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Housing

Prime Minister (2)

MLS 13/10

10 DOWNING STREET

13 October 1982

The Rt Hon Michael Heseltine MP
Secretary of State
Department of the Environment
2 Marsham Street
LONDON SW1

Dear Michael,

COUNCIL HOUSE SALES

At the last meeting of the Family Policy Group, there was general agreement that we should press on with the sale of council houses as fast as possible. Since the Norwich case, we have made great progress with putting pressure on obstructive sellers. Might this be the time to investigate further ways of encouraging hesitant buyers? The numbers of applicants are rising fast. Even so, on present form it looks unlikely that we shall have liberated much more than 10% of council tenants by the time of the Election.

One proposal that originally caught the imagination some years ago was, I think, Peter Walker's: that any tenant who had lived in the same council dwelling for 20 or 25 years should, ipso facto, become its owner. This was financially dubious, since in many cases the tenant's rent over the past period - being artificially depressed by rent control - would not have paid for the house on any reasonable computation.

But if instead we think about projecting a similar scheme into the future, we can surely construct a financially sound plan to "swap your rent book for a mortgage" and so offer a release from serfdom to virtually every council house tenant.

In his speech to Conference, John Stanley pointed out some remarkable facts which are, I suspect, still known only to a minority of council tenants:

> "On the latest figures we have, the average building society mortgage needed by council tenants buying their homes was just £7,950 - that is all. Thanks to the Government's success in lowering interest rates, the cost of that mortgage after tax relief is now just £13.97 a week. But the average council rent is now £13.54 a week. So the difference between the average mortgage and the average rent for council tenants is just 43p a week. For some tenants it may even cost less per week to buy than to rent."

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One way forward is to make sure that every council tenant does know how easy it can be to take out a mortgage, as Cecil Parkinson's letter explains.

But that message may be rejected as party political propaganda by some tenants. And there is surely a case for building into the system a rent-book-into-mortgage scheme.

I attach some further work done by Christopher Monckton, now of the No.10 Policy Unit. Building on the various low-start schemes now available, he suggests a nationwide promotion of a rent-based mortgage scheme at minimal cost to public funds.

We do not, of course, claim to put forward a finalised proposal. But there does seem to be enough scope here for some work to be done urgently, with a view perhaps to a Manifesto commitment.

Would you be agreeable to Christopher Monckton meeting your experts - possibly together with Treasury representatives and outside professionals as well - to see if we can progress any further?

I am copying this letter to the Prime Minister and Geoffrey Howe.

Yours ever
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FERDINAND MOUNT

HOW TO SELL MORE COUNCIL HOUSES

The paper prepared by the Secretary of State for the Environment for the Family Policy Group shows how much progress has been made in selling council houses to their tenants under the Government's Right to Buy scheme. The success of the scheme is one of the outstanding achievements of the present Administration.

Yet it is at first sight surprising that the number of tenants wishing to take advantage of the very generous discounts now on offer is not very much larger than it is.

A. WHY TENANTS DO NOT BUY

The reasons for tenants' resistance to purchase are likely to include the following:

1. Even though the average discount on the sale of a council house is as high as 44%, giving an average discounted price of only £9,700, the initial loan repayments under a standard repayment mortgage are rather higher than what the tenant was previously paying in rent. Many tenants simply cannot afford the extra weekly outgoings. Mr John Stanley pointed out in his speech to the Conservative Party Conference that the average mortgage on a council house sale is now only £7,950; but that implies that the average purchaser is having to find a deposit of £1,750, which is not an easy sum for most working families to raise.

   EXAMPLE: The average council rent is £13.54 a week. A tenant borrowing £10,000 (the average sale price plus £300 for legal fees and other initial costs) would have to pay the monthly equivalent of £17.50 a week in mortgage repayments, with a further £2-£3 a week for insurances and maintenance. Thus his total weekly outgoings rise from £13.54 to around £20. Even if the tenant has managed to find the large deposit and has borrowed the average amount of £7,950, the weekly equivalent of his monthly repayments is £13.97 a week, with £2-£3 on top for insurances and maintenance. So he is having to find about £17.50 a week for outgoings on housing, or around £4 a week more than formerly.

