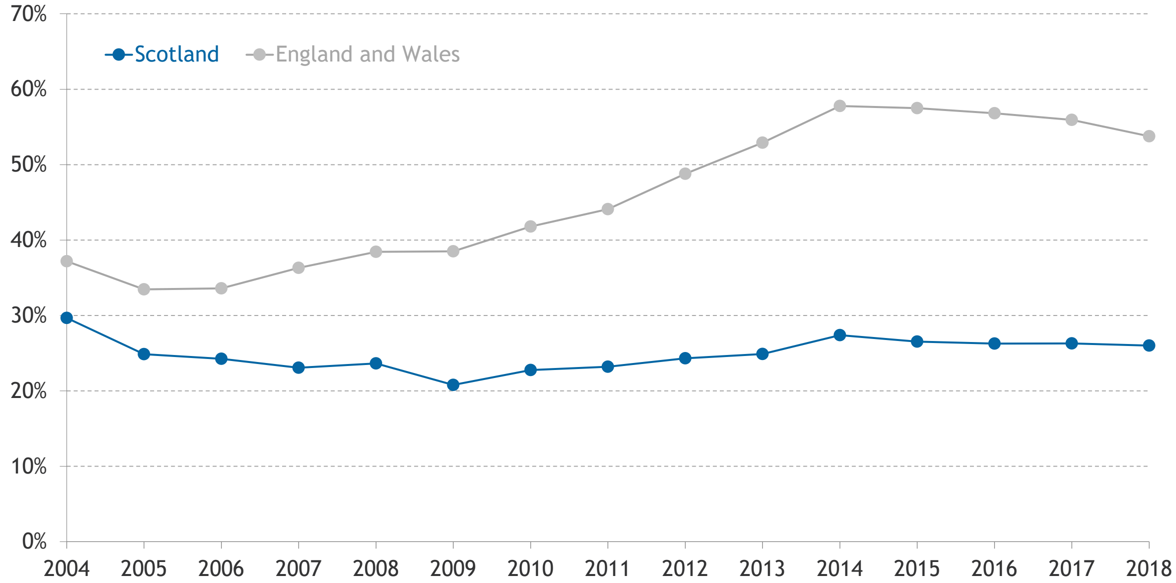


Source: RF analysis of ONS, UK House Price Index

In Figure 20 we show this more formally by presenting the coefficient of variation for house prices across Scottish local authorities, with the fall from 2004 indicating that the range of average house prices at the local level has fallen over time. Interestingly, this looks to have been largely a pre-crisis phenomenon when overall house prices were experiencing their most dramatic growth; post-crisis, the variation across local authorities has grown only slightly. In this respect Scotland looks quite different from England and Wales where the coefficient has grown markedly over the past 14 years, an effect that on its own would drive up housing wealth inequalities between areas.

Figure 20: Variation in house prices across local authorities has reduced in Scotland, in contrast to the rest of Great Britain

Coefficient of house price variation between local authorities



Source: RF analysis of ONS, *UK House Price Index*

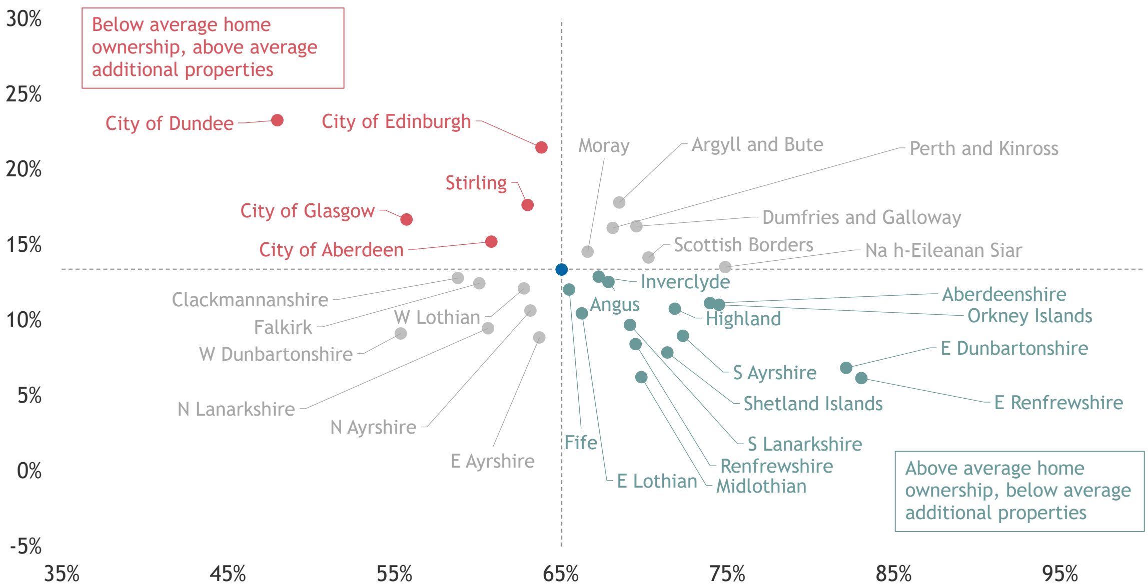
Scottish cities have the least equally distributed housing wealth

Finally, another way to look at the effect of place is to compare prices at a lower geographic level, comparing how prices vary vertically (that is, within local authorities) rather than horizontally (between local authorities). While data limitations constrain our ability to put headline figures on inequality of this nature we can use our data about the distribution of the housing stock in each local authority to examine this issue.

We have shown previously that rising rates of primary residence ownership are inequality-reducing (because more families become 'haves' rather than 'have-nots'), while rising rates of additional property ownership have the opposite effect (because housing wealth becomes concentrated in fewer families' hands). In Figure 21 we plot both the primary residence and additional property ownership rates for each local authority, an exercise which allows us to draw some conclusions about the areas in Scotland where the highest and lowest vertical housing wealth inequalities are most likely to be found.

