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The Social Housing Quasi-Market

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1. INTRODUCTION

Social housing in Britain is at the forefront of major social policy reform in tune with the Government's rhetoric of choice and reform of public services (Glennerster, 2003; Toynbee and Walker, 2005). The reforms are (superficially at least) coherent and raise multiple questions for the future of non-market housing (Marsh and Mullins, 2001; Stephens et al, 2005). Debate has begun to engage with the broad agenda set by Government as well as (more frequently) the specifics of individual elements of the project. This paper seeks to add to the debate by locating the policies within a common framework (quasi-markets viewed through the lens of neo-institutional economics) and by examining the anticipated effects of specific policies as well as re-reading the evidence that already exists, as provided by the literature and by the author's own research.

The paper links to several discrete themes. Marsh's (2004) incisive analysis of contemporary social housing policy raises tantalising questions about using non-mainstream economic analyses (e.g. behavioural economics associated with scholars such as Tversky – see Rabin, 2004) to address choices in a non-market setting. This paper is complementary in that it asks whether a synthesis of mainstream industrial organisation, neo-institutional and institutional economics can help analyse developments in non-market housing. Marsh is concerned with three specific dimensions of the quasi-market: choice-based lettings, rent restructuring and reform of housing benefit. Here, the focus is broader, also explicitly encapsulating the economic nature of the providers of non-market housing by various social landlords and the regulatory (including the financial) environment they inhabit. It is also interested in the working or effectiveness of the non-market system as a whole. This is a wider canvas than the original evaluative quasi-market approach (e.g. Le Grand and Bartlett, 1993). The neo-institutional analysis applied to social housing which is at the centre of this paper has its antecedents in Baker et al, 1992; Marsh, 1995; Maclennan and More, 1997; Whitehead, 2003; Gibb and Maclennan, 2005.

A second theme is an evolutionary or institutional one. The current policy agenda is distinctive because it is incremental, inter-linked and seeks to build toward a common point in the future where the policy framework and household/organisational behaviour work harmoniously in a functional quasi-market. The real time horizon is at least 10 to 15 years and this begs a number of questions about long term variables (e.g. aspirations of current and future households, the financial environment, etc), about path dependency (e.g. social landlords are more or less locked into business plans), long term political risk (e.g. how the regulatory framework will evolve) and dimensions of Knightian uncertainty (i.e. unknowable futures). This of course also makes policy evaluation fraught with difficulty from this early vantage point but it does raise valid criticisms about methods adopted to assess multi-layered policies (including, of course, that attempted here – see the conclusion).

A third theme is also institutional and about the governance of social housing. Marsh (2004) argues that one can view the new policy framework as about increased central control over social landlords and the mechanisms they use (see also, King, 2001). An important feature of the new arrangements therefore concerns the regulatory rules and processes underpinning what social landlords must and must not do, the range and scope of discretion they enjoy, the control of rent-setting, incentive structures that encourage specific ownership and transfer of engagements, the new allocation mechanisms ostensibly between applicant and landlord and the alleged empowerment of applicants and tenants through user choice, payment responsibility and voice mechanisms. These issues are at the heart of institutional thinking in economics in terms of concerns about power, control and structural dynamics. How does this change the institutions of social housing (in terms of rules, practices, rights, responsibilities, structures and relationships across different tiers of social housing governance)? Are these changes desirable and does the institutional framework shed additional light on change to the non-profit housing sector? Insights from institutional economists such as Hodgson (1996) have not had much impact on applied fields in general (however, Guy and Henneberry, 2002, review the link institutional economics has made with planning and development issues). A further theme therefore concerns how useful this loose body of work is for examining the restructuring of social housing?

The structure of the paper is as follows. After the introduction, section 2 briefly sets out the principal reforms that are increasingly argued to amount to a quasi-market in social housing. Section 3 outlines the conceptual framework drawing on ideas from the quasi-markets literature, neo-institutional and institutional economics. Section 4 uses this framework and addresses each of the policy reforms in turn before assessing the overall picture. Section 5 concludes, returning to the themes identified above and asks whether the heterodox, though far from unconventional, economics approach to policy analysis adopted has wider currency.

2. THE POLICIES

First described in the 2000 Housing Green Paper (DETR/DSS, 2000), a linked set of policies have now been introduced either as pilots ('Pathfinders') or have been phased-in or established as time-limited targets. Before describing these policies and their logic, first it is useful to set out a sketch of social housing in Britain (note that the policies discussed apply in total to England and in part only to devolved Scotland – Gibb, 2004).

Social Housing in Britain

The purpose here is not to provide a lot of detail (see: Whitehead 2003; Bramley et al, 2004; Gibb and Maclennan, 2005; Stephens, et al, 2005 – for more context). Rather, this brief outline identifies the key characteristics of social housing in the UK and the main long term challenges it confronts (including the perceptions of Government).

Social housing refers to the 5 million or so British homes owned by non-market landlords either in the form of council housing or through Registered Social Landlords (RSLs), mainly housing associations (Wilcox, 2003). The purpose of social housing is to tackle unmet housing need such as homelessness, overcrowding and that arising from low income. Social housing also plays a wider role in strategies aimed at public health, community development and neighbourhood regeneration. Tenants enjoy a range of rights related to their occupancy including some security from eviction, below market rents, access to means-tested personal subsidies to reduce housing costs and council tenants have a right to buy (RTB) their homes at a discount based on length of tenancy. Housing is primarily allocated by a rationing device that queues applicant according to landlord measurement of relative need.

Council housing, through shrinking, remains the largest provider of social housing. Operating within conventional public expenditure constraints and wider regulation, the sector has lost more than 40% of the 1980 stock to the RTB and more than 930,000 properties have been transferred as a going concern to new and existing RSLs (Social Housing, June 2004). Between 1981 and 2002, the overall level of social housing in England fell from 5.2 million to 4.2 million, a shift in tenure share from 29% to 20%. At the same time, the RSL sector has grown from 410,000 units to 1.467 million and grown as a tenure share from 2.3 to 6.9%. RSLs can be thought of as commercial not for profit landlords. Closely regulated by the state and for fiduciary purposes (as major private finance borrowers), the housing association community has been transformed in the last 15 years into a multi-billion pound social business sector with significant political, community and commercial implications (it also manages to stand largely outside of the public expenditure constraints faced by the increasingly impoverished council landlord sector).

The stock of social housing, particularly the council sector, has become increasingly residualised through sales of the best homes in the more attractive areas. Arguably, this has been exacerbated by the cumulative effects of homelessness policy prioritised through allocations policies (Stephens et al, 2005). The housing itself tends to be concentrated in specific neighbourhoods and purpose-built estates and in increasingly unpopular built forms and design layouts. RSL stock is newer and is often more associated with the cheaper end of private speculative built form. RSLs have also taken over and improved former council stock. Nonetheless, some of the above problems visited on local authority housing neighbourhoods have been found in less successful housing association areas, too.