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2. Council tenants are accustomed to handling simple rent-book transactions but are often terrified at the prospect of having to deal with lawyers, mortgage brokers and banks.

<u>EXAMPLE</u>: A tenant was recently offered the chance to buy her flat for only £5,000. After she had worried about what to do for several weeks, her friends advised her not to go ahead, even though it was in her financial interest to do so, because they knew she could not handle the complications of the purchase.

3. Labour-controlled local authorities have found a number of ways of delaying and obstructing tenants' right to buy. Although Section 86 of the Housing Act 1980 gives power to the County Court to determine any matter under the Right to Buy legislation (with the exception of valuation, which comes under the District Valuer) most council tenants are unaccustomed to fighting in the Courts and would not normally be willing to do so.

<u>EXAMPLE</u>: A tenant recently applied to buy his house from Lewisham Council. The Council told him that he would have to wait because they were short of valuers. He is still waiting. Other tactics include:

(a) deliberate over-valuing, since there is no obligation on councils to value realistically under existing legislation;

(b) service charges for flats set at unreasonably high levels;

(c) incorrectly classifying houses as flats;

(d) refusing to sell garages and gardens with houses;

(e) requiring tenants to remain connected to expensive district heating systems;

(f) imposing far-ranging restrictive covenants on sales with the intention of making resale difficult and therefore discouraging purchase.

4. Many council houses are in bad condition and their tenants are understandably reluctant to buy them and face large repair bills.

5. Although the Government has taken some steps to publicise the right to buy, an astonishing number of council tenants are not aware that they have that right. Even more of them do not realise that, even under existing mortgage arrangements, buying rather than

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renting might be within their means. Mr Stanley has recently drafted a letter for widespread distribution to council tenants, but it might be more advantageous to produce a very clear, simple leaflet, professionally designed, setting out the advantages of the Right to Buy scheme.

For these reasons, of which the first is arguably the most significant, council sales are nothing like as numerous as they should be. Furthermore, some evidence suggests that the number of applications for purchase which fail exceeds the number of applications which result in a sale.

B. <u>HOW TO OVERCOME OBSTACLES TO PURCHASE</u>

The following ways of overcoming the obstacles to council-house purchase are recommended.

1. Many council tenants either cannot afford the repayments on a 100% mortgage (if they can get one) or cannot find the large lump-sum deposit that is usually required.

<u>SOLUTION</u>: What is needed is a generally available, "low-start" mortgage scheme which removes the "front-loading" of the real repayment costs on a standard mortgage and spreads the real cost more evently throughout the loan.

Among the low-start schemes now available are the following.

(a) <u>Lazards/Index Linked Mortgage & Investment Co Ltd (ILMI)</u>

This scheme is run by Lazards in conjunction with the Index Linked Mortgage and Investment Co Ltd. It is a low-start, flexible repayment mortgage allowing borrowers to obtain loans up to 3.5 times annual earnings rather than the usual 2.5 times.

The borrower may vary his repayments above a fixed minimum. At the minimum level, repayments are increased each year in line with the rate of general inflation.

Interest is charged at a true rate of 6.2% above inflation, compared with the building societies' current true rate of 4.7% above inflation. This allows the company to pay its investors an attractive rate of interest, rather above that which building societies can offer.

In the early years of the loan the initial repayments are not enough to meet the interest due. The shortfall each month is added to the principal outstanding, so that in money terms the principal rises during the first half of the loan period. <u>But in real terms the value of the principal outstanding falls throughout the loan period</u>.

The scheme is not at present marketed to council tenants. It is directed at the upper end of the house-price range. There has been very heavy demand for it from potential house-buyers, but institutional investors are only slowly realising that low-start mortgages are a safe and profitable investment.

(b) <u>Halifax Building Society</u>

The Halifax scheme is more limited in scope than the Lazards scheme, and works in an altogether different way. It is available only to borrowers under 35.

The borrower is required to pay to the Society a deposit of 5-10% of the purchase price of the house. The Society invests this sum and uses it to subsidise the first 36 months' repayments. Free life cover is provided.

Again, the scheme has proved to be very popular with house-buyers.