Figure 21: There are five cities where housing wealth is especially bunched

Share of stock held as primary residence (horizontal axis) and additional property ownership (vertical axis) by local authority, 2018



Source: RF analysis of ONS *Labour Force Survey 2018* & Scottish Government, *Empty property and second home web tables*

To begin, we can confidently say that local authorities in the upper left quadrant of our chart, such as the cities of Dundee, Edinburgh and Glasgow, will have the highest levels of vertical housing wealth inequality by virtue of their below average ownership rate but above average additional properties rate. Likewise, those in the lower right quadrant like East Renfrewshire and East Dunbartonshire will have the lowest vertical inequalities because they are the areas where the housing wealth is most widely shared. While we can be less conclusive about the distribution of housing wealth in the other two parts of the chart, it is plausible that places in the top right quadrant will have lower levels of inequality than those in the bottom left given their higher rates of home ownership.

To conclude, in this section we have explored housing wealth inequalities across four key domains: people, income, age and place. We have seen how, in many respects, the Scottish story is a positive one: the expansion of home ownership has driven down housing wealth inequality over time. So are worries about housing wealth inequality misplaced? The recent uptick in the Gini coefficient suggests not, and in the next section we turn to explore in more depth why policy makers are right to be concerned.

Section 3

Policy and housing wealth

Holding wealth in any form has multiple benefits for the individuals concerned. The evidence suggests, for example, that those with assets are able to take more risks which often come with rewards, have higher wellbeing and a higher propensity to spend their income than those without.[16] But owning property has value over and above these general wealth effects in that it can also provide a secure home (in the case of the primary residence); a source of income (in the case of additional properties that are then rented out); and a hedge against increasing housing costs in later life.

Given this, it is not surprising that policy makers in the UK have taken a largely positive view of housing wealth accumulation over time. From Right to Buy in the 1980s, through to Help to Buy today, enabling families to become housing wealth 'haves' has been an enduring political objective. However, in recent years, a number of concerns about the growth and distribution of housing wealth have also come to the fore. To begin, anxieties have emerged simply about the scale of housing wealth growth: between 1994 and 2017, for example, the real value of Scottish housing wealth grew by more than 350 per cent, compared to 151 per cent for real incomes. But beyond this, we identify three reasons why distributional concerns about housing wealth have also grown in recent years.

Those without property wealth are more likely to experience housing 'stress'

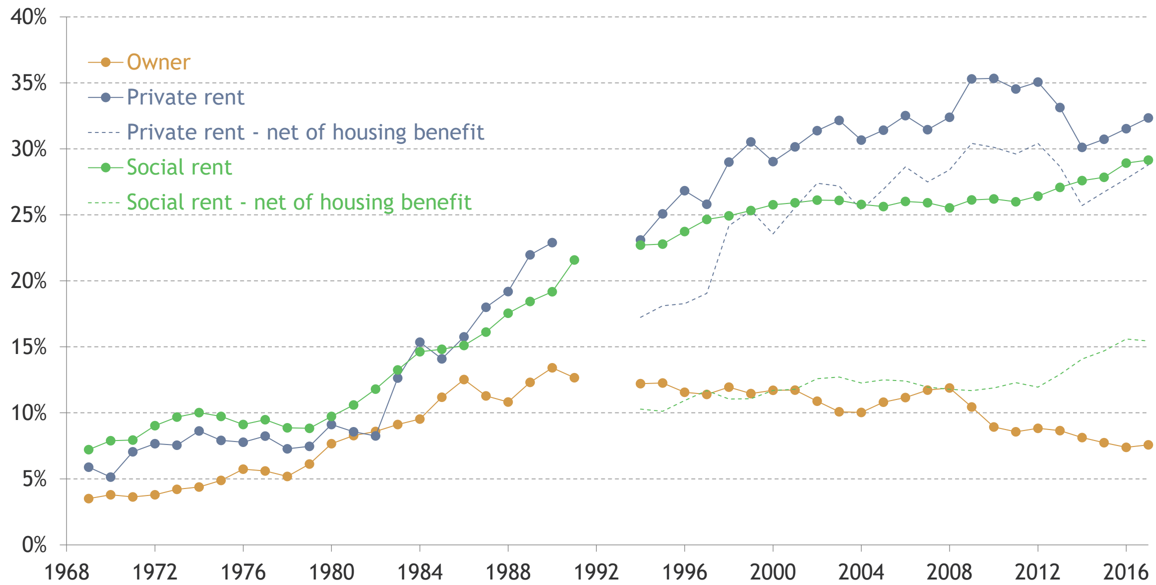
The rising levels of housing wealth are thrown into sharp relief by the growing number of families struggling to find affordable (or indeed any) homes in Scotland today.[17] In Figure 22 we show how the share of income spent on *ongoing* housing costs has changed over time, comparing the fortunes of those who hold property wealth (owners) with those who do not (renters).[18] As this makes clear, renters have always needed to spend more of their incomes on housing than owners but until the mid-1980s all groups saw their housing cost to income ratio increase at broadly the same rate.

[16] For a comprehensive overview of the literature on wealth effects including accounts that dispute the benefits see the sister paper to this report, A M Soaita, K Gibb and D Maclennan, *Housing Wealth Inequalities in Scotland: An Evidence Review*, Scottish Poverty and Inequality Commission, June 2019.
[17] According to the latest statistics, there were close to 19,000 applications for homelessness assistance between April and September 2018, 2 per cent higher than the same 6 month period in 2017. See Scottish Government, Homelessness in Scotland: update to 30 September 2018, January 2019.
[18] We exclude the principal repayment from housing costs of owners in our analysis here as it is more properly treated as the accumulation of an asset.

From this point on, however, the experience of those with and without property wealth has diverged. Owners enjoyed a period when their housing costs have been relatively stable as a share of income up to 2008, since when very low interest rates have served to drive down the amount they spend servicing their mortgages. In contrast, both social and private renters have experienced a dramatic increase in their housing-cost-to-income ratio during a period when income growth have been weak. Today, those living in the social-rented sector spend close to 30 per cent on their income on housing costs (although housing benefit then takes a large part of the strain, reducing the burden borne by the families themselves to 15 per cent). Private renters in Scotland spend even more, averaging nearly 33 per cent of their incomes on rent, a figure that is widely regarded as the point at which housing is deemed 'unaffordable' (and housing benefit ameliorating the situation for this group to a far lesser degree).[19]

Figure 22: Renters are spending close to an unaffordable share of their income on housing costs today

Proportion of family income spent on housing costs (two-year rolling average): Scotland, 1968 to 2018



Notes: Owners' housing costs excludes principal repayment
Source: RF analysis of Family Expenditure Survey 1968-1991; Family Resources Survey 1994-2018

[19] See for example The Smith Institute, *Defining and measuring housing affordability: an alternative approach*, Affordable Housing Commission June 2019.

