



Housing affordability since 1979: Determinants and solutions

by Ian Mulheim, James Browne, Christos Tsoukalis.

Rents in the private and social rented sectors are close to their highest for decades as a share of tenants' incomes - this report examines why, and the policy options that could help tenants stay afloat.

Housing affordability since 1979: Determinants and solutions

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This study calculates how the level of housing subsidies for renters – through sub-market rents for social housing, private sector rent controls and housing benefits – has changed since 1979. It shows that the waning generosity of these measures can fully explain the deterioration of housing affordability for renters over the past 40 years. The report examines the optimal mix of housing subsidies today, arguing for an expansion of social housing and reforms to housing benefits to improve housing affordability.

What you need to know

- Reversing the decline in housing subsidies is key to enhancing the affordability of housing for renters. The value of housing subsidies has fallen from 16.5% of total day-to-day cost of housing services in the national accounts in 1979 to 11.5% in 2019–20. If housing subsidies had remained at their 1979 levels as a share of total housing costs, they would have been worth £45 billion in 2019–20 rather than their actual level of £31 billion.
- The erosion of subsidies explains the decline in housing affordability for renters over the past 40 years. This underlines the importance of subsidies if housing affordability is to be improved.
- The appropriate mix of housing subsidies should be determined by differentiating between the needs of different household types. Social housing is the most appropriate solution for low-income families with children, pensioners and those with a disability. An additional 700,000 social properties would allow the level of social renting among lower-income families with children to return to its 1979 level and the share of lower-income working-age disabled people living in private rented accommodation to be reduced below 10%.
- Housing Benefit should remain a complementary policy tool to help households who are temporarily poor, or for whom labour mobility and choice are the most important considerations. To improve the experience of renting in the private sector, policy-makers should end the Local Housing Allowance freeze, re-link rates to the 30th percentile of local rents and introduce the reforms to the private rented sector outlined in the recent 'fairer private rented sector' White Paper.

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JRF is working with governments, businesses, communities, charities and individuals to solve UK poverty. *Housing affordability since 1979: determinants and solutions* plays an important part in making sure more people live in a decent, affordable home, a key focus of our [strategy to solve UK poverty](#).

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Executive summary

- Recent years have seen housing affordability become the focus of growing political debate. Rents in both the private and social rented sectors (SRS) are close to their highest for decades as a share of tenants' incomes. This paper examines some of the reasons for the deterioration of affordability for renters and policy options that could be taken in response.
- Rising rents have seen spending on housing benefits grow over the last 30 years. However, housing benefit is only one form of effective subsidy to tenants. In economic terms, sub-market rents for social housing are best seen as a housing subsidy. And rent controls, before the deregulation of the private rented sector in the 1980s, held rents well below their market rate, also effectively providing a subsidy from landlords to tenants.
- These three policy levers – cash payments, social housing and rent controls – all have the effect of lowering the net amount of rent tenants pay out of their own pockets. We therefore refer to them collectively as 'housing subsidies'. This paper attempts to quantify the full impact of changes in these three forms of housing subsidy for renters in England since 1979.
- Non-cash housing subsidies have shrunk markedly over the past 40 years even as spending on housing benefits has increased. The value of housing subsidies has fallen from 16.5% of total day-to-day cost of housing services in the national accounts in 1979 to 11.5% in 2019–20. Had subsidies not been reduced, housing affordability for renters would have been largely unchanged relative to 1979. If housing subsidies had remained at their 1979 levels as a share of total housing costs, they would have been worth £45 billion in 2019–20 rather than their actual level of £31 billion.
- What lies behind this fall in subsidies? Less generous sub-market rents for social housing contributed five percentage points to the reduction in housing subsidies as a share of aggregate UK housing costs seen between 1979 and 2009–10. The social rented sector shrank from 31% to 17% of the English housing stock and social rents moved from around half to two-thirds of market levels. The abolition of private sector rent controls in the 1980s cut the subsidy to renters by a further five percentage points of total housing costs.
- Housing benefits took the strain, increasing from 2.5% to more than 9% of total housing costs between 1979 and 2009–10, offsetting around two-thirds of the decline. But since 2010, reductions in the generosity of housing benefits have cut the share of aggregate housing costs covered by subsidies by a further percentage point.
- Housing subsidies are therefore the most important determinant of housing affordability for lower-income households. If we are to boost affordability, what combination of subsidy measures should Government use? The exchequer cost of providing housing subsidies is inevitably an important consideration in comparing the merits of social housing and housing benefits. Since the Government can borrow more cheaply than private landlords, it will typically be cheaper to use state-backed borrowing to increase the social housing stock than to pay housing benefits to private landlords. Social housing also offers more secure tenancies and stronger work incentives for tenants.
- Despite these advantages, fiscal constraints will always limit the optimal size of the social rented sector. There are disadvantages for tenants too, who have little choice as to the precise location or type of property they are allocated. This may prevent them from taking up employment opportunities outside their local area, hampering productivity in the economy.
- Therefore, housing policy needs to offer a balance of these two forms of subsidy. The appropriate mix should be determined by differentiating between the needs of different household types.
- We argue that for 1.9 million low-income families with children, pensioners and people with a disability, more secure housing tenure should be the priority. Some of these households could be helped into homeownership with the appropriate policy reforms, but for many this will not be an option suggesting significant need for additional social housing. An additional 700,000 social properties would allow the level of social renting among lower-income families with children to return to its 1979 level and the share of lower-income working-age disabled people living in private rented accommodation to be reduced below 10%.