Although average rents have been long controlled through different explicit and implicit devices, social landlords have been until recently left to set their own rent policies to distribute rental income across the stock as they see fit. This discretion has led to a patchwork of rent levels, flat versus sharp differentials, inconsistencies and obscure price signals for tenants within and across landlords in specific areas as well as comparisons made wider afield. RSLs can receive upfront capital grants that are combined with private finance (funded by rents) to develop new homes. Councils have not build general needs homes in any numbers for many years but face often stark problems of housing debt repayment as a result of the combined effects of sales and declining demand for their properties. Successive needs and demand exercises indicate that insufficient quantities of new affordable, often social, housing are being developed to cope with pressure within the wider housing system.

Social sector tenants are increasingly characterised as being disproportionately young and single, single parents and also the elderly. Relatively low numbers of social tenants have connections with the world of work and consequently are highly dependent on means-tested benefits and housing benefit in particular (levels of 62% of housing association tenants received HB in 2002 – Wilcox, 2003). It is hard not to draw the conclusion that social housing is viewed by many as an inferior good (in the technical sense) and despite the more favoured financial and political environment facing the RSL sector, the growing similarity of the client group characteristics, means that all social housing confronts common demand issues.

Prior to 2000, the main inter-linked challenges facing the sector revolved around specific demand weakness for specific property types, locations and in some cases, much more broadly for housing as a whole (private and social). There are of course particular pressurised social housing markets where shortages are the key problem but for many areas and for the long term, it is low demand that is the key structural problem. This low demand phenomenon has many explanations (Bramley and Pawson, 2002) such as inter-regional out-migration associated with economic restructuring, compound neighbourhood problems, landlord management failure, the redundancy of specific property types, the failure to defend investments, but also genuine demand problems arising from rising aspirations about housing and neighbourhood quality which it is perceived cannot be met by social housing. The shadow across social housing in the long term is one of viability – can investment and stock utilisation be sustained in order to maintain these organisations and meet their financial and regulatory requirements. In short, can they provide a sufficiently attractive service and product to keep their properties occupied?

In their recent wide-ranging synthetic review of English housing policy, Stephens, et al (2005) argue that the 25 years up to 2000 were characterised by a restructuring of subsidy from supply to demand-side assistance alongside the asset restructuring of social housing towards a more business-oriented RSL sector. The latter long term process has been undoubtedly accelerated by Labour since 1997. The authors identify a number of challenges facing policy for social housing: the need to reverse the fragmentation of the sector, to devise policies that work with the grain of the social and economic environment, to provide more choice in social housing, to make it more viable, more integrated with the market and to reverse the decline in subsidised social housing. Although these are the result of reflection on long term policy trajectories they also apply in the light of the more recent policy reforms that are discussed in this paper. We return to these ideas later in the paper.

The Reforms

In a manner consistent if not in the vanguard of other social policy public service reform or modernisation agendas, the Government has wholeheartedly embraced the quasi-market choice logic of restructuring social housing provision, aiming to widen and realise consumer choice and provide an array of incentives to encourage or steer the sector in the future. Apart from being similar to earlier experiments with market signals in school provision under the earlier Conservative Government, the policy framework also echoes contemporary developments such as foundation hospitals and enhanced user involvement and direct payments in social care.

On the supply-side, Government has introduced both incentives and financial structures that will reshape *social sector provision* both by transferring council housing to non-council landlords but also by changing the framework and (it is hoped) the behaviour of council landlords who retain stock. This ambition is based on two closely linked policies. First, council housing in England has had significant reform of its financial and business planning requirements, effectively bringing council housing closer to a social business. The main ways this will be achieved are:

- A restructuring of statutory accounts away from traditional annual statements to long term measures of the opportunity cost of capital and depreciation associated with council housing as a going concern (and a corresponding focus on long term maintenance and viability).
- A focus on long term business planning, demand viability and the transparency of landlord management and strategic assumptions.
- Opportunities for the best performing council landlords (as viewed by their regulator) to access prudential borrowing for new investment, provided debt and operational management costs allow future rental streams to comfortably cover new commitments.

Second, all social landlords are expected to deliver all of their retained housing at a minimum statutory quality standard (the Decent Homes standard) within 10 years (i.e. by 2012) and to have implemented strategies to improve their stock to the requisite level. Essentially, council landlords only have a limited set of options, approaches which, of course, help the Government achieve its wider objective of further breaking up council housing and widening the plural provision of social housing through the RSL sector. The options are:

- If the council meets the performance and financial criteria, to use prudential borrowing within a long term financial planning framework to fund improvements (but increasingly operate as a social business with the alleged micro-efficiency benefits thereof).

- If the council performs wells enough according to its external regulator, to access public subsidy to fund improvements as an arms-length housing organisation, distanced from traditional council ownership but retaining tenants' rights.
- A PFI/PPP model has also been piloted, wherein councils enter into a long term lease with a private concern who will manage, improve and run the housing as a going concern for an annual fee before returning the housing to the council a the end of the lease. Tenants remain council tenants through the life of the project.
- If the above do not apply, the main alternative remains partial or total stock transfer to a new or existing RSL. Councils have to decide which if ay properties are to be demolished and whether partial or whole transfer makes more sense (and the public finance implications of there is overhanging debt upon sale). Government willingness to assume outstanding debts has made stock transfer more likely though demand viability issues clearly remain.

As we examine in part 4 of this paper, the key features of the options open to most councils are that all face a strong regulatory environment relating to performance, policies and business behaviour. Equally, exposure to private finance creates a different form of regulatory discipline. For all of the emerging models, efficient utilisation of the stock, optimising cash management and sustaining demand are critical (Gibb, et al, 2005). While in the long term one can see how the playing field is being levelled for providers (particularly when we also consider other complementary reforms), it does not follow that there will be necessarily more supplier competition between social landlords. Whereas in Scotland similar pressures to stock transfer have been predicated on smaller scale local organisations that operate at a community level and involve strong tenant or community involvement, the priorities in England have been much more about scale economies, minimum efficient size and viability at the expense of tenant involvement and possible local competition.

Three further, linked policies are being piloted with a view to subsequent comprehensive delivery. First, government wants to reform the practice of what are reasonably viewed as remote, bureaucratic allocations systems where tenants play a passive role. Instead, tenants will be offered currency (normally related to their housing needs) with which they can bid for properties. They also can monitor feedback on the currency required to be allocated such properties. In this way, so-called *Choice-based Lettings* (CBL) allow applicants to play a more proactive role in housing allocations and in some ways to introduce elements of choice into the system. At the same time, applicants are to be helped by the proposed development of common housing registers where all landlords within an area would combine their housing lists in this way improving consumer information and, one assumes, helping make better choices (or stated preferences) for social housing.