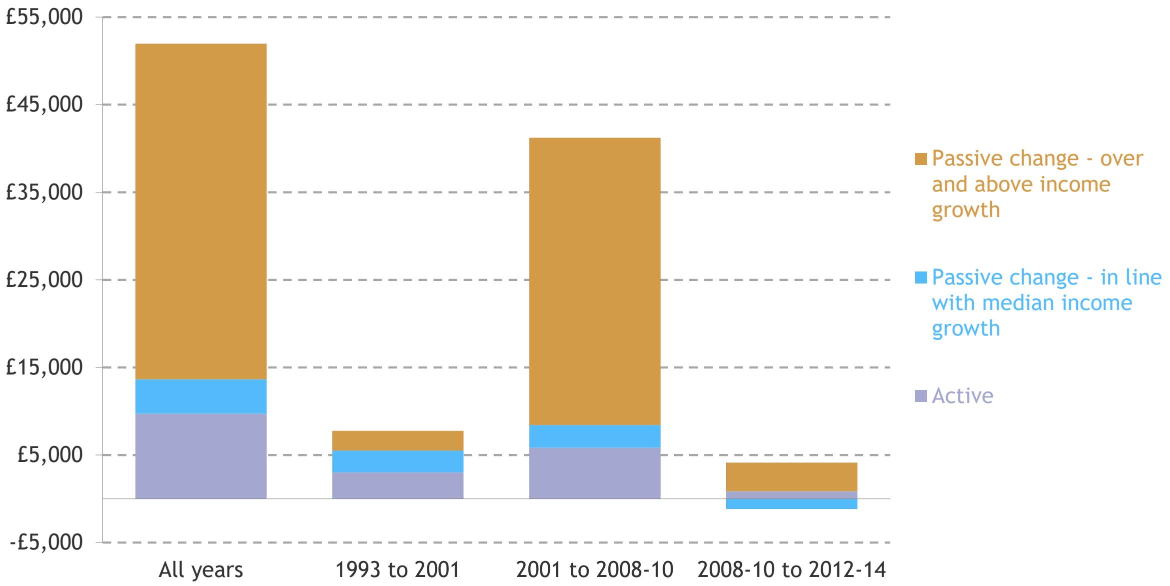
The majority of housing wealth gains in Scotland have been 'passively' acquired

Another reason why many find the growth in housing wealth increasingly problematic could be that much of the gain that has accrued to housing 'haves' over time stems from the long-term increases in house prices we documented in Section 1.

We explore this more fully in Figure 23. Here we distinguish three sources of housing wealth growth between 1993 and 2012-14. To begin, we note that property wealth has grown as a result of 'active' behaviour on a family's part: paying off the mortgage, for example, or building an extension which adds value to the home. Second, we know there is a reasonable expectation that house prices will increase over time in line with median incomes and therefore we distinguish the uplift resulting from that effect. But third, and as the chart makes clear, more than 70 per cent of the change in average property wealth per adult in Scotland over the past 25 years has resulted from house price growth over and above income growth – with the scale of this 'passive' change being largely dependent on luck (of where a family owns and - as the chart makes very clear - when they bought).

Figure 23: Close to three-quarters of the housing wealth gains since 1993 have come from house price growth over-and-above incomes

Change to average family net property wealth per adult: Scotland, 1993 to 2012-14



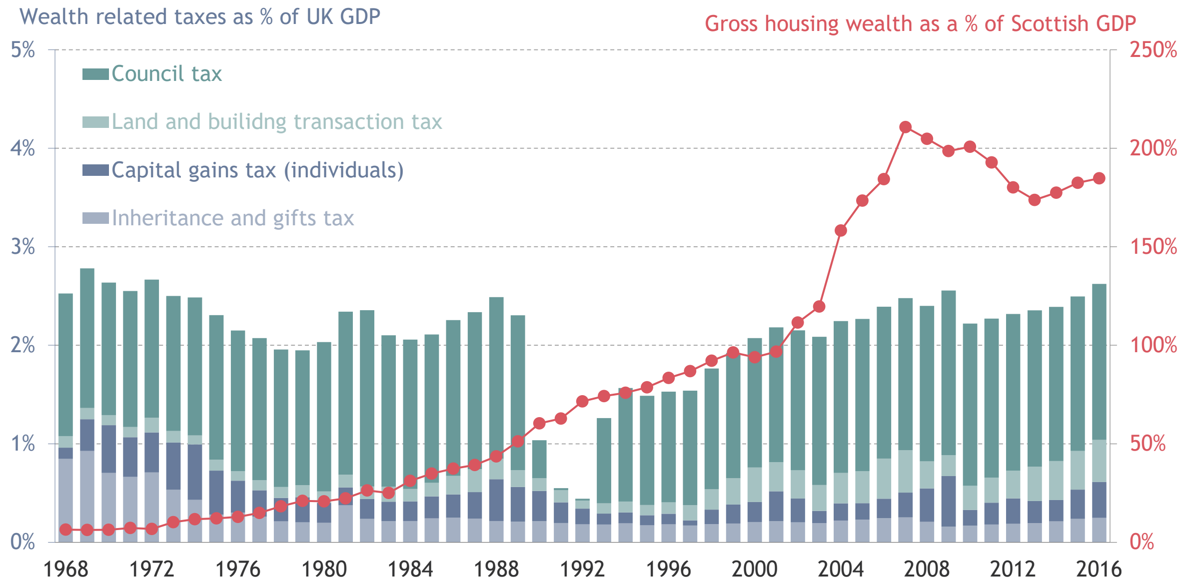
Source: RF analysis of ISER, *British Household Panel Survey, Understanding Society*; ONS, *Wealth and Assets Survey.*

Property taxation has not kept pace with rising housing wealth

Despite the scale of these windfall gains, housing wealth has become ever more lightly taxed over time. In Figure 24 we show that, with the exception of the Poll Tax period, the tax take from property wealth has changed very little as a percentage of GDP over time (although the amount raised from different property taxes has shifted somewhat). In stark contrast, and it is worth really noting the scale of the two axes, the value of housing wealth in GDP terms has increased dramatically in Scotland over the past half century.

