Rent consultation analysis
Resume of analysis

Chartered Institute of Housing

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Rent Consultation analysis: resume and summary

Introduction

The analysis work has been undertaken by Savills Affordable Housing for the Chartered Institute of Housing (CIH) working in association with trade body partners: the National Housing Federation, the Local Government Association, the Association of Retained Council Housing, the National Federation of ALMOs, the Councils with ALMOs Group and the Northern Housing Consortium.

The government published a consultation on the future of Social Housing Rent Policy alongside the Budget on 30th October 2024. The consultation has a closing date of the 23rd December and the various partners commissioned this analysis in order to support their submissions to the consultation.

The work has been undertaken in late November and early December 2024. A detailed analysis is annexed to this summary setting out the bases, inputs, assumptions, outputs, together with a detailed view on the potential implications of each of the rent policy options discussed within the consultation document. This resume provides an overview of the key findings of the analysis.

The key proposals within the consultation are as follows:
- Establish an approach to a longer-term rent settlement across multiple years to deliver stability and predictability – initially for 5 years beginning 2026.27 potential for a rolling 5-year rent setting horizon from 2027.28, or settlement for a further period – up to 10 years
- Allow social rent increases up to CPI+1%
- Views sought on stability, length of settlement, rate of increase, and any other measures in relation to rents that would help housing providers deliver on asset management and ambitions for new supply
- Views also sought on affordability and any other non-rent measures that would assist providers.

The summary below covers an analysis for each of these proposals by adopting an approach to the modelling of five separate scenarios, each set out respectively for the local authority sector and the housing association sector. For each sector, Savills has built upon work undertaken earlier in 2024 on both (May for the housing association sector and September for the local authority sector), making a series of changes to the core input assumptions that reflect economic, inflationary and policy changes since those dates.

The work is intended to exemplify the additional income and therefore additional investment capacity arising from the application of a stabilised rent policy and increases at CPI+1% as opposed to CPI-only. Many within both sectors are keen to stress the need to also consider the reintroduction of convergence of rents to formula rents for social housing tenants as a means of addressing the historic inconsistencies in rents paid by existing tenants and the impact of the 7% rent cap applied to general needs rents in 2023.24.

The analysis also addresses the impact of a longer 10-year rent settlement, including by using equity pricing as a way of quantifying the benefits.

Specifically for the HRA sector, there is also an assessment of the implications for the self-financing settlement of 2012 and any proposal to reopen the settlement.

A high level assessment of affordability is also made.

The analysis provides the basis for assessing the movement in average rents for both housing associations and local authorities under the different scenarios, which can then be converted into additional rent income that might arise from the implementation of different policies, which in turn can then be applied against expenditure within each sector in order to derive the amount of additional headroom for new investment into sector priorities (which include the existing stock and new supply).

The scenarios are as follows:

1. Baseline projection – in turn this incorporates the following high level assumptions
    a. Additions of costs arising from the uplift to employers National Insurance contributions
    b. Property additions for housing associations in line with an assumed reduction from totals in 2023.24
    c. Property reductions for local authorities in line with reduced Right to Buy discounts
    d. CPI+1% rent increase to 2025.26 which is at 2.7%
    e. From 2026 onwards, rent increases at CPI-only.

2. Revised baseline projection CPI+1% for 5 years from 2026-2031 – this reflects the government's intention within the consultation to introduce a 5-year settlement with annual increases of CPI+1%.

3. Revised baseline projection CPI+1% for 10 years from 2026-2036.

4. Convergence scenario with CPI+1% rent increases for 10 years and with local authorities and housing associations reletting vacant properties at formula rent with additional rent convergence in which a fixed amount is added to CPI+1% rent increases for existing tenants until formula rent is met - up to £2/week.

5. As for (4) above but with rent convergence up to £3/week for existing tenants.

Details of the technical inputs and assumptions are set out in the annex.