We look at the evidence on CBL below but a couple of preliminary points should be made now. Introducing elements of choice or user power into allocations is a necessary condition to allow other parts of the quasi-market to work i.e. providing clear or coherent price signals and funds for low income households to shop around, only makes sense if there is a means to then be allocated housing that fits with relative preferences. It has been pointed out (Marsh, 2004) that there is something anomalous going on where either social housing is allocated by means of prioritising need and therefore (quasi-) market forces are abrogated, or, not-for-profit housing is allocated though (in part) choice based on a currency in fact itself based on the landlord's measurement of that applicant's housing need! Marsh concludes that the policy is incoherent in this regard. We return to this issue in part 4 of the paper.

The second leg of the linked quasi-market mechanisms concerns the *pricing of social housing*. All social landlords are on a 10 or 15 year trajectory towards a common national rent structure imposed on them by Government, thereby ending local rent policy discretion. Landlords are also being obliged to converge local average rents between different landlords (i.e. rental growth is typically slowing for RSLs who have traditionally had relatively higher rents than councils). This is dampened to reduce large year on year transitional effects. The new formula takes the national average rent and then weights it (0.7) according to relative regional affordability of the area (i.e. earnings locally as a share of average national earnings) and also weights (0.3) the relative capital value of the open market value of the individual unit relative to the national average and includes a further weighting element for the number of bedrooms (correlated with capital value (from 0.9 to 1.1). As Marsh suggests (2004, p.191), the formula distributes average sector rents to individual dwellings with a relatively high weighting on affordability considerations and a lower one to capital values. However, areas with above average capital values will clearly impact through higher rents and because earnings vary less than capital values, this will reinforce large inter-regional rent differences.

Apart from the repercussions this policy is having on forward financial plans (an example of the political risks faced by RSLs), rent restructuring by formulae will in time provide consistent price signals for consumers comparing social landlords locally. One may take issue with the structure of the formula and its underlying components, but it does have the virtue of providing clear common signals within housing market areas.

The third leg of the quasi-market reforms and one initially predicated on the existence of a well-functioning social housing 'market', refers to the radical re-shaping of the Housing Benefit (HB) system and its replacement with a *local housing allowance*. The existing HB system sits uneasily between income maintenance objectives (where it guarantees post housing cost income levels for Income Support tenant claimants) and its many impacts on low income housing. Key features of the structure of HB are:

- Recipients on full HB typically have no connection to the rent for their property because 100% of eligible housing costs (usually the full rent) are paid directly to the landlord.
- All recipients of HB paying nothing at the margin if their rent increases because it is only if income rises relative to their assumed allowance level that HB falls.
- A means-tested benefit, HB has a high taper of withdrawal as income rises (65%) and is associated with disincentive effects as are other features of the system (e.g. disincentives against savings which is treated as tariff income).

As the cost of HB grew after 1988 and its path dependent features linked into the labour market, social security, arrears control and as comfort for private finance, it was often argued that the Gordian knot of a plainly perverse system could not be cut and thorough-going reform introduced. In 2002, after much discussion of the options for reforming HB, Government announced a pilot scheme to be operated in pathfinder areas for the private rented sector (where a market is supposed to exist by definition – though this is in places questionable). The new policy once piloted would be developed for the entire private sector and in time to the social sector as well, once the other quasi-market elements were operational.

In line with the Government's rights and responsibilities social policy agenda, all eligible tenants who receive the local housing allowance are responsible for paying their net housing costs themselves (exceptions will be made for vulnerable tenants and those in arrears). Landlords will not generally receive the allowance direct. The allowance is calculated according to the local reference rent (LRR) for different property sizes within a local market area. This is the median private sector rent for non-outlier properties and has until now been used as a ceiling for HB purposes. Under the local housing allowance, eligible tenants in the pathfinder area are given this LRR as a cash allowance and the idea is that they can shop around and keep any savings. Means-testing still applies as before and consequently those with slightly higher incomes will only be eligible for part of the allowance. The logic of the local housing allowance is to focus on shopping incentives and personal responsibility while in principle it undermines the fundamental income maintenance requirement of guaranteeing post housing cost incomes for low income households (unless one is in work and can benefit from the available mixture of benefits and tax credits).

The social housing quasi-market that will evolve over the next decade will consist of a new mix of providers seeking to deliver at least a minimum acceptable level of quality of social housing, within a common regulatory and planning framework. Providers will interact with 'empowered' potential and current tenants who are to have better information about landlords and the allocation of housing, consistent price signals and low income households will have an allowance with which to bid for social housing. The next section suggests a conceptual framework with which to analyse the social housing quasi-market.

3. A FRAMEWORK FOR ANALYSIS

The first wave of quasi-market policies (the internal market in health, school education, the purchaser-provider split in social care and direct payments, etc) led to valuable evaluative research and a coherent analytical framework (Le Grand and Bartlett, 1993). The argument developed below is that this framework can be usefully extended in the not-for-profit housing sector by examining specific neo-institutional economics questions relating to the market-hierarchy structures associated with the providers and the choices and incentives facing their current and potential tenants. The framework can also be modified to take explicit account of the broadly institutional features of the social housing system, its wider context and the constraints this imposes on policy reform.

Assessing Quasi-Markets

Le Grand and Bartlett (1993) employ a two-part framework for analysis of the 'first wave' of quasi-market policies. First of all, they consider (1993, p.13) the appropriate measures for success induced by the quasi-market policy change. Second, they set out the necessary conditions if these criteria established earlier are indeed to be achieved.

The criteria used by Le Grand and Bartlett cover policy goals of efficiency, responsiveness, choice and equity.

- Efficiency. The focus here is on productive efficiency i.e. providing a given quality/quantity of a service at minimum cost. In this context, this perspective is not extended (by Le Grand and Bartlett) to allocative efficiency. Seeking micro-efficiency gains has always been a strong emphasis in social policy quasi-markets.
- Responsiveness. This criterion stems from concerns about traditionally remote or unresponsive relationships with users. Although it is tied up with the quality of service, its prominence as an issue politically explains its independent position in this list.