(c) <u>The Building Trust</u>

Under the Building Trust scheme, the borrower pays only two-thirds of the prevailing mortgage interest rate charged by the building societies. For example, the current declared rate is 12% and the Building Trust charges 8%.

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The Trust takes a share in the equity of the house, so that if the borrower sells before he has paid off the loan, he pays a substantial sum to the Trust to compensate for his former low repayments.

The scheme has the advantage that the repayments are very close to council rents. When it was launched earlier this year, with some press publicity, the offices of the Building Trust were beseiged by callers asking for details. The Trust estimates that it received at least 10,000 enquiries in the first week alone.

Again, its difficulty was in raising finance for loans of this type. The pension funds, who are the only institutions permitted to lend to the Trust for legal reasons, have so far only lent the Trust enough money to provide 18 mortgages.

2. Promoting Low-Start Mortgages

The exceptionally heavy demand for low-start mortgages reported by the lending institutions now in the field supports the contention that very many more council tenants would opt to buy their homes if such mortgages were available to them.

However, the pension funds and other sources of finance have been reluctant to move into this field because they fear that, in the event of default by the mortgagor, their equity in his property might not be worth enough to match his debt to them, although in practice there is no real danger that this would happen. If the Government were prepared to guarantee certain kinds of low-start mortgage against default, there would be no shortage of investors.

Table A of the Appendix shows that, although the borrower's indebtedness rises during the first half of an index-linked loan on the Lazards/ILMI model, in real terms his indebtedness falls steadily.

Council tenants typically buy their homes at a discount of 44%, so there would be very little risk that a lender's equity would be lost in the event of default. The Government may therefore care to consider guaranteeing against default certain approved low-start schemes for council houses whose tenants were able to obtain a

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discount on the market value at or above a specified minimum level - say 30%.

This move would encourage the lending institutions to obtain from the pension funds and from private investors the necessary cash to fund the vary large number of mortgages that might be demanded.

From the point of view of council tenants, the proposed "rent-based mortgage" overcomes many of the disadvantages of the schemes now available and has certain additional advantages, both to the lender and to the borrower. The Department of the Environment has raised some objections to the proposal - objections which would also apply to the Lazards/ILMI scheme, which is similar to the rent-based mortgage proposal. These objections are answered in the Appendix.

3. Making Purchase Easy for Tenants

To overcome the fear of many tenants at having to deal with lawyers, mortgage brokers and bankers, the Government could set up a simple "package deal" under the slogan "Swap your Rent-Book for a Mortgage". The deal would be worked out in collaboration with the building societies, and particularly with those who offered low-start mortgages.

The tenant would be able to borrow not only 100% of the discounted purchase price of his house, but also enough to pay the legal fees andother initial costs.

The tenant would choose a solicitor from the local list and all the work would then be arranged on his behalf by the solicitor working with solicitors acting on behalf of the local authority.

The tenant's paperwork would be kept to the minimum, so that all he would have to do was to trade in his rent-book for a mortgage account with the building society.

The Government would promote the package vigorously, with leaflets spelling out the advantages and showing the cost of buying rather than renting.

Obstructive Local Authorities

Despite the Government's efforts to ensure that tenants have the right to buy their homes even from local authorities hostile to council house sales, some councils are still proving obstructive. And even some Conservative councils are not doing all they should to promote sales of council houses.

SOLUTION: One way to prevent Labour-controlled councils from using delaying tactics would be to publish a central telephone number which tenants having undue difficulties with house purchase could ring. In this way, the activities of councils like Lewisham would be detected quickly and action could be taken to prevent further delays. Mr Stanley has already publicly suggested that tenants having difficulties with house purchase should write to him, but many council tenants would be nervous of drafting a letter to the Minister and would find a telephone call to a special office rather easier to handle.

SOLUTION: If further legislation is possible, the following provisions might be considered:

(a) Realistic valuations, with a simple appeal system, should be mandatory on councils.

(b) The position of leasehold properties needs clarification.

(c) Reasonable limits should be set on service charges for flats.

(d) Tenants should have the right to buy all the property they occupy, including garages and gardens.

(e) There should be some limitation on the imposition of restrictive covenants by councils.

(f) A simple system of appeal, preferably using the courts only as a last resort, should be considered.