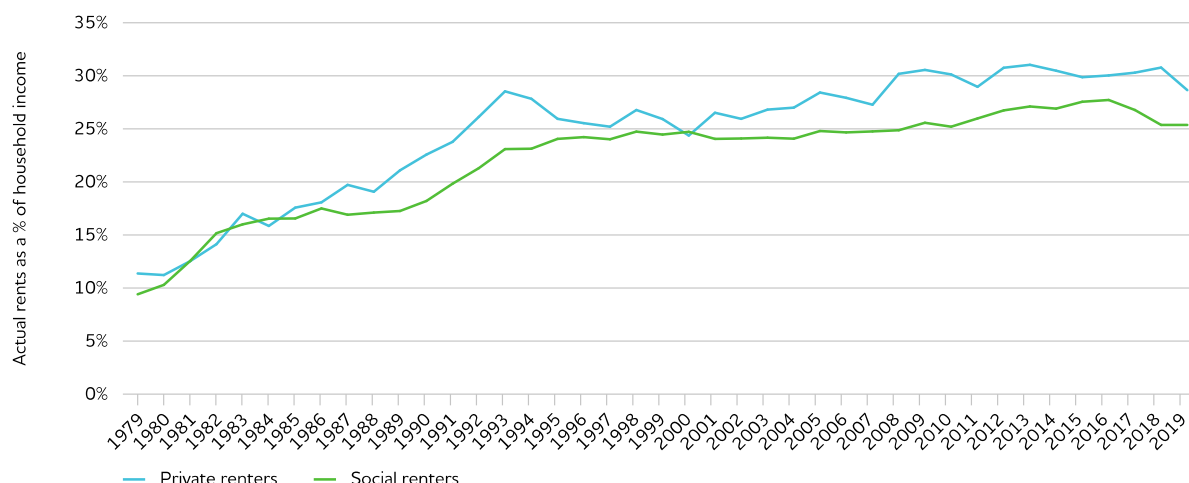
- Supporting, through Housing Benefit, households in the private rented sector who are temporarily poor, or for whom labour mobility and choice are the most important considerations, will remain an important policy tool. To enhance the experience of renting in the private sector, policy-makers should end the Local Housing Allowance freeze and re-link rates to the 30th percentile of local rents and introduce the reforms to the private rented sector outlined in the recent 'fairer private rented sector' White Paper.
- The housing affordability crisis for renters is firmly grounded in the waning generosity of the subsidies on offer to lower-income households over the past 40 years. Consequently, there is no credible route to significantly improving affordability that does not involve rebuilding some of those support systems. On both social and economic grounds, there is a strong case for action.