- Choice. The importance of extending user choice through quasi-market innovation is both about empowerment and allocative efficiency. Le Grand and Bartlett (p.16-18) ask important ancillary questions about choice. Is choice extended by the policy for the user or for an agent working on behalf of the agent? Is the extension of choice in relation to the service itself (e.g. residential or non-residential care) or to the provider of that service (e.g. private sector, voluntary or NHS)? Thirdly, they ask whether the extension of choice is a goal in itself or as part of the means to achieve greater efficiency or responsiveness. They point out that there are other mechanisms that could facilitate these objectives, such as Hirschmann's voice and exit mechanisms (Hirschmann, 1970).
- Equity. Although this is considered to be the least articulated aspect of successful quasi-market policies, it does (and should) feature, not least as a goal associated with the core social justice objectives of most social policies in practice. Le Grand and Bartlett simply define equity in terms of meeting need though acknowledging the difficulty that this may raise definitionally.

Le Grand and Bartlett then go on to identify a number of conditions required for quasi-market policies if they are to achieve these criteria for success. Five discrete areas are identified and these are briefly outlined below.

First, what is the market structure of provision associated with the quasi-market? To what extent is the market competitive in terms of sufficient numbers of providers and consumers or the threat of market entry in order to at least create the conditions for a contestable market? This implies that, for providers, market entry and exit should be relatively low cost and there should be at least some threat of bankruptcy to encourage efficiency. Prices should be determined by demand and supply and should be able to move in response to changing market conditions. These are in fact an immensely challenging set of requirements (Le Grand and Bartlett, p. 20-24), some of which in failing to be met may raise second best questions about what would be the best alternate course of action.

A second area concerns service information. Both sides of the market require low cost accurate information to improve choices concerning the price and quality of the service in question. Typical problems in this regard arise because of opportunistic behaviour exploiting likely informational asymmetries such as adverse selection and moral hazard. This class of problem is likely to be acute for quasi-markets because of the centrality of information required for monitoring the quality of service. A key feature of quasi-markets (and also the regulation of natural monopolies) is that a quality floor is placed on provision but this requires adequate information and the capacity to process, analyse and monitor information continuously. But when hierarchies are split into contracting commercial relationships, especially in complex systems such as primary health care, this can easily become difficult [analogous problems arise for social housing regulators]. Le Grand and Bartlett worry that the benefits of quasi-markets may be dissipated by a number of factors such as the scope for opportunistic behaviour by the monitored.

Third, there are important issues bound up with transactions costs and uncertainty. Williamson (1975; 1985) argued that the extent of transactions costs help decide the market v hierarchy choice of organisational form. Quasi-market development clearly moves the delivery of a social policy service along the organisational spectrum towards the market end. It therefore has to overcome the main transaction costs in terms of benefits outweighing such costs.

Le Grand and Bartlett (1993) highlight the basic insights that transactions costs provide for quasi-markets, distinguishing between ex ante and ex post transactions costs. Ex ante costs are the costs of setting up an exchange, wherein complex exchanges are often contracts with legal and wider opportunity costs. Ex post transactions costs refer to the monitoring of these exchange agreements or contracts once in place. Skimping on the ex ante costs may mean high costs of enforcement and compliance later on. The idea behind the market-hierarchy split was that as Coase (1937) suggested, transactions costs may be so high that it would be preferable to internalise them within the firm rather than through a series of commercial contracts.

Le Grand and Bartlett (pp.27-30) raise several important considerations about transactions costs and quasi-markets. First, the efficient balance between centralisation and decentralisation or market v hierarchy is not fixed but is highly contingent on the market sector and industry in question (and by extension, the quasi-market in question). Second, where there are asset specificity issues, that is, where human and physical capital are tied together such that the cost of replacing them is very high or where there is no alternate use, there will be generally advantages in remaining integrated rather than split into market relationships.

Third, problems with future uncertainty of demand are linked to issues of bounded rationality and the limited scope of individuals to make efficient decisions in the face of complexity and uncertainty. This also, according to Williamson, helps explain bureaucratic over market systems in such circumstances, by allowing agents to deal with the unknown in an adaptive and sequential fashion (Le Grand and Bartlett, p.29-30; Marsh, 1995). If the contracts struck in the quasi-market are complex and outcomes are contingent on uncertain states of nature, then the transactions costs may be very high and some form of risk-sharing is often written into the contract. Again, the costs may outweigh the other benefits of moving to the quasi-market. The more uncertain the environment, the more difficult it is to agree an encompassing contract (Marsh, 1995).

Fourth, there are important requirements associated with the motivations of providers, linked to the fact that the providers are often not for profit organisations. There has to be an underlying financial motive otherwise agents will not respond to market signals. This is arguably less of an issue for social housing since all providers would be commercially oriented not-for-profit businesses.

Fifth, there may be scope for quasi-market providers to discriminate or cream-skim which would be socially detrimental. The problem here is that there may be scope to discriminate against high cost users and more generally to seek out inappropriate low cost solutions – this will be a matter for regulation and for the design of the user-provider interface. This may well be an important issue for social housing in the future.

Le Grand and Bartlett's framework is an excellent starting point for the analysis of the new social housing quasi-market. At the heart of it is a concern with industrial organisation questions and the key application of information asymmetries and transaction cost or market-hierarchy questions. However, it is possible to take these themes somewhat further and look more closely at how one might evaluate the economic performance of not for profit but commercially-oriented social housing.

Social Housing Dimensions

The housing economics literature has primarily evaluated non-market housing from the perspective of an individual's welfare and the efficiency of service production, rather than from the perspective of the provider or wider system's efficiency. Green and Malpezzi (2003) review the (North American) literature on the production, consumption and administrative efficiency of public housng subsidy. Muth (1973) and Mayo (1986) argue that production inefficiency is a public housing problem with a high likelihood of a capital intensive, anti-maintenance construction bias. Green and Malpezzi summarise this by arguing that these price distortions will lead to higher (lifetime) costs per unit. They review several studies of consumption efficiency concluding that higher efficiency is found with demand-side approaches such as allowances compared with public housing programmes.

Rather than focus exclusively on individual welfare, Gibb and Maclennan (2005), building on a paper by Maclennan and More (1997), argue that analysis of the economic interests, property rights and structures of social housing and how they impact on incentives and behaviour, can shed evaluative light on both the effectiveness of individual providers (and provider types) as well as the non-market system as a whole (including consumption interests). At the heart of the analysis is identifying the nature and consequences of the interests of the different parties in social housing and how these are reconciled and adapted by regulation and by the rules of the quasi-market.

Assessment of the quasi-market model for social housing needs to look closely at the incentives for performance at the individual organisation level, the type of provider and the wider system effects. This requires a clear sense of the structure of ownership and control within organisations, their market-hierarchy split and the impact of external regulation from the state and from loan finance. Maclennan and More (1997) argue that analysis of the effectiveness of a system of not for profit social housing should focus in on five dimensions of performance: competitiveness, the control of owner/manager discretion, internal incentive structures, hierarchy design and the setting the hierarchy/market boundary (1997, p.542).