(g) The workings of the cost-floor provisions need to be re-examined. They are not always equitable. It would be best to give any tenant the right to "top up" his total number of years as a tenant, regardless of which properties he has occupied or which local authorities have been his landlords. It might also be worth examining the possibility of making the cost floor provisions even more generous than they already are, particularly for those who are not at present entitled to large discounts.

5. Council Properties in Bad Repair

A frequent complaint of council tenants is that their homes are in bad repair and that they cannot get maintenance carried out because councils plead lack of money.

The construction industry has been particularly hard-hit by the recession and the Government has been looking at ways of stimulating it. Construction was one of the industries which led the way out of the recession and high unemployment of the 1930s.

However, the housing statistics now show that there are more units of housing than households in all parts of the country. So the demand for new housing is not what it was.

The demand for repairs to the existing housing stock is considerable, particularly in the public sector. If the Government were to give priority to repairs on council houses which the tenants had decided to buy, and were able to make funds available for this purpose, a notable stimulus would be given both to the construction industry and to demand for council house purchase.

The Government, as part of the "Swap your Rent-Book for a Mortgage" package, could announce to tenants that their homes would be repaired at public expense, if any major defects were found, before the sale. It might also be possible to give tenants a guarantee against the emergence of major structural defects during the life of their mortgage.

Such Government guarantees against structural defects would be expensive. But it is not right that council tenants should be condemned to live in bad conditions. And it is usually, though not always, cheaper to repair and restore existing houses and flats rather than to demolish them and build new ones in their place.

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APPENDIX

The schemes for low-start mortgages operated by Lazards, the Halifax Building Society and the Building Trust all have drawbacks not shared by the rent-based mortgage proposal.

For example, the Lazards scheme, which is in many respects similar to the rent-based mortgage proposal, has initial repayments at a higher level than the rent-based scheme. The Halifax scheme requires the borrower to find a deposit of up to 10% of the purchase price. Under the Building Trust's scheme, the lender takes what amounts to a share in the householder's equity in his property. In this respect, the scheme is not unlike the Government's shared appreciation scheme.

ADVANTAGES OF THE RENT-BASED MORTGAGE

The advantages of the rent-based mortgage are:

1. Lower initial repayments than under any other scheme.
2. Extreme simplicity from the tenant's point of view.
3. Ease of administration from the lender's point of view.
4. Grossed-up tax relief in the early years of the mortgage.
5. No extra cost to the Government.
6. Comparative insensitivity to to interest-rate fluctuations.
7. Nothing to pay in deposit at the beginning of the loan.
8. Nothing to pay at the end of the loan.
9. The lender takes no equity in the property.
10. No primary legislation needed.
11. Repayments are so small that the risk of default is minimal.
12. Even a man on basic social security could afford to buy his home.

APPENDIX (cont.) CONFIDENTIAL

OBJECTIONS TO THE RENT-BASED MORTGAGE

The original objections to the scheme, on the ground that there would be no significant demand for low-start mortgages of any kind, have now been amply demonstrated to have been ill-founded. All the companies offering such mortgages report heavy demand.

The present objection is that "if borrowers' initial payments are set well below rent levels, then the debt is likely to grow considerably and the time needed to pay off the loan will lengthen" (paper by Secretary of State for the Environment, prepared for Family Policy group).

Unfortunately the Department of the Environment may not have fully understood the method of calculating rent-based mortgages as set out in the original paper outlining the idea. Its own calculations are accordingly incorrect. (See note below).

There is no need for the initial repayments to be set far below rent levels. All that is needed is to set them at or somewhat below the rent level. Ideally, the starting figure should be £2-£3 a week below the rent level, to allow the borrower to meet the costs of insurance and maintenance.

A PRESENT-DAY EXAMPLE

The rate of inflation is now at 8 per cent. and the building societies' declared rate of interest is 12 per cent., which represents an A.P.R. of 12.7 per cent. So the real mortgage interest rate is 4.7 per cent. above inflation. Let us assume that this unusually high real rate of interest were to persist throughout the 25-year loan period.