Figure 24: While the tax take from housing stands at less than 3 per cent of GDP, net housing wealth is worth close to 200 per cent

Aggregate housing wealth and wealth-related taxes as a proportion of GDP, 1968-2018



Note: Legend refers to the tax's current name
Source: RF analysis of ONS, Family Expenditure Survey 1961-1983; Labour Force Survey 1984-2018; & UK house price index & OECD statistics

Moreover, the failure of taxation policy to keep up with rising housing wealth reinforces key housing market challenges: for example, there is little disincentive to over-occupy. It is no surprise, then, that policy makers increasing feel that there is a strong case for reconsidering the approach to taxing housing wealth. In Box 3, we overview how the Scottish Government has engaged with, and taken action on, the issue to date.

Box 3: Tackling housing wealth inequalities in Scotland

Scotland has engaged with the question of housing wealth in recent years, not least because it has powers over some types of taxation as part of devolution. In 2015, for example, the Government introduced a new Land and Building Transaction Tax (LBBT) with steeper rates for higher value properties than its predecessor stamp duty.

Even more significantly, in 2015 the Scottish Government set up a cross-party Commission on Local Tax Reform to consider action to improve both the progressivity and revenue raising power of Council Tax. In 2017, in response to the Commission, the Scottish Government made a welcome move and raised the rate of Council Tax levied on higher-value properties. However, action only went so far: Council Tax continues to be based on the 1991 value of properties in Scotland despite widespread recognition that house price inflation since that point has vastly increased the potential tax base.

The accumulation and taxation of housing wealth remains a live issues in Scotland: the 2019-20 Budget was passed with Green support in exchange for the SNP promising cross-party talks on replacing Council Tax. Moreover, in its National Performance Framework, the Scottish Government has indicated its wish to pursue policies consistent with long term stable house prices and a reduction in dependence on housing as an asset.

Action to support entry into home ownership needs careful calibration

One obvious way that policy makers could respond to growing housing wealth inequality is by intensifying action to help those currently locked out of home ownership become property holders. For example, they could extend the scope of the Help to Buy (Scotland) scheme by increasing the price caps or allowing it to be used for all properties rather than just new-build ones (or ration it just to those who are first-time buyers). However, recent studies of the Help to Buy programme in England suggest caution may be in order: the (more generous) English scheme has a considerable deadweight, and has driven up house prices in areas where there is already high demand.[20]

In this context, it is instructive to think through how the lower home ownership rates of today's young people may evolve in the absence of policy intervention. At a UK level, previous Resolution Foundation work has shown that a return of the conditions that prevailed during the decade of strongest home ownership growth in the past 50 years would enable young people to 'catch up' eventually with most previous birth cohorts in

[20] See, for example, National Audit Office, *Help to Buy: Equity Loan scheme - progress review*, NAO June 2019 and F Carozzi, C Hilber and X Yu, *The economic impacts of Help to Buy*, UCL presentation June 2018.

the home ownership stakes.[21] Conversely, if the underlying conditions we saw during the decade with the slowest home ownership growth were to hold sway, no more than half of young people today would be owners by the age of 45 (with the assumption being that they will find it a challenge to get on the housing ladder thereafter).

It is worth noting, however, that young people in Scotland may have some particular tailwinds when it comes to home ownership: house prices fell by 0.2% between April 2018 and April 2019, for example, plus the population is projected to grow only slowly over the coming decades putting less pressure on supply. On the other hand, there are some Scotland-specific headwinds to consider as well. Whatever one's view on its broader social impact, Right to Buy has in the past had an accelerator effect on home ownership rates; its demise in Scotland may, therefore, act as a brake on future rates to some extent.

Arguably, a better approach to supporting home ownership would be to rebalance demand for housing in the interests of first-time buyers through better use of the tax system. Given that Council Tax is the most significant tax on housing in Scotland in terms of revenue (as Figure 24 makes clear), is the only property tax that is paid on a recurrent basis, and, of course, is fully devolved, it is to this topic that we now turn.

Council Tax has increasingly come to resemble the Poll Tax it replaced

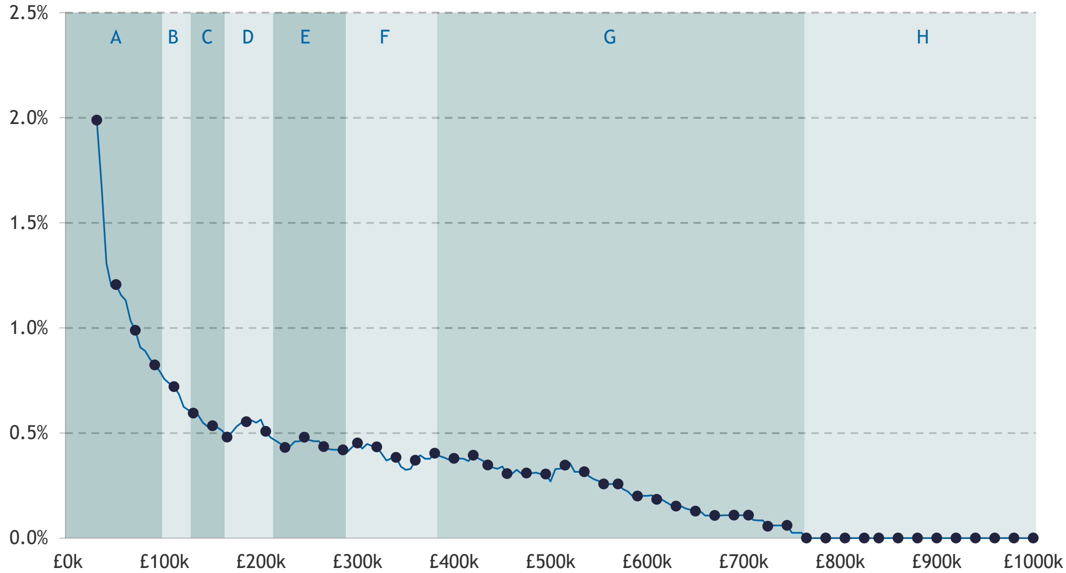
With Scotland ahead of the game compared to England when it comes to local taxation, is the status quo really that bad? In fact, despite the recent changes to Council Tax in Scotland it remains regressive both in terms of property values and family incomes.

