A rent pressure zone for Edinburgh?

Review of evidence

Ben Parker on behalf of the Green Group of Councillors in Edinburgh

Ben Parker is a student at the University of Edinburgh

Summary

- In response to concern about rising private rents, the Scottish Parliament has passed new legislation which allows councils to designate areas as rent pressure zones (RPZs), the effect of which is to limit rent rises in existing tenancies.

- Edinburgh has the largest and most expensive private rented sector in Scotland, so is the obvious place to start in examining the case for an RPZ.

- Drawing on both rent officer data and Citylets data as a proxy for rents generally, this report seeks to quantify the scale of rent rises and the impact of limits on rents.

- Between 2010 and 2017, new rents for two bedroom properties in Edinburgh have risen by 39.8% at a time when inflation measured by the consumer price index was 15.6%.

- The rise in rents at rates well in excess of inflation has happened across all postcodes in the city.

- The data appear to suggest that rent rises have been accelerating since 2014.

- Wage income in the bottom 50% of workers has risen by only 8.1% in the period 2010-2016.

- If rents continued to rise at the same rate then, by 2020, 2 bedroom properties would cost 61% more than in 2010.

- Looking across the period 2010-2017, if rents had been capped at inflation + 1%, then they would have risen at not much over half the actual rise rate over the period.

- Looking further ahead, if a cap of inflation + 1% were applied now, tenants could be over £50 a month better off by 2020 than if no cap applied.

- Edinburgh should proceed with implementing an RPZ and it should apply to the whole city. At the same time, the council should press the Scottish Government to improve the evidence base on existing rents and continue to push for rent controls on new lettings as well as those on existing tenancies.

Introduction

Rent pressure zones (RPZ) were introduced by the Private Tenancies (Housing) Scotland Act 2016. They give local authorities new powers to apply to Scottish ministers to designate all or part of their area as such a zone, having the effect of limiting rent rises once a tenancy has started. The limits on rents are set to be at least inflation + 1%. Inflation is measured by the consumer price index (CPI). The limits, if applied, only affect rent rises once tenancies have started. New lets will continue to be determined by the market.

> *Tenant A has been a tenant for a year. After the end of that year the landlord says that the rent will rise by 10%, despite no improvements having been made to the property. The tenant says that the council has designated the area as an RPZ. The Consumer Price Index has risen by 2% in the last year so the rent rise is capped at 3%.*
>
> *Tenant B is a new tenant. The landlord asks for a rent of £880 for the property. Tenant B says that the property was let to the previous tenant at £800, so the rent has risen by 10%. However, the RPZ has no impact on this.*

To introduce an RPZ a council has to show that rents are rising by too much; that those rises are causing undue hardship to tenants; and that the council is coming under increasing pressure to provide housing as a result of those rises.

At the time of writing, the legal power to seek to designate an area as an RPZ is expected to go live in December 2017. If that is the case, then the first applications from Scottish councils could be in early 2018.

This short paper analyses the potential effects of implementing an RPZ in Edinburgh in response to rising rent costs in the city's expanding private rental sector. Reviewing trends in rent rises since 2010, the paper looks at future rent costs based on these trends, and compares these with forecasted rent costs had an RPZ formula of CPI+1% been implemented previously, and if such a formula were to be implemented now.

Reflecting on wage increases in relation to rising prices in the private rental sector, this paper concludes that implementing an RPZ in Edinburgh would go some way to alleviating the strain on Edinburgh's private renters.