The average council rent is now £13.54 net of rates and the average discounted sale price of a council house is £9,700. The tenant opts to buy and borrows £10,000, enough to pay the sale price

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and the legal fees. Even if inflation were to stay at 8 per cent. and mortgage interest at 12.7 per cent., the weekly equivalent of the monthly repayment at the outset of a rent-based mortgage would work out at £9.56, about £4 less than the borrower's former rent. At the end of 25 years, the borrower would have paid off the full capital and interest on his loan, assuming that his weekly repayments, like the rent payments of the tenant next door, were raised once a year in line with inflation.

As Table A shows, the paper money value of the borrower's indebtedness rises during the first half of the loan, but its real value falls steadily throughout.

If the building societies found it necessary to charge a 6.2 per cent. A.P.R. for rent-based mortgages, as Lazards/I.L.M.I. do for their index-linked loans, the borrower's initial weekly repayment figure would rise to £10.83, which is still £2.70 below what he was formerly paying in rent.

To illustrate the adaptability of the scheme to continuous, high real rates of interest, Table B shows the repayment periods for a variety of interest and inflation rates, assuming that the tenant paid an initial weekly repayment figure equivalent to a sum ranging from £3 below his former rent to £2 above it.

The Chelsea Building Society, whose Financial Controller and Chief Executive both examined the original paper on rent-based mortgages, have said that they would participate in a rent-based mortgage scheme. If the Government were to introduce a scheme along the lines described above, other building societies would be likely to follow suit.

The resulting sales figures for council houses would almost certainly be very large indeed. If the Government were to accept the scheme, it could be introduced within months and might have some effect on the outcome of the next General Election.

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Taking Mr Stanley's figure of £7,950 as the average amount actually borrowed by council tenants buying their homes, the weekly repayments under the rent-based mortgage proposal would be only £7.61 on a 25-year loan at current rates of interest and inflation, compared with an average rent of £13.54 and a standard mortgage repayment of £13.97. It is obvious that very many more tenants would opt to buy if they were able to get their repayments down to the very low levels which the rent-based mortgage would make possible.

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TABLE A

YR.	PROPOSED "RENT-BASED" MORTGAGE A	B	C	D	STANDARD "REPAYMENT" MORTGAGE A	B	C	D
0	10000.00	10000.00	56.7	7636.36	10000.00	10000.00	56.7	7636.36
1	10469.58	9694.06	55.0	7942.30	9938.45	9202.27	52.2	8434.09
2	10989.04	9421.33	53.4	8215.03	9863.16	3456.07	47.9	9180.29
3	11509.71	9136.78	51.8	8499.58	9778.31	7762.34	44.0	9874.02
4	12026.58	8839.90	50.1	8796.46	9682.71	7117.08	40.4	10519.28
5	12533.57	8530.14	48.4	9106.22	9574.98	6516.57	36.9	11119.79
6	13023.40	8206.95	46.5	9429.41	9453.59	5957.37	33.8	11678.99
7	13487.37	7869.75	44.6	9766.61	9316.81	5436.27	30.8	12200.09
8	13915.16	7517.93	42.6	10118.43	9162.67	4950.31	28.1	12686.05
9	14294.59	7150.86	40.5	10485.50	8988.99	4496.73	25.5	13139.63
10	14611.31	6767.86	38.4	10868.50	8793.29	4073.00	23.1	13563.36
11	14848.51	6368.27	36.1	11268.09	8572.76	3676.71	20.8	13959.65
12	14986.52	5951.36	33.7	11685.00	8324.26	3305.68	18.7	14330.68
13	15002.42	5516.36	31.3	12120.00	8044.25	2957.85	16.8	14678.51
14	14910.94	5076.60	28.8	12559.76	7728.72	2631.33	14.9	15005.03
15	14699.24	4633.81	26.3	13002.55	7373.18	2324.33	13.2	15312.03
16	14374.92	4188.02	23.7	13448.34	6972.54	2035.22	11.5	15601.14
17	13835.18	3739.22	21.2	13897.14	6571.10	1762.45	10.0	15873.91
18	13136.43	3287.37	18.6	14348.99	6012.40	1504.60	8.5	16131.76
19	12224.13	2832.48	16.1	14803.88	5439.19	1260.33	7.1	16376.03
20	11067.44	2374.50	13.5	15261.86	4793.27	1028.39	5.8	16607.97
21	9631.85	1913.42	10.8	15722.94	4065.44	807.62	4.6	16828.74
22	7878.75	1449.22	8.2	16187.14	3245.30	596.94	3.4	17039.42
23	5765.07	981.88	5.6	16654.48	2321.15	395.33	2.2	17241.03
24	3242.72	511.38	2.9	17124.98	1279.80	201.82	1.1	17434.54
25	0.00	0.00	0.0	17636.36	0.00	0.00	0.0	17636.36