- To what extent are not for profit social housing providers exposed to competition or contestable forces? This is more than the concerns raised by Le Grand and Bartlett. Maclennan and More identify the degree of competition for capital subsidy and the degree of competition within spatial boundaries as important dimensions of competition, arguing that below market rents and properties allocated by queues imply landlords with downward sloping demand curves (up to the market rent level). Even if grant allocation is competitive, there will be scope for discretion in price and output mix.
- Ownership is not always clear in the not for profit sector. What scope do stakeholders have to limit the discretion of owner/managers of not for profits in terms of their choice of tenants, pricing and quality of service? Maclennan and More identify four key stakeholders: government agencies (subsidy providers and regulators), private finance interests (again with an ex ante but also on-going regulatory or monitoring role), tenants (with longer term time horizons than staff?) and management staff. Tenants have different roles in these organisations as consumers, owners and electors in different forms of social housing (at both centralised and decentralised levels). What are the exit, voice and loyalty mechanisms that tenants have to influence investment and service outcomes? Maclennan and More contend that organisational growth, and job/organisational security are central but depends on how hard the budget constraint actually is for not for profit social housing providers. They argue (1997, p.544) that, in practice,

the regulator is far more likely to use mergers or transfer of engagement rather than let the organisation go under.

- How effective are incentive compatible internal incentives for staff to operate efficiently? Maclennan and More view them as comparatively weak conceptually because of the difficulty of measuring service outputs and practically due to national wage-setting inhibiting meaningful performance related pay.
- Where on the centralised–decentralised spectrum should not for profit housing organisations be located? Maclennan and More make a strong case for a decentralised system following Sah and Stiglitz (1988) in that decentralisation ‘facilitates information-gathering, encourages experimental variety and exposes intra-organisational differences in performance. These observations appear pertinent in social housing where decentralisation may also encourage resident involvement’ (1997, p.545). Further, they argue that ‘the superior innovation and information properties of localised, multiple providers are likely to outweigh the economies of scale of larger hierarchies’ (p.545). The RSLs are not for profit commercial social businesses. They also, to a greater or lesser extent, have to (and indeed may want to) work in partnership with other landlords, developers and councils. A key question therefore is how effective are the incentives to cooperate and synergise with other housing providers in the local housing system as well as to compete?
- While there has been no systematic assessment of whether inputs should be purchased by not for profit housing providers through market or hierarchy structures, Maclennan and More argue that there should be regular market testing of the alternatives, while accepting that it may not be sensible or desirable to produce efficient contracts for all such aspects. However, one should critically assess the system-wide impacts of the choices made and whether they are, in a sense, being used to prevent competition.

These points apply to the specifics of the design of not for profit social housing system, but also complement and add to the points raised by Le Grand and Bartlett in their more general social policy quasi-markets framework.

Evolutionary and Institutional Dimensions

The social housing quasi-market is essentially evolutionary in that it develops to its desired state over time incrementally and dynamically. It is also arguable that the intentional development of the quasi-market system involves an institutional regime shift from one based on a traditional non-market bureaucratic system (admittedly one interacting with limited consumer choice) towards a new set of arrangements based on a mix of price signals, incentives, market forces and an element of non-market needs assessment. Can institutional and evolutionary economics shed light and add to our analytical framework?

Institutional and evolutionary economics ideas remain non-mainstream and raise issues about methodological compatibility. Hodgson (1996), for instance, has argued that neo-institutional perspectives with its focus on property rights and transactions costs, remains firmly in the mainstream economics tradition because, individuals treat institutions as effectively new constraints to their optimising behaviour (the same analogy applies to information asymmetries). The institutional economics and evolutionary economics paradigms however do not sit well with optimising rational individualism centred on exogenously determined preferences.

Samuels (1995, p.573-5) attributes eight key facets to the institutional economics paradigm:

1. It emphasises social and economic evolution and therefore takes an explicitly proactive or activist approach toward social institutions.
2. It affirms the importance of social control and the exercise of collective action.
3. It emphasises technology as a major driver of change in economic systems.
4. Rather than an abstract market mechanism, it is institutions that allocated resources, specifically their power structures that shape markets ‘and to which markets give effect’ (p.573).
5. The theory of value is now based, not on relative prices, but on a process in which institutions, social structure and behaviour all play central roles.

6. Institutionalists emphasise the role of culture within the process of cumulative causation. Veblen (1899, 1998) eschewed equilibrium to describe the economic system as a ‘cumulatively unfolding process’.
7. Insitutionalists with their focus on power, hierarchy, inequality, structure and habit – tend to be pluralistic and democratic in outlook and certainly do not take these features for granted.
8. Institutionalists tend to be holistic, multidisciplinary and interested in the non-market sector as well as the market economy.

How do these ideas relate to framing an analysis of the social housing quasi-market? The value of this approach is that makes one concentrate on the broadly institutional features of the social housing system (in terms of rules, practices, rights, responsibilities, structures and relationships across different tiers of social housing governance), its wider context and the constraints this imposes on policy reform. The approach emphasises the historical development of the institution of social housing, the processes by which it attempts to respond to the evolving political, social and economic context, and the constraints that inertia and path dependency place on innovative policies. The institutional perspective is particularly suited for helping the analyst think through questions to do with the distribution of power and control in the social housing policy framework (e.g. the role of the state as regulator and loan finance in a similar capacity) and the impact of endogenous preferences – the idea that aspirations and preferences are not fixed but are to an extent shaped by experience and are malleable as a result of policy change. This latter point is an important part of the story regarding shifting patterns of social housing demand in recent years.

A Framework for Analysis

Figure 1 schematically fits together the different elements of the conceptual framework in a multidirectional heuristic wiring diagram. Here, institutional analysis is used to help understand the wider structure and place of social housing in the wider environment. Essentially, this is an attempt to develop the analysis by looking more closely at the social housing system as an institution, drawing on the key themes identified in the paragraphs above. The analysis at the bottom of the diagram draws from the neo-institutional and organisational economics is used to analyse the performance of the social housing quasi-market policies that seek to change the social housing system.

4. ASSESSMENT

In this section, we use the framework set out above to shed light on the quasi-market policies for social housing, both singly and together. In so doing we combine in-principle arguments with evidence from existing relevant evaluative research.

Provider Competition

Does the new structure of provision create a contestable market on the supply side? The new minimum housing standard along with new funding and regulatory rules will in time create a new mix of social housing provision consisting of council housing, operating under business management and prudential principles, arms-length housing organisations, traditional and LSVT housing associations. These organisations will be focused on improving their stock to the required standard, maximising occupancy and hence cash flow and in general focusing on asset management. In time there will be considerable convergence in provider type, operating within a common regulatory framework.

