CIH response to the social housing rents consultation

Summary

- The social housing sector houses over 4.4 million households (with over one million on waiting lists), with rents set below market rates and reinvested to provide quality services and homes. General needs (social rent) homes make up the majority of the sector at 77% of all stock, with supported housing at 13% and low-cost home ownership at 7% (RSH social housing stock, Oct 2021). Up to two thirds of social housing residents are on some form of housing benefit/universal credit support for rents and benefitable service charges, with around three-fifths of income covered by benefits.
- Social housing providers are committed to keeping homes safe and well maintained, improving energy efficiency to lower bills, and building much needed new social homes. Providers have been working hard to support tenants and residents struggling with the cost of living and have put extensive help in place for this winter (as highlighted in our cost of living briefing series). However, without government intervention on welfare reform an increasing number of people face hardship. Even before the recent spike in inflation 68% of social housing residents were worried 'all or most of the time' about meeting normal monthly living expenses (Resident Voice Index).
- Whilst recognising the sovereignty of boards and councils to be best placed to make informed and localised decisions, we understand government's wish to intervene in rent setting next year given cost of living pressures. In the absence of intervention, we would expect most social housing providers to increase rents by significantly less than CPI+1%, alongside targeted support for those most in need. Rent increases below CPI will however mean reduced investment without additional government support, which will impact tenants and residents.
- Should the government choose to apply a cap, our analysis shows that based on the current economic outlook:
    - 3% would lead to a projected net loss of resources for LAs of c7-9% of all operating costs (management, maintenance and major repairs) and over 10% of operating expenditure excluding major repairs. For HAs it would equate to c9% operating expenditure or loss of interest cover of up to 30bps.
    - 5% would lead to a reduction of c5-7% in operating costs and c7-9% of operating expenditure (excluding major repairs) for LAs. For HAs it would equate to c7% operating expenditure or loss of interest cover of up to 15-20bps.
    - 7% would equate to a cut for LAs of c3-5% of all operating costs and c5-7% of operating expenditure (excluding major repairs). For HAs, a c3-5% cut in operating expenditure or loss of interest cover of up to 5-10bps. Even at the highest cap providers would have to take difficult decisions about what to prioritise and how to make savings, but this would be more manageable. Our analysis suggests it would allow social housing providers to adapt increases to their context and target support for residents facing affordability challenges.
- Under any cap scenario essential investment in social homes is at risk. To maintain investment in services and homes for residents, while keeping rents affordable next year, the government should:

  - provide grant to support investment in homes and services for residents, to at least the level of the benefit savings resulting from any cap
  - commit to reintroducing a 'catch up' mechanism so that rents can gradually return to their real terms level once inflation has fallen back, preserving long term investment for residents and confidence for lenders.
- Should government choose to intervene, any cap should be for no more than one year given the level of economic uncertainty. Supported housing should be exempt, reflecting its vulnerable financial position and viability risks.
- The impact assessment which accompanies the rents consultation underestimates the cost to the sector. We call on the government to publish a full assessment of economic impacts, including the loss of new development, impact on building safety works, decarbonisation and repairs and maintenance programmes before making a final decision on next steps.
- Whilst we agree with the imposition of a rent cap in these unique circumstances, it is important to recognise that this is the second time in seven years that a rent settlement has been broken and this does much to undermine the critical partnership between government and the sector and the investor confidence that is crucial to ensuring a viable, sustainable social housing sector. We welcome the commitment to shortly consult on a post 2025 rent settlement; the detail of which will be essential in shoring up investor confidence and guarding against future fiscal shocks, thus delivering affordable rents for residents and securing future investment in homes and services.

Introduction

The Chartered Institute of Housing (CIH) welcomes the opportunity to respond to this consultation. Affordability for tenants and residents is of paramount importance and we know from our discussions that social housing landlords were already exploring how best to balance this with viability and investment responsibilities. In order to inform our response, we commissioned Savills to provide an independent commentary and analysis (attached and referenced). We also hosted a member roundtable with DLUHC officials, ran an online member survey and spoke to tenant representatives and other partner organisations.