It should be noted that the baseline projection (scenario 1) is changed since the work earlier this year, primarily reflecting the lower than expected level of September CPI driving rent increases for 2025.26 (2.7% vs 3.5%), the introduction of additional National Insurance costs, and additional inflationary pressures applying particularly to repairs and capital expenditure. For both sectors, the baseline projection is financially worse than earlier in the year, although the forecast for HRAs improves after the short-term as a result of lower Right to Buy sales.

Summary of results: rent forecasts

For local authorities, the average rent in 2023.24 was £99.32 whilst the average formula rent was £105.06. The average "gap" between actual and formula rent was £5.74 or 5.47%.

CPI+1% for rents over 10 years with no convergence would result in average rents of £149.21 compared to £135.36 for CPI-only increases. Average formula rents increasing with CPI+1% would be £157.85 by 2035.36.

Rent increases at CPI+1% + £3/week combined with reletting voids at formula rent would result in convergence with average formula rents in 2032.33. Rent increases at CPI+1% + £2/week would result in rents within 5p/week of convergence with average formula rents by 2035.36.

For housing associations, the average rent in 2023.24 was £109.34 whilst the average formula rent was £112.11. The average "gap" between actual and formula rent was 2.47% (with no tolerances[1] added).

CPI+1% for rents over 10 years with no convergence would results in average rents of £164.28 compared to £149.02 for CPI only increases. Average formula rents increasing with CPI+1% would be £168.43 by 2035.36 (excluding any tolerances).

Rent increases at CPI+1% + £3/week combined with reletting voids at formula rent would result in rents within 2p/week of convergence with average formula rents by 2035.36. Rent increases at CPI+1% + £2/week would result in rents within 16p/week.

Summary of results: additional rent income

For local authorities, the cumulative annual in-year impact of CPI+1% increases over 10 years (compared to CPI-only) increases = £1.1bn per year by 2035.36 – the impact of which would continue all years beyond 2036; this totals cumulative additional income in 10 years of £5.6billion and an estimated cumulative £31billion over a 30-year business planning period.

Conversely, if CPI+1% rent increases are allowed for 5 years only, the impact is much reduced to £0.48bn per year by 2030.31, cumulatively £16billion over 30 years.

The total additional rent income over 10 years from convergence at £2/week and reletting at formula rents would be £5.516billion and at £3/week would be £5.970billion. Table 1.1 shows the outputs.

Table 1.1: Additional rent income from convergence – local authorities

Additional rent income from convergence scenarios	£2 / week convergence	£3/ week convergence
In year impact by 2035.36	£674m	£685m
Cumulative additional rent income 10 years	£5,516m	£5,970m

[1] *Tolerance refers to the ability to be able to relet properties at formula rent plus a tolerance up to a further 5%*

For housing associations, the cumulative annual in-year impact of CPI+1% increases for 10 years (compared to CPI only) increases = £1.4bn per year by 2035.36 – the impact of which would continue all years beyond 2036; this totals cumulative additional income in 10 years of £7.4billion and an estimated cumulative £41billion over a 30-year business planning period.

Conversely, for CPI+1% rent increases for only 5 years, the impact is much reduced to £0.64bn per year by 2030.31, cumulatively £21billion over 30 years.

The total additional rent income over 10 years from convergence at £2/week and reletting at formula rents would be £2.953billion and at £3/week would be £3.284billion. Table 1.2 shows the outputs.

Table 1.2: Additional rent income from convergence – housing associations

Additional rent income from convergence scenarios	£2 / week convergence	£3/ week convergence
In year impact by 2035.36	£379m	£392m
Cumulative additional rent income 10 years	£2,953m	£3,284m

Whilst the above analysis compares projections for rents as a result of CPI+1% increases and convergence in all forms, it is noted that as most providers will usually relet voids at formula rents under the current rent regime, reletting at target at CPI-only might be seen as part of the baseline forecast. This is not 100% the case as many local authorities in particular do not relet at formula rent at this time.