TABLE A shows the position at the end of each year of a 25-year loan of £10,000, assuming that the borrower buys his council house worth £17.636.36 at a 45% discount (ie he pays £9,700) and that he borrows £300 in addition for legal fees. The borrower on the "rent-based" mortgage pays the equivalent of £9.56 each week, raised every 12 months in line with inflation.

The inflation rate is assumed to be 8% per year and the mortgage interest rate is assumed to be 12% per year throughout the loan. It is unlikely that mortgage interest rates would remain this far above the rate of inflation throughout, but these figures show that the rent-based mortgage scheme would work even if they did so.

Column A is the principal outstanding at the end of each year. Column B is the real spending-power of the figure in Column A, at today's prices. Column C shows the percentage of the total value of the house represented by the principal outstanding, assuming that house prices keep pace with inflation. Column D shows how much the house-owner would get, after paying off the principal outstanding, if he sold his house (figures at today's prices).

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TABLE B : LOAN PERIODS FOR RENT-BASED MORTGAGES

This table shows the loan periods for a rent-based mortgage of £10,000 at various weekly repayment figures, assuming different rates of inflation and of mortgage interest.

In this table, the mortgage interest rate is always assumed to be higher than that of inflation. For instance, the column marked "MR= 5" indicates that the mortgage interest rate, as declared by the building societies, is 5 per cent. above inflation. The loan periods would, of course, be shorter still if there were a zero or negative real rate of mortgage interest, as there has been during most of the past 15 years.

In practice, real mortgage interest rates are expected to be 2.5 to 3 per cent. above inflation during the next 25 years.

All figures are in years and months. No loan period greater than 30 years has been included.

IR = the annual inflation rate.

MR = the real rate of mortgage interest, i.e. the excess of the building societies' declared rate of interest over the rate of annual inflation.

REPAYMENT = £10.54, £3 less than the average net council rent.

IR:	MR= 1	MR= 2	MR= 3	MR= 4	MR= 5	MR= 6	MR= 7	MR= 8	MR= 9	MR=10
0:	19y 6	21y 0	23y 0	25y 6	29y 0					
5:	17y 7	18y 9	20y 1	21y11	24y 7	29y 1				
8:	16y11	18y 1	19y 7	21y 8	24y10					
10:	16y 9	18y 1	19y 9	22y 0	25y 6					
15:	17y 3	18y10	20y11	24y 0	29y 2					
20:	18y 5	20y 6	23y 5	28y 1						
25:	20y 6	23y 5	28y 2							
30:	24y 1	29y 3								

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TABLE B (cont.)

REPAYMENT = £11.54, £2 less than the average net council rent.

IR:	MR= 1	MR= 2	MR= 3	MR= 4	MR= 5	MR= 6	MR= 7	MR= 8	MR= 9	MR=10
0:	17y 8	18y11	20y 6	22y 5	24y11	28y 7				
5:	16y 2	17y 1	18y 3	19y 7	21y 5	24y 3	29y 3			
8:	15y 6	16y 5	17y 8	19y 2	21y 4	24y 8				
10:	15y 4	16y 5	17y 8	19y 4	21y 9	25y 6				
15:	15y 8	16y11	18y 6	20y 8	23y11	29y10				
20:	16y 7	18y 2	20y 3	23y 4	28y 8					
25:	18y 2	20y 4	23y 5	28y11						
30:	20y 9	24y 2								
35:	25y 7									

REPAYMENT = £12.54, £1 less than the average net council rent.