Context

Since the consultation was launched on 31 August, the economic climate has become even more challenging. Inflation is forecast to rise to 13% by the end of the year so whatever cap is introduced providers and tenants/residents will face considerable financial challenges. To that end, this consultation cannot be viewed in isolation. Government decisions on uprating benefits (previously committed to but now unknown), the impact of some measures announced in the 'mini budget' and decisions to be taken in the October Budget have a significant bearing. We continue to call on government to address the benefits shortfall. Up to two thirds of social housing tenants are on some form of housing benefit/universal credit support for rents and benefitable service charges, with around three-fifths of income covered by benefits. Many of these are working but on low incomes that need topping up (or unable to work because of disabilities or caring responsibilities). Even before the recent spike in inflation, basic benefits were worth 11% less than a decade ago – equivalent to a benefit cut of £1,800 for a family with two children. We welcomed recent government support via the energy unit price cap, however, at £2,500 for the average household's bill, this is still nearly double the amount that residents would have paid this time last year and out of reach for many.

Similarly, wider government priorities on building safety, decarbonisation, housing supply and economic growth, homelessness prevention, maintenance programmes, tenant engagement etc all risk being impacted by a cut to housing provider income. The current situation facing the social housing sector is very different to when a rent freeze was implemented in 2016. This comes after a pandemic, a building safety crisis and an acknowledged climate change crisis. We cannot afford to step back on the medium-long term agenda. Recent analysis and discussions support this. For example:

- Latest figures from the Regulator of Social Housing (RSH) show investment in major repairs across the sector was 33% below target last quarter because of inflationary pressures, as well as labour and material shortages.
- Analysis from the Local Government Association highlights that slow progress in insulating homes will cost Government at least £4.2 billion in energy waste over the next two years. To illustrate this, one housing association said the difference in heating costs for their worst stock compared with their best was £2,000 annually. Another highlighted that their plans to improve the energy efficiency of their homes would save tenants far more in reduced energy costs than the marginal saving they would make from rents being capped at 5% rather than 7%: the

average annual savings of a property moving from EPC D to C is £500, whereas the average saving in rent would be £84 per week x2% x52 = £87pa. These energy efficiency plans are however at risk if rents are capped without substitute investment.
- Research by the Institute for Public Policy Research shows that a government retrofitting programme could sustain over 400,000 direct jobs and 500,000 indirect jobs by 2030.
- As the UK Housing Review shows, government grant forms a relatively small part of social landlords' new build investment (e.g., outside London, only 13%), meaning that by far the biggest proportion of the cost is met from their own resources which in turn means their rental income.

Social housing landlords are already facing cost increases running at CPI or, in the case of construction work, higher. Borrowing costs have more than doubled in the last year. The latest economic signals (rising interest rates) will add to this pressure. (Savills' analysis for us provides an assessment of key determinants of landlord costs and likely inflation, as well as impact of financial market movements.) Providers are already starting to be asked to provide more assurance on mitigations to protect operating margins to satisfy ratings agencies. (If UK government debt is downgraded there is a risk that housing association debt will follow suit.) Moody's have warned that a rent cap, at any level, would constrain revenue growth for housing associations and impact credit scores, noting that we can expect to see trade-offs within the sector, such as reducing investment in existing stock and developing new homes. Without support to counter this, there is a real risk that the government's economic growth plans and wider policy agenda will be undermined.

Conversely, many tenants and residents are already struggling with day-to-day costs. A survey of over 5,000 social housing residents by Resident Voice Index in April/May (pre-dating the latest inflation spike) found that 68% were worried all or most of the time about meeting normal monthly living expenses. This rose to 82% for under 35s. Our research during the summer highlighted that for one large London-based housing association, 25% of residents regularly found their rent unaffordable and 35% were already finding that they had "nothing left" after meeting all essential outgoings. Our research suggests that cost of living pressures already play into the current (2022/23) financial year with an increased risk of arrears at up to 10-15% of rent across the whole sector. In response, many social housing associations have reiterated their evictions pledge, reassuring residents that where they engage with their landlord, they will not be evicted as a result of financial hardship.

It would be wrong to see a dichotomy between "tenants" and "landlords" on this issue. Tenants are well aware that the quality of service they receive depends on their rents, and for them the cost-of-living crisis may be more about energy and fuel costs, and income failing to keep pace with inflation, than about their rents. Social housing providers are acutely aware of the impact of what they do on tenants' wellbeing, and want to assist tenants to manage the current crisis, reduce their energy costs and help them survive on what are likely to be low incomes. To do this, of course, they need resources and their main one is rental income.