For completeness therefore, we have modelled the future rent forecast with relet at formula rent (based on a national average 5% relet churn) based on a prevailing CPI-only policy. This identifies that:

- c£2.0billion of the additional rent income of £5.97billion over 10 years for local authorities might arise from relet at formula rent.
- c£1.1billion of the additional rent income of £3.28billion over 10 years for local authorities might arise from relet at formula rent.

In overall terms therefore, the total additional rent income from full convergence combined with CPI+1% rent increases for 10 years, compared to actual rents increasing at CPI-only with no convergence at all is as follows:

- An estimated £11.6billion of additional income for local authorities over 10 years.
- An estimated £10.7billion of additional income for housing associations over 10 years.

National projections: financial pressures within an updated baseline projection

Additional income projections arising from changes to rent policy are only one side of the picture. In order to understand the implications for capacity and delivery from rent policy scenarios, there is also a need to understand expenditure pressures. These have intensified during the course of 2024.

A proportion, potentially a large proportion, of any additional rent income arising from higher increases and/or rent convergence will be required to address these additional expenditure pressures.

For example, the implications for both sectors of changes in National Insurance costs are estimated at £50-60million pa for local authorities and over £100million pa for housing associations, with a bigger relative impact on those with high levels of care and support provision. Lower September 2024 inflation at 1.7% compared to the expected 2.5% reduces 2025.26 rent income by c£65m for local authorities and c£105m for housing associations in that year.

There are also major financial pressures from inflation and additional demand applying to repairs / Awaab's Law services, and inflation in capital costs from rising unit rates and progression of stock surveys highlighting challenges with stock conditions, all intensifying during the course of 2024. Both result in inflation well above CPI for repairs and capital expenditure.

Both national financial projections have therefore worsened in the short-medium term as a result of the above pressures.

For local authorities, lower Right to Buy sales volumes result in retention of more net income over the long term and the financial projection is improved after around 5 years.

Summary of results: national projections

For local authorities, at CPI only rent increases, cumulative HRA deficits are over £12billion by 2036.37.

CPI+1% rent increases for 5 years improves the position to a cumulative deficit just below £8billion.

CPI+1% rent increases for 10 years stabilises net rent income by 2036.37 (i.e. the national HRA position is no longer in annual deficit), though cumulative deficits to that point are over £5billion.

If rent convergence applied for local authorities in which voids are relet at formula rent on top of CPI+1% increases and convergence for existing tenants applies at £3/week, this shows the potential for cumulative *surpluses* of up to £1.0billion by 2036.37, potentially enabling all existing stock pressures to be addressed with some capacity for additional development.

This is the only scenario in which the national HRA returns to surplus over the modelling period. However, the projected move to surplus takes effect from 2034, implying that deficits will need to be addressed by resources other than additional rent in the medium-term.

Local authorities would return to surplus earlier with additional subsidy and support to address pressures on the existing stock. The injection of additional resources to address immediate and short-term deficits would release capacity for investment into new supply at an earlier year.

For housing associations, at CPI only rent increases, interest cover declines to c90% for the medium term (on the basis of £40k/unit asset investment).

CPI+1% rent increases for 5 years improves cover to 114% by 2036.37 whilst CPI+1% rent increases for 10 years improves cover to 137% by 2036.37.

If housing associations relet voids at formula rent on top of CPI+1% rent increases and rent convergence for existing tenants was applied at £3/week, this delivers interest cover of around 157% by 2036.37.

If the sector is to target a return to interest cover norms of 150% over a 10-year period, the implied capacity for additional new development (over and above what is already in housing association business plans) is therefore limited.

With the addition of subsidies for the existing stock to cover (for example) building safety and commencing decarbonisation at £2bn a year, and with the positive financing impact of extending affordable housing debt guarantees, capacity for the sector to invest in additional new development rises to around 650,000 additional homes over the period to 2036.37.

For both sectors, a key conclusion is that rent policy itself, even with full convergence, is unlikely to deliver any meaningful additional capacity for additional new supply without the addition of resources to cover financial pressures within the existing stock being made available to unlock the capacity that a stable and predictable rent policy could bring.