IR:	MR= 1	MR= 2	MR= 3	MR= 4	MR= 5	MR= 6	MR= 7	MR= 8	MR= 9	MR=10
0:	16y 3	17y 3	18y 6	20y 0	21y11	24y 6	28y 4			
5:	14y11	15y 9	16y 8	17y 9	19y 2	21y 1	24y 1	29y10		
8:	14y 5	15y 2	16y 1	17y 3	18y10	21y 2	24y 9			
10:	14y 2	15y 0	16y 1	17y 4	19y 1	21y 7	25y 9			
15:	14y 4	15y 4	16y 7	18y 3	20y 6	24y 1				
20:	15y 1	16y 4	17y11	20y 1	23y 6	29y10				
25:	16y 4	18y 0	20y 3	23y 8						
30:	18y 4	20y 9	24y 6							
35:	21y 9	26y 2								
40:	29y 3									

REPAYMENT = £13.54, the average council rent net of rates.

IR:	MR= 1	MR= 2	MR= 3	MR= 4	MR= 5	MR= 6	MR= 7	MR= 8	MR= 9	MR=10
0:	14y11	15y11	16y10	18y 1	19y 7	21y 7	24y 3	28y 2		
5:	13y11	14y 7	15y 5	16y 4	17y 5	18y10	20y10	24y 2		
8:	13y 5	14y 1	14y10	15y 9	17y 0	18y 7	21y 0	25y 0		
10:	13y 3	13y11	14y 9	15y 9	17y 1	18y11	21y 7	26y 3		
15:	13y 3	14y 1	15y 1	16y 4	18y 1	20y 5	24y 5			
20:	13y10	14y10	16y 1	17y 9	20y 1	23y10				
25:	14y11	16y 2	17y10	20y 3	24y 1					
30:	16y 6	18y 3	20y10	25y 1						
35:	19y 1	22y 0	27y 3							

REPAYMENT = £14.54, £1 more than the average council rent.

IR:	MR= 1	MR= 2	MR= 3	MR= 4	MR= 5	MR= 6	MR= 7	MR= 8	MR= 9	MR=10
0:	13y10	14y 7	15y 6	16y 6	17y 9	19y 3	21y 3	24y 0	28y 3	
5:	13y 0	13y 7	14y 3	15y 1	16y 0	17y 1	18y 7	20y 9	24y 4	
8:	12y 7	13y 2	13y 9	14y 6	15y 6	16y 9	18y 5	21y 0	25y 6	
10:	12y 4	12y11	13y 7	14y 5	15y 6	16y10	18y 9	21y 8	27y 2	
15:	12y 4	13y 1	13y10	14y11	16y 2	17y11	20y 6	25y 1		
20:	12y10	13y 8	14y 8	16y 0	17y 8	20y 2	24y 5			
25:	13y 8	14y 8	16y 1	17y10	20y 5	24y 9				
30:	15y 0	16y 4	18y 3	21y 1	26y 1					
35:	17y 0	19y 2	22y 5	28y11						
40:	20y 6	24y 8								
45:	28y11									

Continued overleaf:

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TABLE B (cont.)

REPAYMENT = £15.54, £2 more than the average net council rent.

IR:	MR= 1	MR= 2	MR= 3	MR= 4	MR= 5	MR= 6	MR= 7	MR= 8	MR= 9	MR=10
0:	12y11	13y 7	14y 4	15y 2	16y 2	17y 5	19y 0	21y 0	23y11	28y 7
5:	12y 2	12y 8	13y 4	14y 0	14y 9	15y 8	16y10	18y 4	20y 8	24y 9
8:	11y10	12y 4	12y10	13y 6	14y 3	15y 3	16y 7	18y 4	21y 1	26y 6
10:	11y 8	12y 2	12y 8	13y 5	14y 3	15y 4	16y 9	18y 9	21y11	28y10
15:	11y 7	12y 2	12y10	13y 8	14y 8	16y 1	17y11	20y 9	26y 2	
20:	11y11	12y 8	13y 6	14y 6	15y10	17y 8	20y 5	25y 5		
25:	12y 8	13y 6	14y 7	16y 0	17y10	20y 8	25y11			
30:	13y 9	14y10	16y 4	18y 4	21y 6	27y 9				
35:	15y 4	17y 0	19y 4	23y 1						
40:	18y 1	20y10	26y 0							
45:	23y 4									

NOTE:

The Department of the Environment has calculated that, on a loan of £9,000 assuming weekly repayments of £6 at the outset, inflation at 10 per cent. and the true rate of interest at 13 per cent. (equivalent to a building societies' declared rate of 12.28421%), the mortgage would have to run for 37 years and the outstanding debt would reach a peak of £36,000.