In weighing up the way forward, we would urge government to reflect on lessons learnt from the previous compulsory rent reductions – introduced before Grenfell – which directly led to reduced investment in maintaining existing stock, and reduced expenditure on tenant involvement. It is important to avoid inadvertently triggering a race to the bottom in terms of cost cutting, especially with regard to building safety. Post Grenfell, (and with the Building Safety Act) it is now more likely that new development and decarbonisation would be impacted – with consequent impacts on housing needs, including higher public expenditure on temporary accommodation for homeless families and energy support. We must also be mindful of wider supply chain vulnerability, with some private sector suppliers exiting from the market.

Finally, under the council housing self-financing settlement in 2012, councils took on considerable debt from HM Government on the understanding that future rent levels would sustain these debts, whilst maintaining homes at a decent standard. It is therefore appropriate that any decision to cap rents should be supported with substitute grant.

CIH response to consultation questions

Question 1: Do you agree that the maximum social housing rent increase from 1 April 2023 to 31 March 2024 should be subject to a specific ceiling in addition to the existing CPI+1% limit? To what extent would Registered Providers be likely to increase rents in that year if the government did not impose a specific ceiling?

Response:

Yes. Our discussions with providers, coupled with Savills' analysis for us, suggests that most (if not all) providers would have exercised restraint in increasing rents. However, we recognise that a cap could be helpful to ensure a level playing field and to assist local authority providers under pressure to keep rents artificially low, for example those facing contested elections. We do, however, recognise that individual boards and councils are best placed to determine the appropriate level of rent setting based on their circumstances. (These decisions should always follow tenant consultation, which could, in some scenarios, call for rents to be higher in order for services or investment in homes to be maintained.) It is also important to note that, despite the unique circumstances in which this consultation is taking place, the impact of government intervening in what is meant to be a long-term rental framework risks undermining investor confidence and our discussions suggest that it will inevitably do so.

Whilst we support the principal of a cap despite these reservations, we believe that the £4.6bn which DWP is forecast to save over the next five years should, as a minimum, be redistributed into grant to protect existing investment in current and new homes and support for tenants, compensating lost rental income. This funding could be made available through a combination of existing schemes such as the Social Housing Decarbonisation Fund, the Affordable Homes Programme, and the Building Safety Fund, or distributed directly to providers via a new mechanism explicitly aimed at revenue support. As we set out under mitigations at p.10, there is also a strong case for additional government investment.

To maintain and improve existing residents' homes, and to continue to build much needed new affordable homes, significant investment each year is essential. As not-for-profit organisations, the resources which social housing providers generate are put back into the homes they provide and build, and to support the services residents receive. Re-investable rental income is critical to supporting this work so any reduction will come at a cost in some form. The surpluses (and/or 'reserves') that are reported as part of financial results are key to securing borrowing to deliver the essential work that they do, and are held as fixed assets and working capital, rather than cash.

Question 2: Do you agree with imposing a ceiling of 5%, or are there alternative percentages that would be preferable, such as a 3% or 7% ceiling? Do you have any comments or evidence about the potential impact of different options, including of the 3%, 5% and 7% options as assessed in our Impact Assessment (Annex D)?
Response:

No. On balance, we believe that it would be more appropriate to impose a ceiling of 7%, on the understanding that this is a cap and not a target and that for some providers a 5% cap (and certainly a 3% cap) would be prohibitive. For example, a cap will significantly impact providers with large development programmes and those with large building safety or decarbonisation programmes. As our research with Savills notes, given that many of these programmes are deemed essential in order to comply with legislation, and are also subject to 10% inflationary pressures, this is likely to focus the recovery of operating margins within housing associations towards savings in day-to-day management and service costs. For LAs, given the pressures on HRAs arising from net reductions in income, if these essential programmes are to be completed, there is likely to be a need for direct capital grant support. (Recognising the pressure on rental affordability, one mitigating approach could be to provide a strong direction to apply a 5% ceiling but with an upper 7% cap to give those providers under financial pressures some margin.)