Summary of results: potential additional capacity

For both sectors, the principal benefit of additional rent increases in the short-medium term would be to allow business plans to be stabilised on the basis of current delivery. Both sectors are under financial pressure and core projections are for increased costs to deliver on their existing stocks.

For local authorities, the principal benefit of a rent increase policy of CPI+1% would be towards stabilisation of HRA finances into the medium term. Additional annual rent of £487m by the fifth year of a CPI+1% policy would assist in helping reduce annual deficits but not eliminate them. Additional annual rent of £1.1bn by the tenth year of a CPI+1% policy would return the annual HRA position to surplus.

Only a package around full rent convergence in addition to CPI+1% increases would return the national HRA to cumulative surplus in 10 years – by delivering an annual addition to rent income of £687m in the tenth year (based on £3/week).

If all of the additional rent income from convergence were committed to borrowing for development/acquisition, this might suggest c£10bn of additional borrowing capacity. Based on £250k delivery cost and 50% average grant for HRA social rent, this might suggest capacity for up to 80,000 additional homes. In practice, authorities are likely to commit additional rent income to existing stock pressures in order to return to HRA surplus – beyond 2034, capacity for investment rises rapidly and could allow the delivery of an additional 30,000[2] homes from that date.

[2] *This estimate is based on an assessment that authorities may commit a proportion of surpluses (over half) towards new supply*

For housing associations, the principal benefit of a rent increase policy of CPI+1% would be towards stabilisation of housing association finances into the medium term. CPI+1% rent increases for 5 years would help stabilise interest cover to main funder covenants with little or no additional capacity for investment. As a minimum, only CPI+1% for 10 years returns the housing association sector cover to above funder covenants.

Even a package around full rent convergence (including relet using tolerances) does not allow a meaningful increase in investment capacity over a 10-year period.

Only with resources made available for the existing stock, or through other measures such as extending debt guarantees, can capacity be unlocked for a meaningful additional investment into new homes – we have modelled 650,000 over a 10-year period which allows the sector to return to a 150% interest cover norm.

HRA debt settlement

Work undertaken for CIH in the spring of 2024 analysed the impact of a range of changes to government policy since the HRA self-financing settlement of 2012 on the amount of debt that HRAs can support. The methodology adopted is based on revisiting the original settlement by applying various policy and other changes (outside of local authority control which have been since the settlement.

As a general point, much more work would need to be done at the local authority level, particularly for those issues relating to standards (where stock composition would be very different between different authorities), however for rent policy changes, these apply to all authorities.

The original settlement envisaged rent increases at RPI+0.5% for 30 years (equivalent to CPI+1%). The outputs from the previous exercise with an estimated revision to the debt settlement to £11.251bn therefore contains an assumption that rent increases would be CPI+1% in all years from 2025 onwards with no rent convergence.

If rent increases are CPI+1% for only 10 years – the settlement would reduce to £11.024bn. If rent increases are CPI+1% for only 5 years – the settlement would reduce to £10.465n. If rent increases revert to CPI-only all years from 2026, the settlement would reduce to £9.455bn.

The headline finding from this exercise is that, by allowing rent convergence at £3/week and if rent increases were CPI+1% for 10 years reverting to CPI-only thereafter, the debt sustainable by HRAs would be **£12.676bn**.

Equity investment

10 years of certainty over rent policy would give housing association boards and local authority members more confidence to invest in bigger schemes, buy land more strategically, and invest in their supply chains and internal capacity. It may also lead to cheaper debt costs.

All these provide the potential to deliver more new homes more efficiently, than two consecutive five-year settlements with the uncertainty halfway through of one ending and another being confirmed.

One way of quantifying the benefit of a ten-year settlement is to look at how equity investment would be priced differently under the two scenarios (5 years and 10 years).

Savills has worked with a range of investors, fund managers and For Profit RP providers. We have aimed to generate an estimate of the financial and investment premium that predictability in rent policy might deliver.