The correct figures are 33 years 3 months and £28,714 respectively.

At first sight the figure of £28,714 seems alarmingly high. However, two points should be borne in mind:

1. At today's prices, £6 a week is an unrealistically low repayment, representing only half the council rent that the borrower would pay as a tenant. As the above table suggests, one advantage of the rent-based mortgage is that it is comparatively insensitive to changes in the rates of inflation and interest. For instance, if the borrower were to pay £7.38 rather than £6 a week at the outset, his mortgage would be paid off in 25 years exactly, on the assumption that he borrowed £9,000 at a mortgage interest of 13 per cent. true, with inflation at a constant 10 per cent, The outstanding debt would reach a peak of £16.100 at the end of year 14.

2. The peak money indebtedness is, of course, insignificant in real terms. Taking the £6 example, the peak money indebtedness of £28,714 is reached at the end of year 22. The real value, after 22 years of compound inflation at 10 per cent., is only £3,527.50 - or, if house prices have remained constant in real terms, only 22 per cent. of the value of the borrower's house.

Taking the £7.38 example, the peak money indebtedness is reached at the end of year 14 and its real value is £4,239.50, or about 26 per cent. of the value of the house. NB: the value of the house is assumed to be £16,070, which yields a sale price of £9,000 after a 44 per cent. discount.

For the Department's convenience, a listing of a computer program to calculate rent-based mortgages is given overleaf

TABLE B (cont.) CONFIDENTIAL

PROGRAM IN MICROSOFT BASIC COMPUTER LANGUAGE
FOR CALCULATING MONTHLY PRINTOUTS OF RENT-BASED MORTGAGES

```
10 INPUT "PRINCIPAL (£)";PRINCPAL
20 INPUT "WEEKLY REPAYMENT (£)";WEEKREPT
30 INPUT "RATE OF TAX RELIEF (%)";TAXRATE
40 INPUT "INFLATION RATE (%)";INFLRATE
50 INPUT "BUILDING SOCIETIES' INTEREST RATE (%)";MGGRATE
60 PRINT:PRINT
70 MTHREPT=WEEKREPT*365.25/84
80 INFLMULT=INFLRATE/100+1
90 MGGMULT=MGGRATE/1200
100 ACTLTAX=TAXRATE/100
110 GROSSTAX=TAXRATE/(100-TAXRATE)+1
120 A=PRINCPAL
130 C1=GROSSTAX*MTHREPT
140 B=A*MGGMULT
150 Y=1
160 IF C1>B THEN 330
170 PRINT "YEAR";Y,"REPAYMENT";MTHREPT
180 PRINT "A","B","C1","D1":PRINT
190 FOR X=1 TO 12
200 B=A*MGGMULT
210 D1=B-C1
220 PRINT A,B,C1,D1
230 A=A+D1
240 NEXT X
250 PRINT:PRINT
260 INPUT "CONTINUE";Z
270 C1=C1*INFLMULT
280 MTHREPT=MTHREPT*INFLMULT
290 Y=Y+1
300 B=A*MGGMULT
310 IF C1>B THEN 330
320 GOTO 170
330 PRINT "YEAR";Y,"REPAYMENT";MTHREPT
340 PRINT "A","B","T","C2","D2":PRINT
350 FOR X=1 TO 12
360 B=A*MGGMULT
370 T=B*ACTLTAX
380 C2=MTHREPT+T
390 D2=C2-B
400 PRINT A,B,T,C2,D2
410 A=A-D2
420 IF A<=0 THEN 490
430 NEXT X
440 PRINT:PRINT
450 INPUT "CONTINUE";Z
460 MTHREPT=MTHREPT*INFLMULT
470 Y=Y+1
480 GOTO 330
490 PRINT:PRINT:PRINT "MORTGAGE PAID OFF"
500 PRINT "IN MONTH";X;"OF YEAR";Y:PRINT:PRINT
```