We believe that a 7% cap should be conditional on government uprating benefits in line with inflation (as previously committed to) so that existing tenants and residents in receipt of benefits are not unfairly penalised. This would allow housing providers to provide discretionary support for those not in receipt of benefits (in full or part) where needed. As set out above, a decision on cap level should not be taken in isolation from wider decisions on welfare uprating/reform.

When forming a view on cap level, we have referred to Savills' analysis which highlights the projected net resource challenge for 2023/24 and includes case studies to illustrate. This shows that the "minimum rent increase required to stand-still" as stated by LAs and HAs engaged as part of their research falls into the range of 7-9%, which they suggest might be understated.

In summary:

At a cap of 3% for 2023/24:

- LAs projected net loss of resources £600-700million – equating to between c7-9% of all operating costs (management, maintenance and major repairs) and over 10% of operating expenditure excluding major repairs.
- HA projected net loss of resources £1-1.2billion – equating to c9% operating expenditure or loss of interest cover of up to 30bps.

At a cap of 5% for 2023/24:

- LAs projected net loss of resources £400-500million – equating to between c5-7% of all operating costs (management, maintenance and major repairs) and c7-9% of operating expenditure excluding major repairs.

- HAs projected net loss of resources £750million-£1billion – equating to c7% operating expenditure or loss of interest cover of up to 15-20bps.

At a cap of 7% for 2023/24:

- LAs projected net loss of resources up to £300million – equating to between c3-5% of all operating costs (management, maintenance and major repairs) and c5-7% of operating expenditure excluding major repairs.

- HAs projected net loss of resources up to £400million – equating to c3-5% operating expenditure or loss of interest cover of up to 5-10bps.

Taking the net impact of a rent cap at 5% combined with increased financing costs, around 30% of all housing associations may trigger "golden rule" reviews of their lending covenants and business plans. This is likely to result in capital investment cuts and cuts in services. This would negatively impact tenants and residents both now and in the future.

Our discussions with providers over the summer (pre-dating the consultation) highlighted specific examples of potential impacts from cutting rental income. These are summarised in Savills' analysis.

In advocating for a 7% cap, we are very mindful of the impact on tenants of any rent increase. However, if social housing providers must cut their expenditure significantly, apart from new build practically everything they are likely to have to cut is a service to tenants, with often the ones most affected being those in most potential hardship (due to cuts in hardship funds, debt advice, energy-efficiency measures and advice, help into work programmes, etc).

Question 3: Do you agree that the ceiling should only apply to social housing rent increases from 1 April 2023 to 31 March 2024, or do you think it should apply for two years (i.e. up to 31 March 2025)?

Response:

Yes. Given the uncertainties we believe any ceiling should apply for up to one year, with a review thereafter. We recognise that both providers and residents/tenants benefit from longer term certainty where possible, but forecasts suggest that inflation should revert within two years. As Savills' analysis shows, until recently many commentators have tended towards a projection of CPI which falls sharply back to the long-term 2% OBR target but over a period of two years. In the last 2-3 months, the trajectory for reduction has tended to be seen to be shorter, with the average of 14 economic forecasters now projecting CPI at 3-4% next September.

The implications of policy announcements towards energy price caps (domestic and business) could also have a significant impact on the level of CPI next September. For example, one report has suggested that the cap on energy prices could have as much as a 5% impact on the overall level of CPI.

Question 4: Do you agree that the proposed ceiling should not apply to the maximum initial rent that may be charged when Social Rent and Affordable Rent properties are first let and subsequently re-let?

Response:

Yes, though we would expect social housing providers to exercise restraint when setting rent levels for new lets or re-lets. It is important that affordable rents remain affordable.

It is worth noting, as Savills' analysis for us sets out, that re-let rates across the social housing stock vary widely but a consolidated average of no more than 3-5% annual churn is experienced across the sector, and in some cases considerably lower. Some properties churn more than once in a 30-year business planning period, some not at all. Savills estimate that only around 75% of stock will turnover in a 30 year business planning period. The impact of this is that the loss of net revenue is never fully recovered, and to the extent that there is any recovery, it is gradual and extends over decades.

Question 5: We are not proposing to make exceptions for particular categories of rented social housing. Do you think any such exceptions should apply and what are your arguments/evidence for this?

Response:

Yes. We believe that supported housing should be exempt from a cap, though recognising that an exemption does not necessarily mean that providers would increase rent by CPI+1%.