In Figure 25 we plot Council Tax across each band expressed as a share of the property value. This shows that the highest tax rates are faced by the occupants of the lowest-valued properties: those in the cheapest properties face a Council Tax bill amounting to as much as 2 per cent of the value of their property each year, compared to just a miniscule share of the property value for those in Band H. Moreover, it is important to note that Council Tax liability sits with the resident, not the owner, of a property.

[21] A Corlett and L Judge, Home affront: housing across the generations, Resolution Foundation September 2017.

Figure 25: Council tax is poorly related to property values in Scotland despite recent changes

Council Tax as share of property value by Council Tax bands, 2016-17



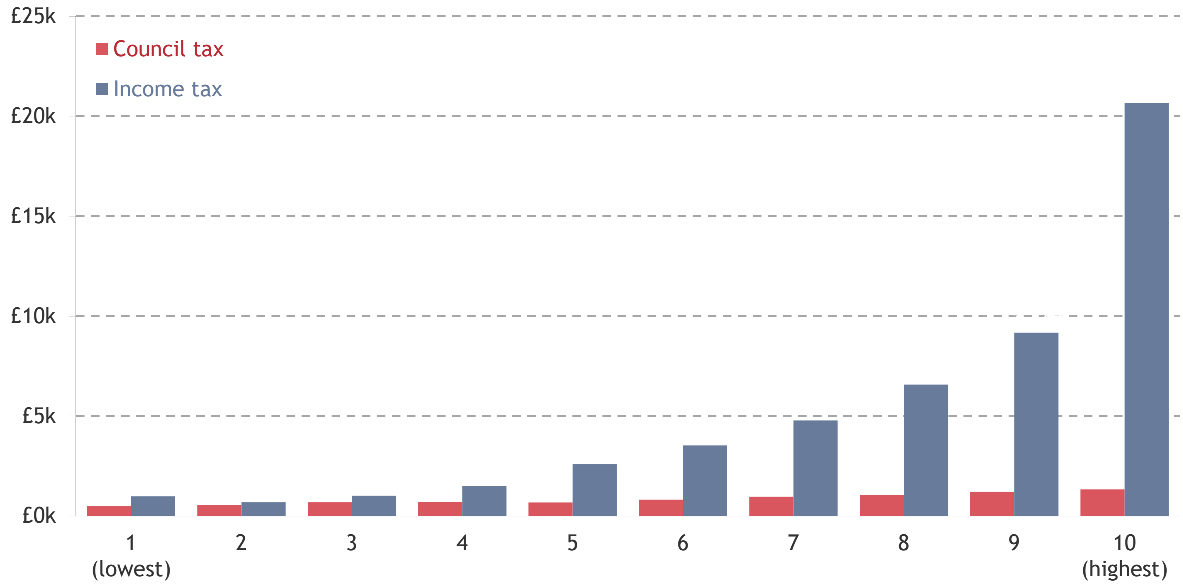
Source: RF modelling based on data from ISER, *Understanding Society*

Comparing Council Tax with the average amount of income tax paid by households in each income decile is also instructive. Figure 26 shows that the lowest amount of Council Tax in cash terms is indeed paid by households in the lowest income decile, largely because of the important reliefs they receive.[22] But unlike income tax which is progressive, Council Tax is remarkably flat right across the distribution. In fact, those in the top decile pay only 2.4 times as much as those in the second decile, compared with income tax where the richest households pay more by a factor of 30-plus.

[22] We note here that compared to England, Scotland has a more generous and nationally administered Council Tax reduction scheme.

Figure 26: Council tax is highly regressive especially compared to income tax

Average household Council Tax and income tax liability by income decile, 2016-17



Notes: Income tax data is UK
Source: ISER, *Understanding Society* & ONS, *Effects of Tax and Benefits, 2016/17*

Four options for Council Tax reform

There is ample scope, then, to improve the progressivity of Council Tax as well as recalibrate its relationship with property values in Scotland today. So what options could be considered? We set out the impact of four possible reform scenarios as follows:[23]

- Working within the bounds of the existing system, revalue properties to current value and tax higher value properties at a marginally higher rate ('Revaluation-plus');

- Replace Scottish Council Tax with a progressive property tax based on up-to-date property values, with a tax-free allowance so that the lowest-value tenth of properties in each local authority pay no tax, and multiple tax bands ('Fully progressive');[24]

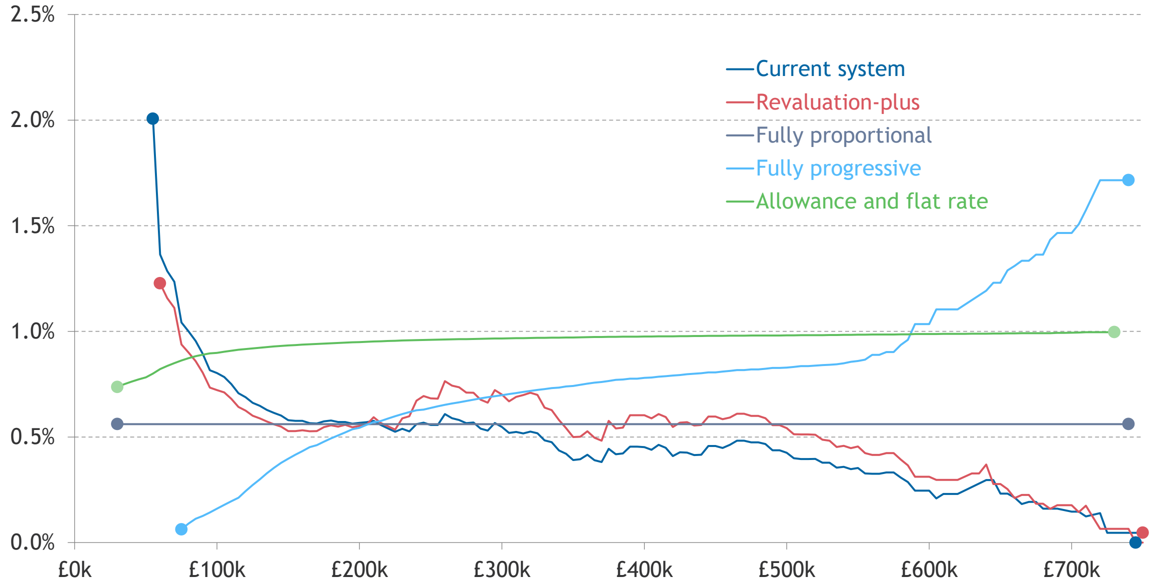
[23] See Annex 2 for more details of each reform specification. In each of the scenarios modelled we assume that the existing Council Tax Reduction scheme providing assistance to households on low- and middle-incomes is retained.
[24] For more details of this option, see A Corlett and L Gardiner, Home affairs: options for reforming property taxation, Resolution Foundation March 2018. In this report we make a small change to the previous Resolution Foundation proposal to reflect the fact that we are looking at Scotland-only policy changes: we model a tax of 0.89 per cent of the value of residential properties, with a tax-free allowance equal to the 10th percentile of Scottish property values, and a surcharge of 1.5 per cent on the portion of the value of any property that exceeds the 90th percentile of Scottish property values.