Background: Edinburgh’s changing housing landscape

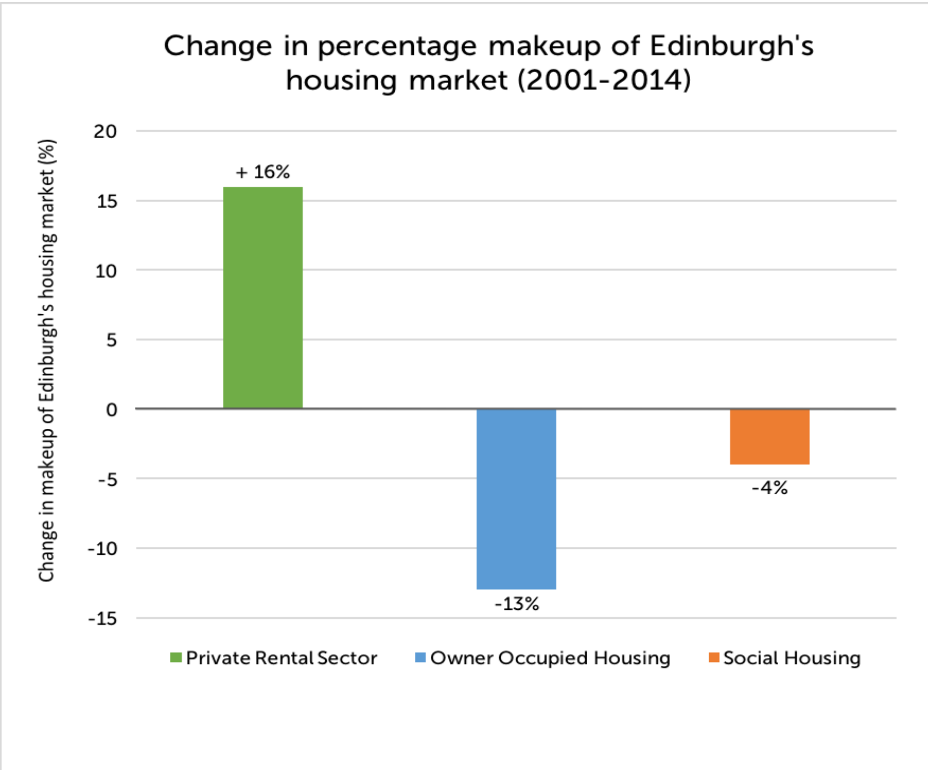
As noted above, councils must show rising private rents are impacting the housing market in order to pursue an RPZ. Edinburgh has a dynamic housing market. In 2014, the city’s housing stock composed of **56% owner occupied housing, 13% social housing and 29% private rental sector housing** (City Housing Strategy, 2016).

These figures represent marked changes from previous years, demonstrating:

- **High growth in the private rental sector**: an increase of 16 percentage points since 2001, and figures more than double the Scottish average of 14%

- **A significant decrease in share of the owner-occupied sector**: from 69% in 2001 to 56% in 2014

- **A small decrease in social housing**: from 17% in 2001 to 13% in 2014, figures significantly below the Scottish average of 23%



Source: Census (2001), City Housing Strategy (2016)

In 2016, Edinburgh was named as the least affordable city in Scotland for house-buying, house prices (on average) being 6.12 times the average gross annual earnings in the city, fuelling a decline in the owner-occupied sector (Bank of Scotland, ‘Affordable Cities Review’, 2016). An accompanying decline in social housing provision means that, for many Edinburgh residents, homes are found in the private rental sector.

Analysing rents in the private rental sector in Edinburgh

In order to get Scottish Government consent to designate an area as an RPZ, the council must submit evidence. The private rented sector is made up of thousands of transactions made between individual tenants and landlords, many of whom own only one or two properties. Resultantly, obtaining comprehensive data to form such evidence is very difficult.

In the analysis below we have used Citylets data; a source drawn on frequently by the city council when analysing the private rented sector. It is the single best data source as it presents data at an Edinburgh and sub-Edinburgh level. There is, however, one caveat with this – Citylets reports new rents, while an RPZ specifically focuses on rent rises *within* a tenancy. So, one assumption made with the data is that new rents can act as a reasonable proxy for the whole rental market. Below we test this assumption using other data sources. While we recognise that this is likely to be an imperfect proxy, we argue that this is not to the extent that it affects our conclusions.