Long-term measurements of operating margins within social housing landlords differ significantly between general need and supported housing. Savills' analysis for us notes that supported housing margins can vary between 10-20% and therefore pressure on net operating budgets from a capped rent increase would be significant in terms of service delivery and essential capital investment (e.g., on building safety).

The government's National Statement of Expectations (NSE) of supported housing notes that "supported housing provides crucial help to some of the most vulnerable people in our country". Supported housing provision is already under financial strain, with rising costs for energy, staff, repairs, security, buildings insurance, safety checks, materials and constructions, and reductions in funding from local authorities. A rent cap could punish the best supported housing providers, many of whom are working to help deliver the government Rough Sleeping Strategy. As a recent article in Inside Housing outlines, organisations such as Centrepoint and other homeless or domestic abuse refuges, which are also struggling with soaring energy costs, have done the right thing and increased pay for their hard-working staff without increasing the service charges for the vulnerable people they support. Without an exemption, many such providers will have to find savings. In lots of cases this would mean cutting back on support and being forced to de-prioritise repairs and maintenance (already under pressure).

The cap could also have particularly dire consequences in some managed properties, where organisations are leasing the building where they deliver services, because owners could see their margins tighten beyond profitability and decide the provision is simply not viable. There has already been a significant reduction of bed spaces in the supported housing sector over the past decade. (With the loss of Supporting People and the previous reviews that threatened changes to income streams we saw some providers exit the market, particularly for short term, complex service users.) This bears out in our street homelessness figures. To lose more would seriously undermine the government's commitment to end rough sleeping by the end of this Parliament. Discussions with local authority partners have highlighted concerns that a cap could lead to the collapse of some supported housing providers, resulting in councils having to find alternative specialist housing in a very limited market – or forcing people to accept residential care which they are trying to avoid where they can support people to live independently in the community. This would add to pressure on NHS services.

A higher proportion of supported housing users are in receipt of benefit to cover rent and service charge costs. With an uprating of benefits, they should continue to receive the support they need to meet any increase in rents to cover inflation. A failure to uprate would be very damaging– many working age tenants in supported housing already struggle with finding and maintaining work as they have little disposable income. Older people make up the largest part of this sector and, where in receipt of benefits, are dependent on an uplift to housing and legacy benefits, as well as state pensions. Those with some private income/resources and therefore not eligible to benefits may struggle with a CPI+1% increase so support would need to be put in place to recognise this.

Other comments

<u>Mitigations</u>

Given the pressures outlined above, we believe that financial mitigations should be announced alongside any rent ceiling decision to prevent significant reduction in investment in existing and new homes, including:

- the reintroduction of rent convergence (further details below)
- urgently make available and if possible augment the full Social Housing Decarbonisation Fund (SHDF)
- allowing Recycled Capital Grant Funding (RCGF) to fund major repairs
- additional grant funding for development of affordable homes
- removing VAT on housing provider activity
- greater flexibility over the use of Right to Buy receipts to allow continued delivery in local authorities
- discussions on the post-2025 rent settlement should introduce a long-term approach based on key principles to secure the financial future of the sector and affordability for residents.

Convergence and future rent settlement

We recognise that the government intends to consult on its future rent strategy but would highlight that in our discussions with providers on a possible cap almost all mentioned the need for convergence towards target rents to be allowed for. Many have 'uncollected' rents from properties at below target rent, equivalent to significant sums (one housing association said £20m annually). One way to do this would be to impose the cap on a social landlord's rental income as a whole, so that in practice rents can be raised to different levels within an overall percentage cap. Savills' analysis for us provides more detail on this.

Further, a convergence mechanism would enable providers to continue to invest in new and existing properties with confidence, where income lost through the imposition of a rent cap could be recovered over multiple years upon inflation returning to normal levels. This would allow the investment to continue in both new and existing homes while shielding tenants from cost-of-living increases at this time of high inflation. The rent convergence mechanism could involve registered providers being offered greater flexibility to increase rents, over a number of years, to recoup the income lost through the application of a rent cap, while ensuring that rents did not increase beyond the level allowable under the current Rent Standard. This would involve providers making moderately higher above-inflation rent increases over a number of years once inflation has returned to 'normal' levels. This would smooth rent increases and avoid tenants being faced with significant cost increases in any single year. The current rent mechanism, which allows registered providers to increase rents by up to CPI+1%, does not allow this type of flexibility and incentivises registered providers to apply the maximum rent uplift every year, as failing to do so means losing the potential income in perpetuity.