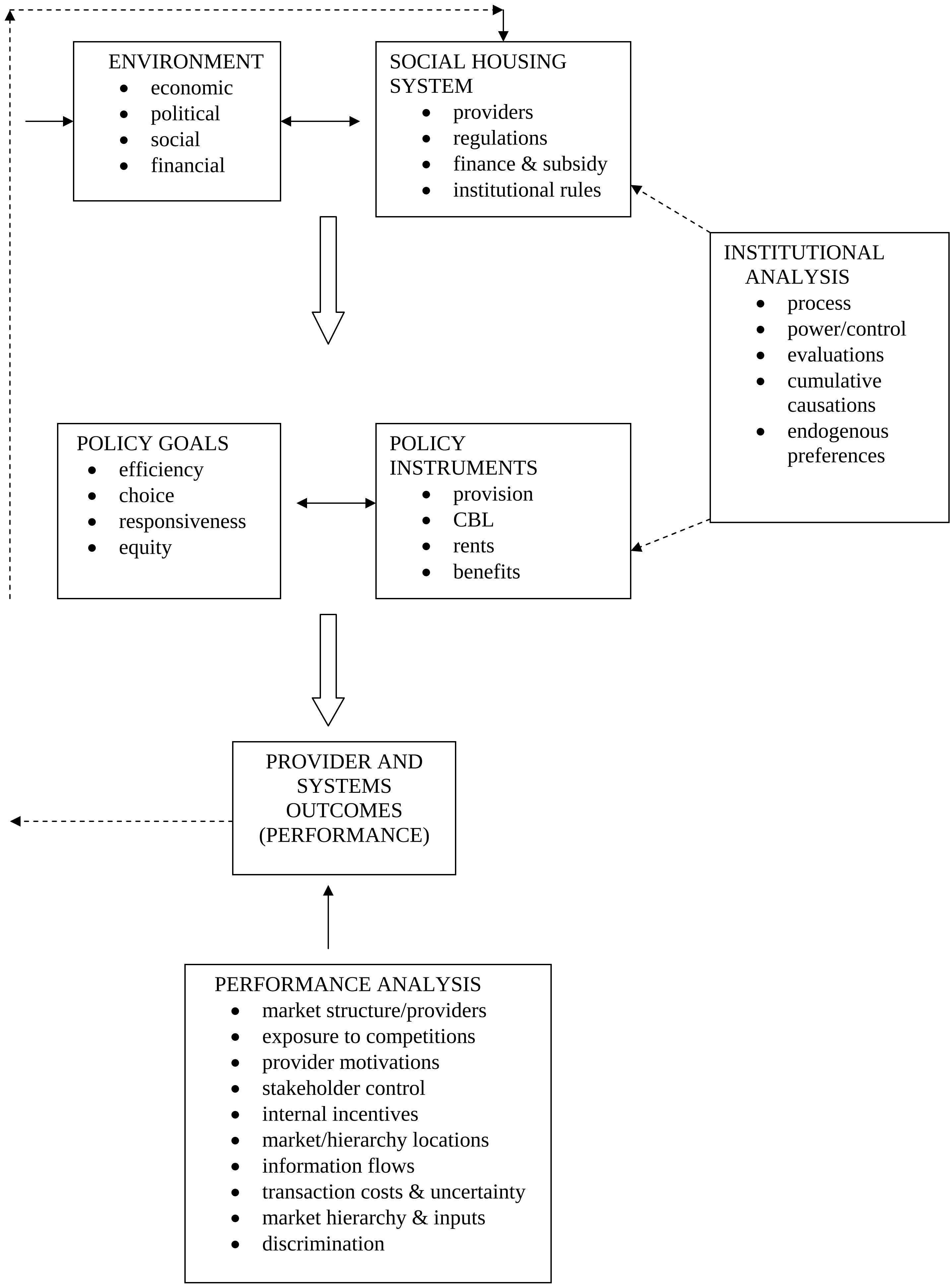
ENVIRONMENT
economic
political
social
financial
SOCIAL HOUSING SYSTEM
providers
regulations
finance & subsidy
institutional rules
INSTITUTIONAL ANALYSIS
process
power/control
evaluations
cumulative causations
endogenous preferences
POLICY GOALS
efficiency
choice
responsiveness
equity
POLICY INSTRUMENTS
provision
CBL
rents
benefits
PROVIDER AND SYSTEMS OUTCOMES (PERFORMANCE)
PERFORMANCE ANALYSIS
market structure/providers
exposure to competitions
provider motivations
stakeholder control
internal incentives
market/hierarchy locations
information flows
transaction costs & uncertainty
market hierarchy & inputs
discrimination

Figure (1) QUASI MARKETS: AN ANALYTICAL FRAMEWORK

The upshot would be a likely increase in the number of providers, although the extent to which they are in open competition is questionable (mainly there will be geographical market power, except where existing multiple providers already existed before the advent of the decent homes standard). The threat of bankruptcy, that is, the existence of hard budgets, is a genuine one. Althoguh the regulator would normally step in to an RSL facing financial or managerial problems, they are empowered to take over the running of the organisation by appointing a new board and/or staff to run it. Moreover, the lenders legally require that their covenants are covered. Social housing providers are not profit-oriented in the normal sense but they often do have growth or revenue maximising objectives. Social business growth would be unlikely to seek to maximise undsitrubuted surplus in the form of for example reserves but at the very least, the impact of competition, of bidding for new development opportunities, of providing service to tenants and income for lenders – will act to motivate providers to cut costs and waste and to provide a responsive service. Whether the majority of providers respond in this way, particularly those who are not in the game of development but would rather, for instance, manage community-based housing stock and prioritise need – is unknown.

Stephens et al (2005) point out that the new arrangements, what they call the supply-side social market, are not promoted by tenants but by Government and by the providers themeselves. Stock transfer is mor elikely to be the entire stock rather than its break-up into smaller community scales (because the finances often prclude this). Furthermore, the development of ALMOs or PFI-type schemes do not widen choice per se. Nonetheless, the desire to win the compulsory ballot will produce voter-friendly packages for tenants after transfer.