- Introduced a proportional property tax of one per cent on all properties, with a £10,000 tax-free allowance for every home as currently advocated by the Scottish Green Party ('Allowance and flat rate');
- And finally, as a thought experiment and useful comparator, consider a flat rate annual property tax set at just over 0.5 per cent for every property, a level which is broadly revenue neutral ('Fully proportional').

So how do each of these policy options compare? In Figure 27 we begin by looking at the way they stack up when it comes to the relationship between the tax they raise and the property value. The first thing to note is that each of the proposed options is preferable to the current system on this metric. However, while the revaluation option would be more efficient, it would not seriously address Council Tax's regressivity (indeed, the revenue neutral proportional tax would align Council Tax more closely with property values). Shifting local taxation onto a more progressive footing would require policy makers to go further, implementing a reform with a generous allowance for those in the lowest value properties, or the fully progressive option as set out above.

Figure 27: There is ample scope to levy Council Tax more proportionately to property values

Scottish Council Tax as share of property value under reform options, 2016-17

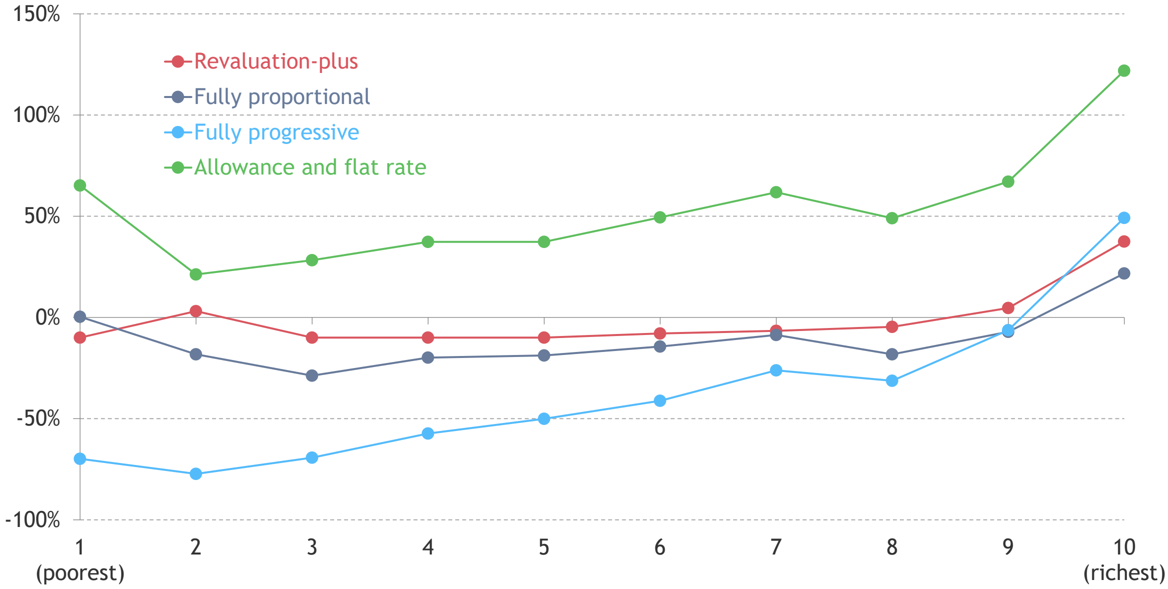


Notes: Modelling is conducted with data for calendar years 2016-17, but when modelling the 'current system' we assume that the higher rates of Council Tax levied on properties in bands E to H (actually introduced by the Scottish Government in April 2017) had been fully implemented throughout this period.
Source: RF modelling based on data from ISER, *Understanding Society*

In Figure 28 we now look at the impact of our four scenarios on Council Tax bills across the income distribution. As the Green Party itself acknowledges, their proposal would increase the amount of Council Tax paid very significantly for all income deciles – from 50 per cent for those in the lowest decile to 122 per cent for households in the highest. Under the other three scenarios only those in the top income decile would pay more tax. When it comes to the winners, as one would expect, the fully progressive model delivers the biggest gains for lower income households. What is interesting to note, however, is that a system where every property is taxed the same proportion of its value is marginally more progressive than the 'revaluation' proposal when assessed in this way.

Figure 28: Each of the reforms modelled would improve the progressivity of Council Tax

Percentage change in average household Council Tax bill under reform options, by Scottish net equivalised household income decile, 2016-17



Notes: Modelling is conducted with data for calendar years 2016-17, but when modelling the 'current system' we assume that the higher rates of Council Tax levied on properties in bands E to H (actually introduced by the Scottish Government in April 2017) had been fully implemented throughout this period.
Source: RF modelling based on data from ISER, *Understanding Society*

Of course, it would be wrong to underestimate the challenges that any government would face in implementing wholesale (or indeed more than marginal) reform of Council Tax. There would be many practical considerations: how to transition to a new system, for example, and how to protect asset-rich but cash-poor households from unreasonable bills. Likewise, a new tax which required an assessment of income such as the 'allowance and flat rate' or the 'fully progressive' options would require cooperation not only between the Scottish Government and local authorities, but also with HMRC and the UK Government.