1 Introduction

Housing affordability is high on the political agenda. Since the early 1980s, rents in both private and social rented housing have risen well above their level in earlier decades as a proportion of tenants' incomes (Figure 1).¹ At the same time, rising house prices and a lack of availability of high loan-to-value mortgages has made it harder for prospective first-time buyers to get on the property ladder (Mulheim et al, 2022).

What lies behind this reduction in housing affordability for renters? Successive governments have blamed an inadequate rate of new housing supply for pushing up the cost of housing. As a result, for the past 20 years at least, the dominant policy prescription to address the housing crisis has been to increase the rate of supply. But an exploration of how housing policy has evolved over the past 40 years suggests that a significant factor behind rising rents is large changes in policies that previously allowed tenants to pay rents at sub-market rates, both in social housing and in the private rented sector. These changes have been accompanied by growing concern in some quarters about rising expenditure on housing benefits.

Figure 1: Out-of-pocket costs of rented housing have been growing as a share of income²



Source: TBI calculations using Households Below Average Income data.

In reality these trends are inextricably linked. Taking a holistic view, three policy levers – housing benefits, social housing and rent controls – all have the potential to lower the amount of rent that tenants pay out of their own pockets. We therefore refer to them collectively as ‘housing subsidies’. Overall, these housing subsidies have shrunk over the past 40 years, not increased.

Forty years ago, the rented sector looked very different from today. The private rented sector was small, only 11.5% of the housing stock in England in 1979,³ and subject to rent controls that made owning rental property unattractive. The size of the sector had been gradually declining over time as landlords sold up and few new properties entered the rental market. By contrast, the social rented sector was much larger at 30% of the housing stock in England and, as is still the case today, rents were set at affordable levels.⁴ As a result, all renters paid rents that were below the levels that would have prevailed in an unrestricted market.

Since then, we have seen cash support through Housing Benefit and Universal Credit emerge as the primary forms of assistance with housing costs for lower-income households. But as the benefits bill has soared in response to a smaller social rented sector, rent deregulation in the private sector and lower homeownership, the past decade has seen reductions in the generosity of these schemes, principally by lowering the maximum amount renters can claim towards their housing costs.

The full scale of these major policy changes on housing affordability for renters has never been quantitatively explored. In this paper, we seek to fill this gap by quantifying the size and distribution of housing subsidies in England through these three channels – sub-market rents for social properties, private sector rent controls and cash support for housing costs – over the 40-year period from 1979 to 2019.

We define subsidies here in an economic sense – the difference between the rent a tenant would have to pay in the open market and the amount they actually pay out of their own pocket. This is a static analysis – we do not attempt to model what would happen in the absence of housing subsidies. For example, rents might fall since many tenants would be unable to afford the full market rent for their current property. Moreover, if there was no social housing, the housing stock and hence the accommodation available to families would look very different. Our analysis abstracts from these issues, simply showing how the level of support for housing costs has changed over time.

This analysis focuses on financial support for renters. We do not include measures designed to subsidise homeownership such as ‘right to buy’ sales at sub-market prices, mortgage interest tax relief (MIRAS) and support for mortgage interest (SMI) through the benefits system in our analysis.

Homeownership subsidies have a distinct policy goal because they are not only paid to allow a household to obtain housing *services*, but for them to purchase housing *assets*. Moreover, homeownership subsidies are different because they are generally not targeted at people who would otherwise struggle to put a roof over their head. If the subsidies that support rental costs, which we study in this paper, are well targeted, there will not be much overlap between their beneficiaries and those of measures to subsidise homeownership.