Whereas one might expect an enhanced degree of responsiveness among providers driven by the need to sustain demand and in terms of ballot promises for stock transfer landlords, it is not so straightforward to argue that choice will generally be increased. Will the providers be more efficient? This is a difficult thing to assess at this relatively early stage in the project's development but there is some illustrative evidence from Scotland. Gibb, et al (2005) evaluated the Scottish Homes stock transfer programme of its own housing. Altogether 118 separate transfers have taken place since 1991, largely at a community-level or well-defined geography, often in areas with established council housing and other RSLs (though the RTB had often been heavily used in the same areas). Although this study was largely qualitative and case study-based it did reach some tenative conclusions about the performance of the stock transfer associations:

- LSVT associations have largely met or improved on their business plan targets.
- Performance does appear to be, albeit somewhat crudely, related to stock size and economies of scale. Smaller associations do appear to be more vulnerable in the long term to merger and rationalisation.
- LSVT associations appear to be learning from their new regulatory and financial environment.
- Tenants do generally seem satitsfied with management performance and the maintenance of key pledges at the time of transfer.
- Particularly in smaller and newer associaitons, tenant involvement is often deeply embedded.
- A simple cost effectiveness study of 12 case studies suggested that while costs were often reasonably high there had been good returns on activities and impacts by the RSLs and a good fit with their overall objectives. Results were strong on service quality, investment, viability, tenant involvement and reduction of void losses.
- However, it is important to remember that these transfers operated in a fairly benign financial environment; many have benefitted form re-financing and, depending on the local context, from operating as deveopers of new social housing, and in seeking out new incme streams through wider aciton activities. Not all RSLs can hope to be well-placed to exploit these opportunities.

A strong message from the Scottish research criticised the ever-changing and usually upward level of regulation, in adidition to financial and audit scrutiny. One very clear us eof power in the social houisng world is the state's ability to set up long term business arrnagements with landlords but then increase the regulatory burden without provision of fianncial support. A reaonable question for tenants, landlords and lenders is how valuable and efficient is the level of regulation imposed on RSLs

Choice-based Lettings

Along with common housing registers, Choice-based lettings (CBL) are designed to give consumers more transparency and choice in social housing by tilting the allocation away from prioritised need towards consumer preference. Stephens et al (2005) argue that CBL should not be overstated. It cannot create better homes or neighbourhoods but might rather contribute to greater residential stability. They argue that the shift away from prioritising need towards prioritising time waiting, on the assumption that the latter are less needy, will alter the balance of power in the system (p.52). However, they think this may be the reason that many of the piloted systems still retain a significant needs element in their formulae. Marsh (2004) argues that the message from the evaluation of piloted CBL systems is that it is possible to increase demand for stock previously considered low demand. The system is found to be popular for its users and the system increases transparency (2004, p.194). However, Marsh identifies some limitations: it is not the case that the system puts applicants in charge but rather, since the system is devised by the landlord, there can still be plenty of scope for social engineering (p.194). Second, greater choice may in fact weaken residential stability but evidence one way or another remains fragmentary. Third, the feedback mechanism much vaunted of CBL has proven rather weak thus far.

Second, choice-based lettings rely on some degree of slackness or vacant housing to operate but we may expect a by-product of the provider reforms to be a reduction in vacant stock over time and the elimination of non-transitory surpluses. If this is so, then the allocations leg of the reforms will increasingly depend on the common housing register which, of itself, is unlikely to have major impacts on widening realised tenant choices, particularly in a system which will become more rather than less tight. However, problems associated with discriminatory practices – for instance, refusing access to social housing, would be appear to be less of an issue, if only because of the presumption that more rather than less regulation from the centre may be expected in the future. If the recent Scottish experience is anything to go by, we may expect to see an increase in tenants rights feeding into landlord practice through regulatory devices.

CBL cannot really be assessed separately from the other demand-side reforms but it does appear to provide potentially more information and transparency about opportunities. Of course it depends on the turnover of the stock and relative demand as to whether it actually makes a material difference. Marsh (2004) argues that the retention of prioritised need remains anomalous in the context of introducing market signals – rent restructuring and housing benefit reform use, as it were, a different *currency* from CBL, which is more artificial and non-monetary. But of course there is a tradition of this in quasi-markets more generally with the NHS remaining free at the point of delivery and relying on various prioritised queues, despite introducing internal markets for micro-efficiency gains in terms of allocative efficiency. It is not unreasonable to argue that a relatively neglected objective of CBL and indeed common housing registers has been to increase micro-efficiency, given the nature of the other reforms on the demand side. Nonetheless, it would appear that this is an area where the underlying policy goal of equity has retained a high salience with the providers of CBL.

Rent Restructuring

Consistent and transparent pricing is essential for the social housing quasi-market. We have seen that rent restructuring, part of the demand-side reforms, will produce local average rent convergence and a national rent structure, moderated by local capital values, regional affordability and bed size. A contrary perspective is that this has been a further example of the regulatory or political risk faced by social landlords with regard to their power relationship with the State. The transparency that will be achieved at the end of the transitional period is a welcome step particularly if one wants consumers to be able to make sensible comparisons between landlords and within a specific landlord's housing stock. However, this does not means that the chosen centrally-determined system is the optimal approach. Walker and Marsh's evaluation (2003) found that the formula would not actually generally sharpen rent differentials in practice. Stephens et al (2005) argue that by better reflecting the open market value of properties, this should in principle be a fairer system (p.53).

Local Housing Allowances

The proposed local housing allowance will do two things: make tenants responsible for meeting their housing payments and secondly offer the incentive to shop around for better value housing. Of course, the first objective, that of personal responsibility, does not require the local housing allowance. The focus then is on the cash allowance aspect of the reform, which is enhanced by rent restructuring and the scope for movement increased by CBL.

Many commentators have focused exclusively on the problems associated with expected high rent arrears as the changeover occurs. This is certainly going to be an issue in the short run, for which there may need to be transitional support, but it will not remain so once the system becomes familiar – this is after all the whole point of the Government's responsibility agenda. There are however certain important technical questions to consider – the geographic boundaries for local housing allowance purposes – should they fit with consumer notions of market area? Should the database for the LHA include just private rents or the social sector once it comes on-stream (and if so, has the implications of rent convergence for LHA levels been fully considered)?

One must be qualified about reading too much into the actions of the pathfinder pilots unless convinced that the behaviour of private tenants within a market sector is genuinely comparable to the social sector after the quasi-market is established. That is a considerable leap for which there is no proper evidence. Gibb (2004) and Stephens et al (2005) point up the potential break with the income support system implied by allowing the LHA to work as planned, since that will lead to a reduction in some low income household's post housing cost levels of income. 'The trade-off is simple: the more that low income tenants are exposed to price signals, the greater their shopping incentive, but the greater the chance that their post-rent income will fall below social assistance levels'

(Stephens et al, 2005, p.53). Whether they reduce non-housing spending or accept lower levels of housing consumption remains to be seen.