Taxing property could reduce housing wealth inequalities through a range of channels

Taxing property more efficiently and equitably may be good objectives in their own right but what would be the effect on housing wealth levels and inequality that we documented in Sections 1 and 2? There are various but diffuse ways in which tax reform could operate to have an impact.

To begin, raising the cost of holding property would have a downward effect on prices which, in and of itself, would directly reduce the absolute gap between the housing 'haves' and 'have-nots'. It is worth noting, however, that an across-the-board reduction in the value of property would not affect the Gini coefficient in the first instance given that the relative distribution of wealth remains unchanged. That said, lower prices may make it easier for first-time buyers to purchase, extending home ownership which, as we have shown, has an inequality-reducing effect. And of course, reforms which tax higher-priced properties at a steeper rate would have a differential price effect across the distribution, reducing the Gini in the process.

What is less clear, however, is whether those with additional properties (held either for private consumption or for rent) would respond differently from primary residence owners under any of the options we explore. This is important given that, as we have noted before, all else being equal additional properties drive up housing wealth inequalities by concentrating the ownership of the dwelling stock. The Scottish Government is clearly alive to this issue – legislating in 2018 to end the automatic Council Tax discount given to those with second homes. But is there more that could be done?

Under the 'fully progressive' option, for example, it would be possible to offer only one tax-free allowance to each person, thereby effectively increasing the tax rate paid by those with additional properties. Alternatively, it would not be illogical to levy local property tax on owners rather than renters, making landlords rather than tenants liable. Such an option has its cons - it could risk undermining local accountability, for example, or landlords might simply pass on the cost via an increase in rent – but from a housing wealth inequalities perspective it is worthy of consideration.[25] Finally, given that the Land and Building Transaction Tax regime is also fully devolved, it is within the Scottish government's gift to take further action to disincentivise the purchase of additional properties through increasing the surcharge levied on such transactions still further.[26]

[25] Council tax as currently constructed clearly does function as a tax for local services as well as a property tax. However, it is worth noting that landlords do benefit from good local services if these are capitalised into the value of the property. See, for example, Department for Education, House prices and schools: do houses close to the best performing schools cost more?, Ad hoc research note March 2017.

[26] Given that the Smith Report unequivocally reserved all aspects of inheritance tax and capital gains tax to Westminster, there is currently little scope for the Scottish government to take policy action to address housing wealth inequalities using these two fiscal tools. However, elsewhere, we have proposed that capital gains on the primary residence should no longer be exempt on death (see L Judge and D Tomlinson, *Home improvements: Action to address the housing challenges faced by young people*, Resolution Foundation April 2018) as well as set out a proposal for the wholesale reform of inheritance tax (see A Corlett, *Passing on: options for reforming inheritance tax*, Resolution Foundation, May 2019).

Revenues raised from taxing property could be used to increase the security and wellbeing of those without housing wealth

Of course, the story does not necessarily end there. As well as improving the equity and efficiency of Council Tax, some types of reform would also raise additional revenue. In Figure 29 we outline the potential gains to the public purse under each of the scenarios we have modelled. With the proportional tax we have modelled set at a broadly revenue neutral level, it raises very little, but the other three options would bring in significant amounts of new money ranging from £0.3 billion a year under the 'revaluation' and 'fully progressive' options, to £1.5 billion a year if the 'allowance and flat rate' proposal were to be implemented.

Figure 29: Raising revenue through more efficient property taxation would enable the government to invest elsewhere

Revenue raised from Council Tax reform scenarios

		Net revenue
Current system		£2.1bn
Revaluation	Level	£2.4bn
	Change	*+£0.3bn*
Fully proportional	Level	£2.1bn
	Change	*+£0.0bn*
Fully progressive	Level	£2.3bn
	Change	*+£0.2bn*
Allowance and flat rate	Level	£3.6bn
	Change	*+£1.5bn*

Notes: All figures here are expressed in 2016/17 levels. Net revenue from the current system is an outturn figure for fiscal year 2016-17 that does not include revenue raised by higher rate of Council Tax levied on properties in bands E to H introduced from April 2017. As such, this modelling is based on a slightly different assumption from that presented in Figures 27 and 28.
Source: RF modelling based on data from ISER, *Understanding Society*

While there would be many calls on any new revenue, clearly it would be within the gift of the Scottish Government to marshal at least some of this to fund interventions that offer those who have no wish to, or no prospect of, holding housing wealth the similar levels of security that those with property assets enjoy. It could, for example, invest some of these proceeds in building new – and especially affordable – homes in areas of high demand; supplement family benefits beyond the recent Scottish Child Payment to reduce levels of child poverty; or improve the quality and efficiency of existing homes through energy efficient retrofitting.

All in all, there is clearly a range of ways that the Scottish government could take action to tackle both the level and distribution of housing wealth. While radical change is a political challenge, when the evidence shows so clearly that the housing wealth gains of the past fifty years have been largely unearned, the main property tax is so inequitable and inefficient, and those who do not hold property wealth are increasingly housing cost-'stressed', the case for action is clear.