We welcome the government's confirmation that it will consult next year on rent policy from 2025 onwards. The detail of long-term rent policy will be important in delivering affordable rents for residents and securing future investment in homes and services. We look forward to working with the government on the detail of this consultation.

Impact Assessment

We believe the Impact Assessment which accompanied the consultation significantly underestimates projected losses within the sector which must be considered when mitigating impact. For example, it sets out rent increase 'losses' below the projected level of CPI+1% but this does not take account of lost growth. One large housing association we spoke to said that a 7% cap equates to a 21% cut in new build whereas 3% would mean a 74% cut and would mean exiting from existing schemes on site with consequent wasted (and penalty) costs. Any cuts generated by a rent cap next year will impact new build in 2-3 years, losing momentum which it will take much longer to recover. Further, some landlords would have to renege on existing contracts, incurring wasted costs and delaying schemes for years. There is a particular impact on complex regeneration schemes which require investment over a period of years (e.g. to buy out leaseholders to enable land to be redeveloped).

There are also additional costs related to cutting planned investment programmes. For example, one large London provider told us that their preliminary modelling of repair demand suggested that implementing their Major Works Investment Programme will prevent the need for 7,500 reactive repairs per year after two years – translating to a direct saving of at least £2.19 million each year. Any delays or reductions to major works investment such as this will cancel out some of the savings identified and undermine customer satisfaction.

Given the above we would urge the government to publish a full assessment of economic impacts, including the loss of new development, impact on building safety works, decarbonisation and repairs and maintenance programmes, before making a final decision on next steps.

Service charges

Whilst the consultation paper makes brief reference to service charges, highlighting that these are not subject to the Rent Standard and therefore not able to be influenced by national policy, there is an implication that government wishes providers to exercise restraint and thus consider restricting increases in line with rents. The affordability of service charge increases is extremely important for residents, and social housing providers will be working hard to minimise increases. However, any service charge increase should reflect the actual costs incurred in providing a service, in discussion with residents. As such service charges should not be subject to a cap.

Shared ownership

There is a significant group of tenants not covered by the proposed cap but which should also be considered. Rent increases for shared owners are set out in their leases and linked to the higher RPI rate of inflation plus up to as much as 2% (so 10%+). This could be unsustainable for those facing rising mortgage costs and/or potential bills for building safety. We are aware that many providers are considering what they can do to offer flexibility and targeted support but also that many shared owners are anxious about their ability to meet their housing costs. We are concerned that a cap of 3% or 5% could place greater pressure on shared ownership rent increases.

Support for tenants in the private rented sector

We recognise that this consultation relates to social housing residents but would encourage government to also consider the lot of private renters (in less secure tenancies) facing rising costs. Private rents are increasing at the fastest rate in 16 years and evictions have doubled. Once again, this points to the need for urgent welfare reform (notably benefits uprating (linked to September CPI) and increase to local housing allowance) and for delivery of the government's commitment to introduce renters reform legislation as soon as possible, removing s21 evictions.

We would be happy to discuss any elements of this consultation response further. We remain fully supportive of the new and enhanced consumer regulation which is currently passing through Parliament, as well as the increased role of the Housing Ombudsman which raises the bar of accountability for housing providers. However, as our response seeks to demonstrate, such standards must be supported by the necessary investment. We will be expanding on some elements of this in our forthcoming budget submission.

Contact:
Rachael Williamson, Head of policy and external affairs: rachael.williamson@cih.org

Background on CIH: The Chartered Institute of Housing (CIH) is the independent voice for housing and the home of professional standards. Our goal is simple – to provide housing professionals and their organisations with the advice, support, and knowledge they need. CIH is a registered charity and not-for-profit organisation. This means that the money we make is put back into the organisation and funds the activities we carry out to support the housing sector. We are a registered charity with a Royal Charter, which means that our work is always focused on the public interest. We have a diverse membership of people who work in both the public and private sectors, in 20 countries on five continents across the world. Further information is available at: www.cih.org.