Social rent is a minority tenure for FPRPs (< 2,000 per the SDR 2024); this means that the issue around convergence back to formula rents is less prevalent amongst FPRPs.

Investor views of risk in relation to various future changes to the investments they make are reflected in the requirement for investment returns; the greater the risk, the higher the return needed. If rent policy is stabilised for 5 or 10 years or longer, the view of risk reduces, investment value increases, return requirements reduce and the capacity for investment and delivery increases.

The additional value derived from CPI+1% rent increases for 5 years would be 0.24% off returns – if CPI-only required 4% yields, this would reduce to 3.76% and represent an increase in capacity of 6%. This would also apply to a 5-year rolling stabilisation policy as decisions are taken on the basis of the position each year.

The additional value derived from CPI+1% rent increases for 10 years would be 0.45% off returns – if CPI-only required 4% yields, this would reduce to 3.55%, an increase in capacity of over 11%. A 10-year settlement would therefore deliver nearly double the additional value.

We estimate that over 10 years, a 5-year rolling settlement might allow delivery of new homes to increase by 40% whilst a 10-year settlement would increase capacity for new homes by 88%. On a purely illustrative basis, if investors were able to finance the delivery of 10,000 new homes annually via development and s106, a 5-year rolling settlement could increase delivery by 40,000 new homes over 10 years, whilst a 10-year settlement could increase delivery by 88,000 over that period.

Affordability: relativity

Savills undertook research into the relative affordability of social rents against market rents in the summer of 2024. The objective was to show how the relative affordability of social rents for an average housing association 2-bed property might change as a result of the introduction of a social rent policy of CPI+1% increases for 10 years from 2026-2036, applied at the local authority area.

The analysis shows that:

- Social rents stay well below market rents in virtually all parts of the country
- In London and the South East, CPI+1% rent increases for social rents maintain them below 50% for most local authority areas
- Only in a handful of authorities (generally those with an under-developed market rented sector), would social rents rise above 80% of market rents over a 10-year period.

The results highlight that there should be confidence that a rent increase policy of CPI+1% will not fundamentally change the relative affordability of social rents compared to the private sector.

Affordability: to tenants

We have compared rent increases implied by changes to rent policy to projections of wage inflation over the next 10 years in order to arrive at a view on the impact on affordability to tenants over time. We have drawn upon material from the CIH (re housing benefit) and the NHF (affordability scenarios for household typologies) in comparing potential future wage inflation projections with increases in average rents under convergence scenarios. We have then converted differential growth in wages against rent increases into an average £/week household pressure. This highlights how rent affordability might change if wage inflation diverges from CPI+1% over the medium term.

Central wage inflation is projected based on OBR forecast: 4.7% in 2024 and 3.6% in 2025 followed by 2.25% pa – we have modelled this at a high of 2.5% and low of 2.0%

If convergence leads to rents rising at the rate set out, the central wage inflation forecast leads to approx. £8 / week additional income that needs to be found to meet higher average rents over time.

This is principally driven by rents rising at CPI+1% (3% pa) and wages forecast at 2.25% pa.

If wage growth is “stagnant” and is the equivalent of CPI, the implied additional affordability pressure is c£12/week by year 10. If wage growth keeps pace with the rate of rent increases, the implied additional affordability pressures is c£4/week by year 10.

However, higher convergence rents in the short-term are potentially able to be matched by higher than CPI wage inflation for wages in the period, indicating that affordability would not be fundamentally affected by convergence as the convergence-period is in the early years.

Therefore, the longer term pressure on affordability arises from CPI+1% being higher than wage inflation.

The majority of social rents are covered by benefits of some kind. On the basis that 65% of rents are covered by benefits and that 55% of tenants are fully covered, affordability pressures are focused onto tenants paying some or all of their rent. For those paying partial rent, increases are likely to be covered by their HB/UC payments. For the minority of tenants paying full rent, the additional pressures arising from faster rent increases with convergence amount to less than £2/week by 2030.

Annex: detailed presentation of analysis

Attached under separate document