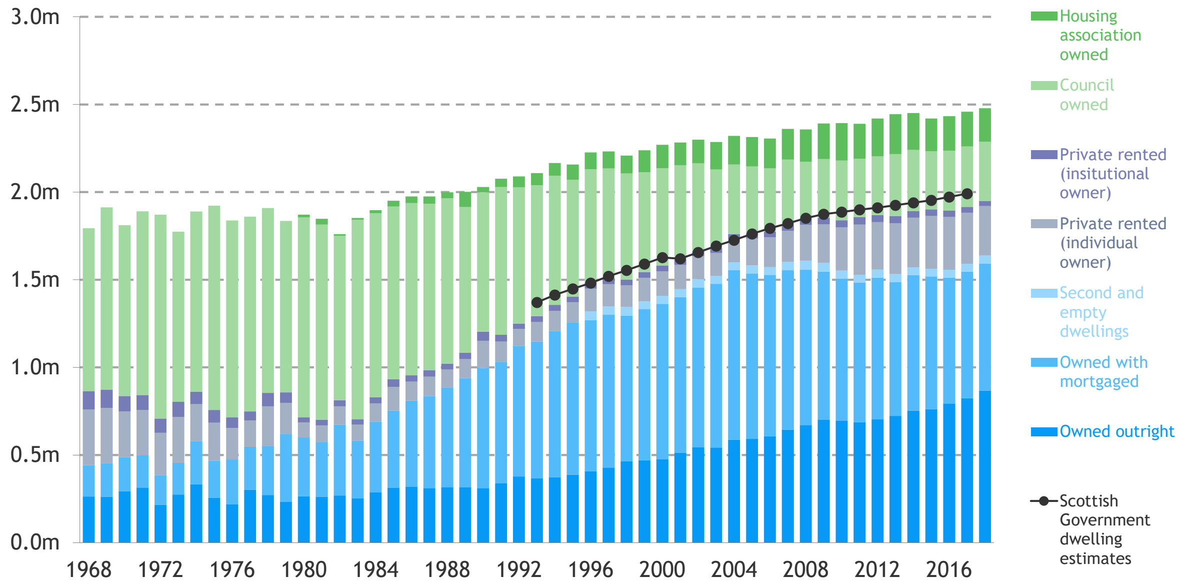
Annex 1: Estimating housing wealth using stock and price data

While housing wealth has been measured using survey methods since 1993, to understand its evolution over a longer time period, and its distribution at lower level geographies, we have to look to different data sources. In this report we construct a long-run time series of housing wealth in Scotland using data on housing stock and the unit price as follows.

We start with household tenure data from ONS Family Expenditure Survey (1968-1983) and Labour Force Survey (1984-2018) which provides an estimate the number of dwellings which are publicly owned (either by a local authority or a housing association) or in private ownership. From 1996 onwards we also add in Scottish Government figures on the number of dwellings which are empty or second homes.

We then use the LFS to estimate the share of dwellings that are privately rented but owned by an institutional rather than an individual landlord. From this, we can estimate of the number of dwellings that are privately owned by individuals (the 'owned outright', 'owned with a mortgage', 'second and empty dwellings' and 'private rented – individual' categories in Figure 30 below). Finally, we cross-check these results with Scottish Government housing stock data which is available for the period 1997-2017.

Figure 30: Residential dwellings by ownership



Notes: Excludes communal properties such as halls of residence and retirement villages. Empty property and second homes data only available 1996 onwards
Source: RF analysis of ONS, *Family Expenditure Survey 1961-1983; Labour Force Survey 1984-2018;* & Scottish Government, *Empty property and second home web tables*

Next, we consider the average value of a residential dwelling over time. The ONS UK house price index provides a mix-adjusted estimate of the average value of residential properties in Scotland since 1968. However, this index presents the geometric rather than the arithmetic mean of house prices.[27] However, a house price index using the arithmetic mean is available for the period 2002-2015 published by the then DLCG. We use this to calculate the ratio between the arithmetic and geometric means for the period when both series are available and apply this across the whole time series of the UKHPI to bottom out the long run arithmetic mean.

We can now make an estimate of gross total housing wealth in Scotland by the simple expedient of multiplying the number of units held by individuals by the arithmetic mean for each year.

Finally, in order to estimate *net* housing wealth held by individuals we must make some assumptions about mortgage debt over the period. Using figures from the Bank of England and UK Finance, we estimate that approximately 40 per cent of the value of owner occupied dwellings that are mortgaged is held by lenders at any one point. We make a different set of assumptions for housing stock which is rented out to another however. For these types of dwellings, we assume none is subject to a mortgage before the introduction of buy-to-let mortgages in 1990. Thereafter, survey sources suggest around half of the private rented stock is unencumbered and we assume 25 per cent of the value of the remaining half is mortgaged.

[27] See HM Land Registry, *UK House Price Index: guidance and methodology, November 2018 for further details.*

Annex 2: Council tax reform specifications

Current system – this models the current Scottish system of Council Tax. As in England, properties are assigned a tax band between A and H, based on the property's value (or simulated value as of 1 April 1991). Local authorities set the rate of Council Tax each year by choosing the tax bill for properties in Band D, and properties in other bands pay set proportions of the Band D bill. In the current Scottish system the multipliers on the top four bands (Bands E – H) relative to Band D are set at a higher level than for England and Wales, while the multipliers for the lower rates are left unchanged. Although this new system was only introduced in April 2017, our modelling is based in calendar years 2016 and 2017 and so we simulate the new Scottish system having been introduced a year early in 2016.

Revaluation-plus – this modifies the current Scottish system of Council Tax to make it even more progressive. We increase the ratio between the top rate and the typical Band D rate from 2.86:1 to 3:1, while also increasing the rates paid by households in bands E to G. We reduce the rates that households in Band A to C are liable for.

Fully progressive – this policy is based on the one proposed in the Final Report of the Intergenerational Commission in May 2018, with minor modifications. Using up-to-date property valuations, it levies an annual tax of 1 per cent of a property's value, with a tax-free allowance per property set at the value of the 10th percentile of Scottish residential property values (in 2016-17 this allowance was £90,268). This annual tax rate is raised to 2% on the slab of property value that exceeds the 90th percentile of Scottish residential property values (a value in 2016-17 of £361,073).

Allowance and flat rate – this policy introduces a 1 per cent annual tax on the value of all properties, with a tax-free allowance of £10,000 per household.

Fully proportional – here we replace the present Council Tax with a single annual proportional tax of 0.53 per cent of a property's value, based on up-to-date property valuations. This level is chosen to raise approximately the same revenue as the current Scottish Council Tax system, assuming that this policy change would have no effect on property values.

Finally, it is important to note that in each of the policy scenarios described above, we assume that the current Scottish system of Council Tax Reduction continues to operate. This system is itself more progressive than the reformed system that currently operates in England and Wales. We assume that take-up of Council Tax Reduction is in line with the most recent take-up statistics published by the Department for Work and Pensions, which have not been published since 2010-11.

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