For this paper’s analysis we use data from the Household Below Average Incomes (HBAI) series, which was derived from the Family Expenditure Survey (FES) until 1994 and the Family Resources Survey (FRS) since then, as the base data for our analysis.⁵ All figures in this report are expressed in 2019–20 prices, indexed using a version of the CPI that includes mortgage interest payments, insurance and ground rent for owner occupiers as this is the measure used in the official HBAI statistics.

First describe the main changes to social housing, private sector rents and housing benefits since 1979 and explain our methodology for calculating the scale and distribution of each form of subsidy before bringing everything together to examine what has happened to housing subsidies overall during this period. We then move beyond describing the key trends to discuss which forms of housing subsidy are most appropriate for different groups and what this means for policy if housing affordability is to be improved.

2 Changing housing subsidies since 1979

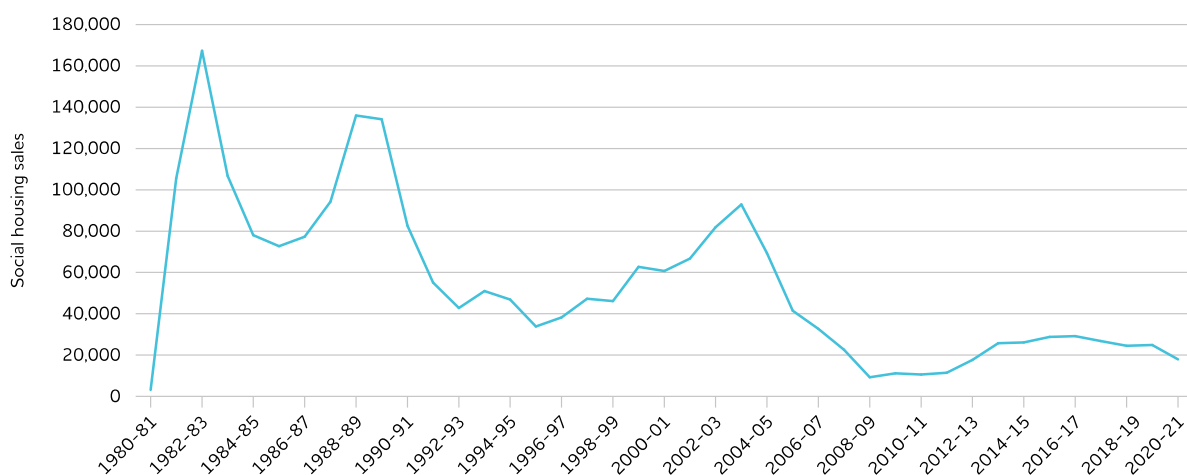
In this section, we outline the reforms to social housing, the private rented sector and Housing Benefit since 1979. We then set out our methodology for quantifying the cash value of these different forms of support and examine how their generosity has changed over the 40-year period under investigation.

Social housing

Social housing is let to tenants at rents that are deliberately kept at an affordable level below the rents it would command on the open market. In economic terms, this represents an effective subsidy to tenants and an opportunity cost to social housing providers from not charging the maximum rent that could be obtained. This economic subsidy is different from public spending on the construction or maintenance of social properties.

As previously mentioned, the big change to the social housing sector over the 1980s and 1990s was the reduction in its size. By the mid-2000s far fewer households benefitted from the sub-market rents and security of tenure available to social tenants. This was chiefly due to the right to buy offered to social tenants from 1980 onwards. The size of the discounts offered to social tenants – initially ranging from 30% to 50% of the market value depending on the length of tenure, later increased to between 44% and 70% for flats, with a maximum discount of £50,000 – made it an attractive option for those able to afford the mortgage repayments. As a result, there were large numbers of sales to social tenants in three waves between 1980 and 2005: as soon as it was introduced, during the boom of the late 1980s and in the early 2000s (Figure 2).

Figure 2: Social housing sales in England



Source: Department for Levelling Up, Housing and Communities statistics (DLUHC), live table 684.