The critical empirical question is whether tenants will respond to the price signals and shopping incentives? Of course, one should expect this to be a building cumulative process that will take time to sort households across the housing system. One should not take limited cross-sectional evidence as conclusive negative or positive proof about behavioural responses. That said, the evidence that does exist, reviewed by Marsh (2004) is limited both in number and in providing definite answers. For Marsh, the key question is how coherent the reforms are as a whole. However, his approach is to look at the three demand side policies rather than the cumulative forces of the supply and demand side reforms. We consider these further below when examining the overall impact of the reforms.

The Wider Quasi-Market

How might tenants be placed after the long term working through of these policies? They will confront a larger number of possible providers who face regulatory and business pressures to perform efficiently and a much simpler process of allocation – through a common waiting list and by utilising choice-based lettings. Rents will be set on a uniform basis so that quality differentials are consistently attributed to indivdual housing units, and average rents will be levelled across different providers so that inter-provider rent differences based on historical debt, etc. will be removed. To these price signal devices, one can add the new cash housing allowance, creating shopping incentives and encouraging the more efficent utilisation of housing space. Moreover, government expects the new housing quality standards to deliver significant improvements in the quality of the housing itself.

The quasi-market framework is undeniably helpful in assessing what government is trying to do but it does so within a fairly narrow state-welfare outcomes remit. Arguably government has not really thought through the long term implications of their approach for competition, choice and efficiency.

As we have seen, Marsh (2004) fundamentally believes that the reforms lack coherence beyond a superficial degree. In particular, he argues that different elements do not sit easily together because of their different currencies. I am less persuaded that this is such a serious problem because we are dealing with a quasi-market and not a market as such and there is no reason why a system which is essentially redistributive should not use prioritised need while at the same time seek to sharpen incentives and increase efficiency, responsiveness and choice (however we define the latter).

Nonetheless, when we turn to the list of performance criteria in figure 1, it is not clear that the policy project will necessarily achieve as much as it would seek to deliver. We can take the four main points in turn. First, the long term effects of the reforms on the supply-side will be to create a more micro-efficient set of providers but it is not clear that they will in any real sense compete with each other. Indeed, the variable geography of their markets, and the asymmetric overlapping of market areas will create an arbitrary element into the choice of alternative suppliers within a given area. It is also not at all clear that the regulatory burden is efficient or provides clear incentives to perform well in terms of future regulation – i.e. it may help with access to public funds but not with the regulatory burden itself. Scottish evidence suggests that regulators duplicate aspects of private lenders' oversight role.

Second, the providers will be sufficiently motivated to avoid loss, minimise waste and work to so-called 'hard' budgets. This is partly the result of the regulatory framework but primarily it is due to the assignment of risk following from the increasing penetration of private finance into the RSL sector. The maximisation of net income in cash flows applies across the social housing sector and this feature will encourage cost control but it may also of course engender growth policies which include take-overs and development strategies – again which may not be socially optimal or indeed may be contingent on pliable local contexts.

Third, the different stakeholders (government, lenders, tenants/board members and staff) will have variable degrees of control to limit the discretion of management. The regulatory process is a powerful one and would appear to be stronger in practice than many boards or tenant representatives, particularly where the organisations are centralised. The tension between ownership and control is also about the contrasting benefits and costs of strategies favouring centralisation over decentralisation. Earlier, we argued in favour of shifting the debate in favour of more decentralised tenant influence on informational economic grounds, though clearly one may argue that this is also a counterpoint in the power relationships between officers and members within the voluntary sector more generally. Internal incentives largely remain weak except where there is scope for organisational growth and advancement – but this is unevenly available and may well be a situation of adverse selection where the social housing market most needing strong leadership finds it hardest to attract and retain good staff.

Fourth, the focus on the demand-side reforms has arguably neglected the totality of the reform impacts on market-hierarchy decisions both for the organisation as a whole and in terms of its input choices. There remains little pressure to decentralise social housing providers (if anything the impact of issues to do with viability and sustainability works in the opposite direction) and the network of rules and stakeholders serves to keep a fairly tight rein on social housing hierarchies. But the point that Maclennan and More (1997) would make is that this is to under-achieve: by not seeking out a better balance between viability and decentralised management, tenant empowerment and local knowledge, the overall effectiveness of the social housing system is impaired. Le Grand and Bartlett also emphasised the contingent nature of the efficient balance between market and hierarchy. Nonetheless, the commercial nature of not for profit housing providers and the importance of local information should push one further in the direction of the market end of the spectrum?

The position on inputs markets, e.g. repair and maintenance contracting, is more straightforward (i.e. with considerably less uncertainty) with the large scale adoption of contracting, with the exception of council and former council housing where the former direct service organisations have often retained some form of monopoly foothold.

At the end of the evolution to the social housing quasi-market, tenants will have more transparent signals and information, as well as an ex ante cash allowance to work with. Their exit options will have been significantly enhanced and that should act to some degree on the quality of service provided to them. This will be reinforced by the decent homes standard and the cash maximisation logic of the commercial not for profit provider. Regulation will also play its part in raising the service quality floor. So, for all these reasons, one might argue from the present vantage point, early in the reform process, that these are movements in a worthwhile direction. However, there is also a debit side: the level of the housing allowance is crucial, the transitional costs are high and need to be factored in to overall assessments and many current providers will not be viable or face merger/takeover because of their size as well as due to genuine competitive advantage. Tenants will have exit routes but will their voice be heard – it is not at all clear that there will be more genuine tenant involvement and decentralised management or tenant control as a result of these reforms?

5. CONCLUSIONS

This paper has looked at the broad set of policies aimed at restructuring social housing in England and has gone beyond the demand-side to look at the restructuring of provision as well. The paper has set out a simple heuristic framework that has applied quasi-market analysis and more specific social housing analysis based on industrial organisation and neo-institutional economics. Policy analysis of social housing needs to work on three different levels: the experience of the consumer, the efficiency of the individual provider (or provider type) and the wider impact on the social housing system as a whole.

The paper has also suggested that there is a place for the non-mainstream institutional economics approach. In the current paper this has been confined to a relatively small contribution in helping to set the process of a long term evolutionary policy in some form of context and to provide an explicit reason for examining power and control issues which are so central to a rounded understanding of the processes of change in social housing and the wider New Labour social policy agenda. Institutional approaches are also useful for work on social housing because they raise important methodological questions about the endogeneity of consumer preferences, and also the significance of cumulative causation processes and path dependency factors which serve to constrain the pace and scope of reform.

Implicitly, this paper has established a wide range of possible research avenues for this broadened economics approach to social housing. Above all, there is a case to examine different forms of non-market provision in their specific settings and trajectories and to assess whether or not these new models, facing the new demand arrangements, will provide better or worse outcomes and why?

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