Testing the data

Below, to take one example utilising Citylets data, we show that rents in Edinburgh for 2 bedroom properties have risen by 39.8% between 2010 and 2017. We can compare this figure to one from the Government Rent Officer Service (looking at a mix of rents, not just those new) which shows that rent rises for the Lothian market area have risen by 25.1% for the same size of property, between 2010 and 2016. Much of the difference between the two data sources can be explained by the different timescales and different geography involved in the sample – adopting a wider market area will dampen the higher-cost Edinburgh prices, and collecting data only up to 2016 means one less year of inflation. Although it is possible there is a third effect at play – that of differences between rises in new lets and all rents – we can still claim, with confidence, that both data sources show rent rises significantly in excess of the consumer price index; it is only the scale of increase which is in question[1].

For the rest of this report we draw on Citylets data as Rent Officer data is not available below the level of the Lothian-wide market.

Rent trends in Edinburgh

Since 2010, in Edinburgh, rents in the private rental sector have risen significantly across all sizes of property:

Property Size	Average Rent (Q1, 2010)	Average Rent (Q1, 2017)	% Increase 2010-2017
1 Bed	£520	£705	**+35.6%**
2 Bed	£664	£928	**+39.8%**
3 Bed	£953	£1347	**+41.3%**
4 Bed	£1345	£1861	**+38.4%**

Source: Citylets

Taking 2 bedroom properties as the benchmark, we can conclude that rents have increased by 39.8% in the period 2010-2017.

[1] From Q2 in 2010 to Q2 in 2017, CPI rose by 15.6%. For the same periods 2010-2016 the change is 12.4%.

Rent rises by postcode

These rises are present across all areas of Edinburgh too. Where data are available, between the shorter period of 2012-2017, rent increases across city postcodes for all property sizes are shown to range between 22% and 33.5%, in all cases considerably ahead of CPI for the same period. Taking 2 bedroom properties as a benchmark, the data show:

Postcode	Average Rent - 2 Bedroom (2012)	Average Rent - 2 Bedroom (2017)	% Increase 2012-2017
EH1	£807	£1071	**+32.7%**
EH3	£882	£1195	**+35.5%**
EH4	£735	£901	**+22.6%**
EH5	£618	£787	**+27.3%**
EH6	£655	£815	**+24.4%**
EH7	£679	£870	**+28.1%**
EH8	£675	£895	**+32.6%**
EH9	£749	£944	**+26.0%**
EH10	£769	£960	**+24.8%**
EH11	£655	£820	**+25.2%**
EH12	£709	£938	**+32.3%**

Source: Citylets (data shown for postcodes where the dataset is sufficiently large to use)

We can conclude that rents in the private rental sector then have not only risen significantly across all sizes of property, but that these rises have occurred across the entire geography of Edinburgh too.

This is important. When applying for RPZ status, councils have the choice to seek the status for all or only part of their area. In our view, this choice is to ensure that those councils which have very large geographies, for example Highland or Aberdeenshire, are not left with one-size-fits-all options for their different markets. In Edinburgh, however, there is a clear single housing market wherein all areas have experienced significant upward pressure on rents. So, the city as a whole should be granted RPZ status.

Year on year rent trends

Looking further at data by property size (where sample size is more comprehensive), taking 2 bedroom properties as the benchmark, **in Edinburgh, private renters have seen an increase in rents of 4.9% year on year**, **with higher growth in later years:**

Property Size	10-11	11-12	12-13	13-14	14-15	15-16	16-17	Annual average over period
1 Bed	+2.7%	+1.9%	+2.9%	+5.7%	+4.6%	+9.5%	+4.0%	**+4.5%**
2 Bed	+4.5%	+3.7%	+1.4%	+4.4%	+8.3%	+5.5%	+6.7%	**+4.9%**
3 Bed	+2.7%	+5.0%	+7.0%	+0.5%	+8.7%	+4.4%	+7.4%	**+5.1%**
4 Bed	+5.4%	-1.3%	+7.4%	+3.5%	+7.5%	+7.7%	+3.4%	**+4.8%**

Source: Citylets

This increase in rent costs is well recorded and anticipated. The city council housing strategy notes that "the reduction in home ownership and comparatively low levels of social rented stock mean more people have to rely on the private rented sector, pushing up housing costs in the city" (2016, p.6).

Recognising that these trends are likely to continue, the council must decide whether such rises are fair. Utilising the data, we can look ahead at future rent costs to inform this decision.

