Why stamp duty relief has not boosted first-time buyers

by Bob Pannell, Economic Adviser to IMLA

Monthly figures for first-time buyers have averaged about 30,000 since the start of this year and now appear to be treading water, after several years of solid improvement.

This must be disappointing for a Government, that has over recent years vested significant firepower in its Help to Buy initiative and used tax measures to tilt the market away from landlords.

Last November, the Chancellor of the Exchequer unveiled a new stamp duty relief for first time buyers, in yet another move to help young people get on the housing ladder. Since then, first-time buyers in England and Northern Ireland (and Wales prior to April) have enjoyed relief from stamp duty land tax (SDLT) of up to £5,000 on purchases of up to £500,000.

Why has this latest measure not helped?

Table 1: Residential transactions claiming first-time buyers' relief (FTBR)

Period	Number of transactions claiming FTBR	: under £300k	: £300-500k	FTBR as % of residential transactions
Q4 2017[1]	23,500	18,800	4,700	18%
Q1 2018	45,600	36,000	9,700	19%
Q2 2018	52,400	40,900	11,500	21%

Source: HMRC Quarterly Stamp Duty Statistics
Notes:
1. Relates to period 22 November 2017-31 December 2017 only.

Part of the reason is that not all first-time buyers benefit from the relief – about a fifth buy properties below the £125,000 threshold at which SDLT becomes payable, and a small proportion, mostly in London and the South East, purchase above the upper limit. On top of these cases, another proportion will not be eligible, because one of those buying has owned before, whether in the UK or elsewhere.

HMRC figures (see Table 1) indicate that those claiming first-time buyer relief are equivalent to about two-thirds of the number of first-time buyers reported by UK Finance.

But even where households qualify for the relief, an even more important factor is at play.

Put simply, cuts in stamp duty do not always benefit buyers.

We know that changes in stamp duty tend to feed through into house prices fairly quickly. Reflecting the permanent nature of the change, the Office for Budget Responsibility estimated that November's change would actually raise house prices by twice the value of the relief. That is, by up to £10,000.

Given this, cuts in stamp duty only make it easier to get on the housing ladder, or broaden choice of property, if the money saved enables households to put down a higher deposit and to borrow more.

This is illustrated in Table 2, where borrower A, after setting aside the £2,500 he will need for SDLT, only has sufficient savings to put down a 5% deposit (£12,500). The cut in SDLT lifts the price of property X by £5,000 (twice the value of the cut in SDLT), but his income will support extra borrowing made possible because he can now put down a larger deposit. In our example, not only could he purchase the original property X, but also a more valuable property Y.

But, for a borrower who is already at the limit of what his income and wider financial circumstances will support (4.45 in the case of borrower B), the cut to SDLT raises the deposit that can be put down, but this is not sufficient even to cover the higher house price that results from the tax change, and he is in fact worse off than before.

Table 2: How SDLT cut affects different borrowers

	Borrower A (deposit-constrained)				Borrower B (income-constrained)	
	Pre-November 2017	Post-November 2017			Pre-November 2017	Post-November 2017
	Property X	Property X	Property Y		Property X	Property X
Property price	£250,000	£255,000	£285,000		£250,000	£255,000
	✓	✓	✓		✓	✗
Mortgage and deposit	£250,000	£255,000	£285,000		£250,000	£252,500
Savings	£15,000	£15,000	£15,000		£30,000	£30,000
: SDLT	£2,500	£0	£0		£2,500	£0
: Deposit	£12,500	£15,000	£15,000		£27,500	£30,000
Mortgage	£237,500	£240,000	£270,000		£222,500	£222,500
LTV	95%	94.1%	94.7%		89%	88.1%
Income	£60,000	£60,000	£60,000		£50,000	£50,000
Income multiple	3.96	4.00	4.50		4.45	4.45

While we cannot say for certain what dynamics are currently affecting first-time buyers the most, nor what their situation would have been in the absence of the cut in stamp duty, the recent UK cities analysis from Hometrack provides a timely reminder of how house price growth continues to outpace that of incomes.

Moreover, the affordability challenge arising from house price to earnings pressure is given still more bite by the macro-prudential levers used by the Financial Policy Committee. In particular, the regulator's insistence that lenders stress affordability at mortgage rates of 7½% or so seems both unduly cautious given market expectations of future rates and limits the ability of all but the youngest to stretch their incomes.

Taking a step back, the recent lacklustre state of the housing market and the levelling off of first-time buyer numbers suggests that now is not the time for the Government to announce major changes to its Help to Buy Equity Loan scheme. For many reasons, the Chancellor's 29 October Budget should be an opportunity for steadying the ship.

2 October 2018