Projecting future rents in the private rental sector

In the table below we have modelled a yearly 4.8% rise in rent (slightly below the benchmark of 4.9%). This is only a "what-if" figure, based on recent trends. If anything, it may be a conservative estimate, especially given predictions by commercial analysts who talk of a period of increased yield in the private rented sector. Against these predictions, it is still important to remember the caveat regarding new/renewal lets covered at the start of the report, and changes to more secure tenancies coming in from the end of 2017[2]. Regardless, the data show:

Property Size	2017	2018	2019	2020
1 Bed	£705	£739	£775	£812
2 Bed	£928	£973	£1020	£1069
3 Bed	£1347	£1412	£1480	£1551
4 Bed	£1861	£1951	£2045	£2143

Based on these figures, between the periods of 2010-2020, rent rises are expected to be:

Property Size	2010	2020	Percentage Increase
1 Bed	£520	£812	**+56.2%**
2 Bed	£664	£1068.79	**+61.0%**
3 Bed	£953	£1551.36	**+62.8%**
4 Bed	£1345	£2143.34	**+59.4%**

This "what-if" forecast, taking 2 bedroom properties as the benchmark again, would mean that rents would have increased by 61.0% within the period.

To understand whether such rises represent good value for money for tenants, we can compare the increase in rent costs to the increase in average income.

[2] There is likely to be a lagged effect on the turnover of tenancies, and the turnover in the private rented sector is likely to remain much higher than for other sectors, given the younger, more mobile demographic of tenants.

Average wages

Over the period 2010-2016, median income for full time workers (those working over 30 hours per week (or 25 for teaching professions)) in Scotland has increased year on year. The ONS deems median income the best indication of typical pay as it is not prone to be skewed by small numbers of very high earners. These increases are:

Year	Gross Median Weekly Income (£)	Percentage Increase
2010	£488	
2011	£488.80	**+0.2%**
2012	£497.70	**+2.6%**
2013	£508.70	**+2.2%**
2014	£519.60	**+2.1%**
2015	£527	**+0.4%**
2016	£535	**+1.5%**

Source: Annual Survey Hours and Earnings

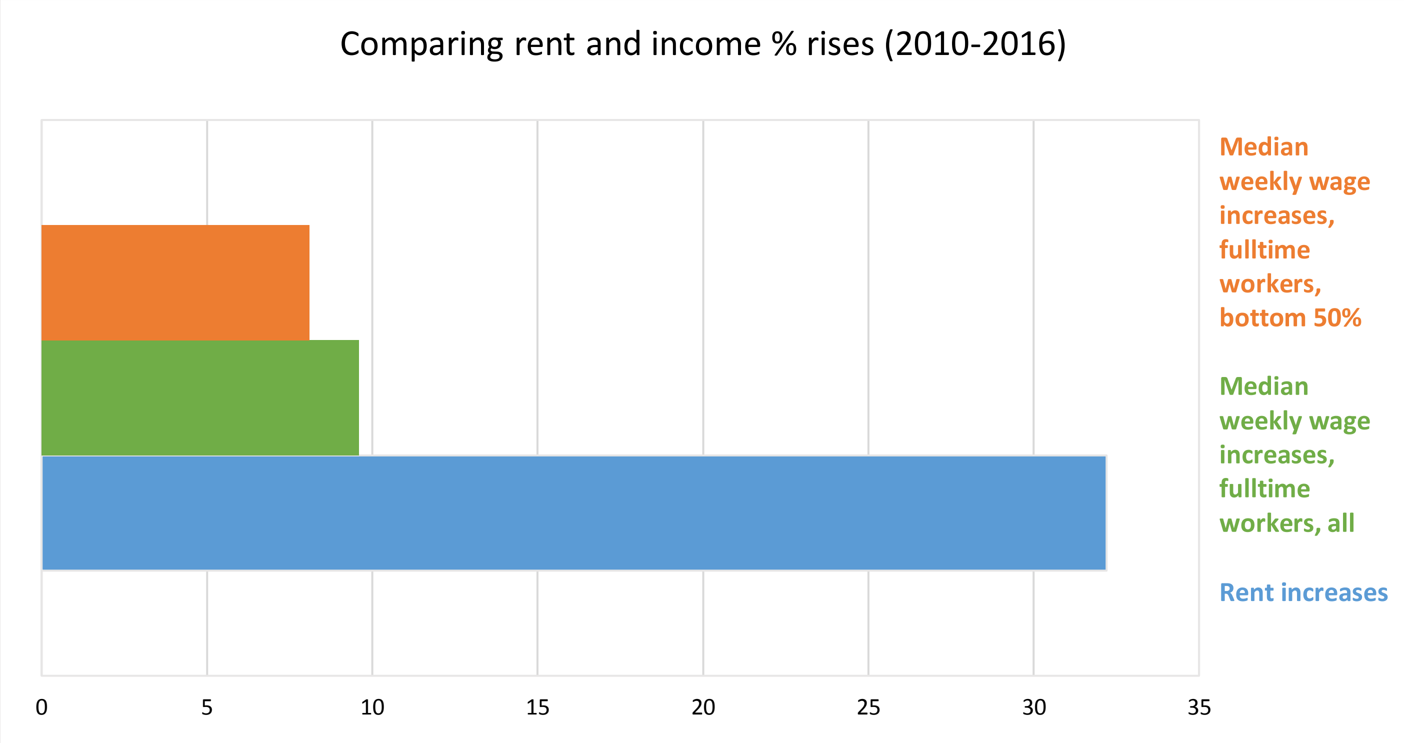
In this period, **gross median weekly income has increased (on average) by 1.5% year on year**. **Over the entire period, gross median weekly income has increased by 9.6%.**

Both of these figures are significantly below the benchmark increase in rents both year on year (4.8%), and over the period (32.2%). Resultantly, rents are becoming significantly less affordable for tenants in the private rental sector.

When we review median weekly income for the bottom two quartiles of the sample – those who are least likely to be home-owners and more likely to be dependent on the private rental sector – wage trends are even starker:

Year	Top threshold of bottom two quartiles (gross weekly income)	Percentage Increase
2010	£498.5	
2011	£500.70	**+0.4%**
2012	£506.10	**+1.1%**
2013	£517.40	**+2.2%**
2014	£518.30	**+0.2%**
2015	£527.10	**+1.7%**
2016	£538.70	**+2.2%**

In this period, the top threshold of the bottom quartiles of gross median weekly income has increased by just 8.1%. **In other words, for the poorest 50% of full time workers, rents have increased at around four times the rate of wages in the same period.**



These data are important because, when reviewing the case for an RPZ, some consideration is needed of the effect that higher rents are having. The comparison with incomes suggests a squeeze is taking place.

Understanding the impact of a rent pressure zone

Under the Private Housing (Tenancies) Scotland Act, a local authority can apply to Scottish Ministers to ask that all or part of the authority's area be designated an RPZ. Being an RPZ means that local authorities can cap rent increases within the designated area.

Such provisions are intended to protect against extreme rent increases in areas where rents are "rising excessively" across most properties (including different property sizes), within the proposed RPZ.

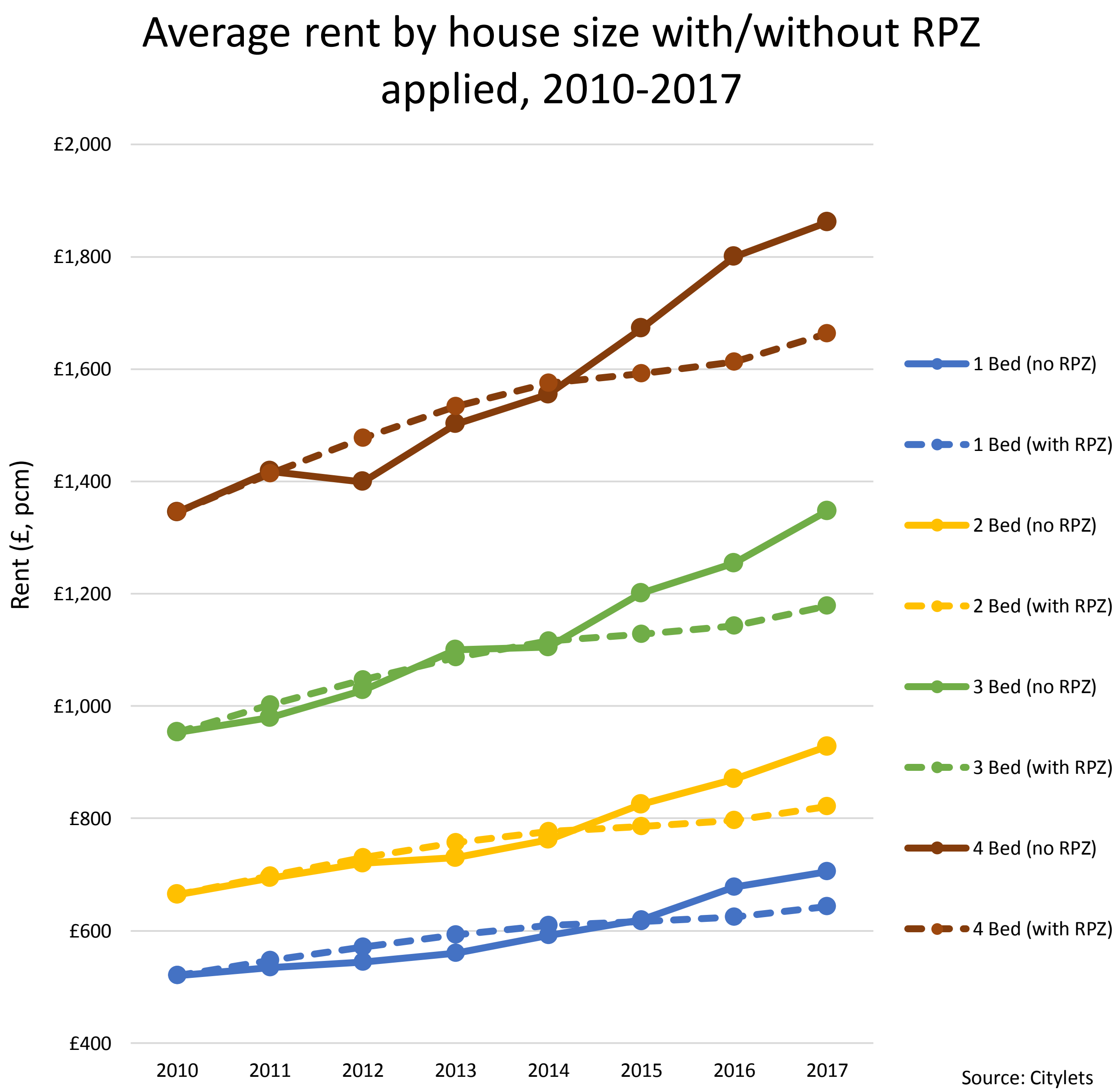
As rent costs have been shown to be rising at a level significantly higher than wages across all of Edinburgh *and* for all property sizes since 2010 (at least), Edinburgh City Council may wish to investigate the implementation of an RPZ as a means of protecting private renters.

Section 38 of the 2016 Act requires that any rent cap set by ministers must allow rents in an RPZ to rise by at least the Consumer Price Index (CPI) + 1% each year; the cap is not intended to keep rent costs constant, merely to limit increases. Utilising this guideline - implementing an RPZ of CPI + 1% - we can use data to model rents had the RPZ formula of CPI+1% been in place since 2010[3].

[3] The same caveat as outlined at the start of the report applies here: that new rents can be a proxy for existing rents.

Year	1 Bed (no RPZ)	1 Bed (with RPZ)	2 Bed (no RPZ)	2 Bed (with RPZ)	3 Bed (no RPZ)	3 Bed (with RPZ)	4 Bed (no RPZ)	4 Bed (with RPZ)
2010	£520	£520	£664	£664	£953	£953	£1345	£1345
2011	£534	£547	£694	£698	£979	£1002	£1418	£1414
2012	£544	£571	£720	£730	£1028	£1047	£1399	£1477
2013	£560	£593	£730	£757	£1100	£1086	£1502	£1533
2014	£592	£609	£762	£777	£1105	£1116	£1555	£1575
2015	£619	£616	£825	£786	£1201	£1128	£1672	£1592
2016	£678	£624	£870	£796	£1254	£1143	£1800	£1613
2017	£705	£643	£928	£821	£1347	£1178	£1861	£1663

These figures are represented in figure 1:



In 2014/2015, rent rises overtook CPI+1% for all property sizes and, by 2017, were well above where rents would have been had CPI+1% been in place. As a change in percentage points, the significance of this difference is clear:

%	1 Bed (no cap)	1 Bed (with CPI+1%)	2 Bed (no cap)	2 Bed (with CPI+1%)	3 Bed (no cap)	3 Bed (with CPI+1%)	4 Bed (no cap)	4 Bed (with CPI+1%
Increase 2010-2017	+35.6%	+23.7%	+39.8%	+23.7%	+41.3%	+23.6%	+38.4%	+23.7%
Difference	**11.9%**		**16.1%**		**17.7%**		**14.7%**	

Hence, it is clear to see the potential of an RPZ. Taking 2 bedroom properties as the benchmark, new let prices have risen at approaching double the rate which they would have, had the RPZ formula of CPI+1% been in place.

We can also look at the effects of implementing the RPZ-type formula were it to be implemented now until 2020, using the (UK) government's own target of maintaining CPI at an average 2% between periods 2018-2020 (Bank of England). Forecasting on the assumption that the government meets this target, figures are:

Property Size	2017	2018 (with RPZ applied)	2019 (with RPZ applied)	2020 (with RPZ applied)	2020 (forecast, without RPZ applied)
1 Bed	£705	£726.15	£747.93	£770.37	£811.96
2 Bed	£928	£955.84	£984.52	£1014.05	£1068.79
3 Bed	£1347	£1387.41	£1429.03	£1471.90	£1551.36
4 Bed	£1861	£1916.83	£1974.33	£2033.56	£2143.34

It is important to be clear what these two tables do/don't show. They don't show how *new* lets would be reduced by an RPZ as any RPZ would not apply to these. However, to the extent that existing rents follow the same trajectory as new lets, the tables do illustrate that capping rent rises, even at just CPI+1%, is likely to have an impact.

The scale of this impact depends on assumptions such as CPI trajectory, the rise in rents in the future (4.8% is used here) and the equivalence of new and existing lets. However, by way of illustration, for 2 bedroom properties, a tenant would be paying just over £50 a month less if RPZ formula of CPI+1% applied than if the market continues to rise unchecked. This is significant.

Conclusion

Private rents are higher in Edinburgh than anywhere else in Scotland. They have been rising over the last 7 years and in a way which appears to be accelerating over recent years. The rises have significantly outstripped incomes. Hence, there is a clear problem to be solved.

This review has argued that implementing an RPZ could play a part in solving that problem. Now the Scottish Government has the powers to act, the city council should be the first in line to use those powers, applying for an RPZ for the whole city.

However, in seeking to take this forward with the Scottish Government, the council may want to pursue two issues, outlined below.

Firstly, of course, this short paper is not fully comprehensive – the council should look to investigate the issues facing Edinburgh's private renters in greater detail. There is a clear need to improve the quality of data on existing rents and those at a local authority level in order to inform this decision, and any application made to the Scottish Government. The Scottish Government must also play a part in this however: its expectations of data and analysis needed in an RPZ application are, arguably, quite onerous. It needs to work with councils and industry experts on some of the data constraints.

Secondly, to the extent that this paper has shown just how dramatic rent rises are and might be for new tenancies, the council need also accept that an RPZ is only one step in the right direction of the wider need to curb high rents in the private rented sector. The option of applying for an RPZ may have been included in the 2016 Act as a very modest measure to fend off pressure to tackle rent rises more generally. However, one impact from this may well be that work investigating the implementation of an RPZ highlights even more starkly the need to control rents in the private market as a whole.