By the time of the financial crisis of 2008, right to buy sales had slowed to a trickle. This was due to several factors. First, the Labour Government in power from 1997 to 2010 sought to reduce maximum discounts available to those seeking to buy their home to ensure value for money and limit the decline in social housing in certain areas. As house prices rose over this period, these limits became increasingly binding, reducing the discount available to tenants in proportional terms.⁶ The minimum time tenants had to live in their home before being eligible to buy was also extended from two to four years. Second, large-scale voluntary transfers of social properties from local authorities to housing associations reduced the number of tenants who had a right to buy. Housing association properties were excluded from the Right to Buy scheme under the 1980 Act. Although sitting tenants at the time of transfers to housing associations retained their right to buy, new housing association tenants did not. As the number of

housing association properties has increased from less than 0.5 million in 1979 to 2.5 million by 2019, those eligible to exercise the right to buy at a significant discount became a smaller and smaller group.

Since 2010, there have been attempts to 'revitalise' the right to buy by the Coalition and Conservative Governments. Larger discounts have boosted the number of right to buy sales a little, but overall numbers remain low. And pledges to extend the right to buy to all housing association tenants, which would involve government compensating housing associations for the discount they would be obliged to offer, are yet to be implemented.

As well as changes in the number of households receiving the benefits of sub-market rents in social housing, there have also been changes in the size of the subsidy offered to tenants. The Conservative Governments of the 1980s and 1990s sought to increase social rents closer to market levels. The 1980 Housing Act that introduced the right to buy also gave ministers the power to set a target annual rent increase for local authorities (Fee, 2009). As the Government wanted to save money by reducing housing grants to local authorities, council rents increased by 165% in cash terms between 1979–80 and 1988–99 (Balchin and Rhoden, 2002).

However, there remained significant differences between rent *levels* in different local authorities, and between local authority rented and housing association properties. These reflected when and where the housing had been built over many decades; changes in the capital and revenue subsidies given to social landlords; and the different rent policies pursued (Wilson, 2019). In 2002, the Labour Government sought to rationalise rent levels across the social sector by setting a 'target rent' for each property. The target rent was set according to a formula and depended on the property's size, its estimated value and local earnings levels. It was intended that all social rents would ultimately converge to their target level, but to avoid dramatic changes in rents, tenants paying less than the target level saw their rents converge at a rate of £2 a week every year. However, these target rents remained well below market levels, and were increased in line with RPI inflation + 0.5% each year.

The Coalition Government between 2010 and 2015 largely maintained this policy; rents had thus for the most part converged with the target rent by 2015. At this point, further convergence was considered unnecessary and it was announced that social rents would rise in line with CPI inflation + 1% each year for the next decade. But after only a year, the new Conservative Government decided to impose a 1% nominal reduction in rents for the four years between 2016–17 and 2020–21. This effectively increased the subsidy provided through sub-market rents for social housing and decreased that provided through housing benefits – the key objective behind the measure.

This was not the only innovation in rent policy during the 2010s. A new form of 'affordable rent', set at up to 80% of market levels, was also introduced. By charging a higher rent, housing providers would be able to build more social rented properties for each pound of grant funding given and raise finance from other sources. 183,675 new homes were provided for affordable rent between 2011–12 and 2020–21, and a further 120,581 homes were converted from social rent to affordable rent.

Finally, the Coalition Government tried to increase rents towards market levels for high-income tenants. From 2012, social housing providers were permitted to charge up to the market rent to tenants with a household income of at least £60,000 a year. In 2015, the Conservative Government announced that this would become compulsory for tenants with a household income of more than £40,000 a year in London and £31,000 a year elsewhere, but ultimately decided not to go ahead with this approach. It is not clear that any social housing providers have implemented such a 'pay to stay' policy. Social landlords do not have access to data on their tenants' incomes, so felt that the administrative costs of implementing a scheme requiring this information to be collected and rents recalculated at frequent intervals would be prohibitive, particularly as it would be unlikely to raise significant revenues in the first place (Wilson, 2017).

Methodology

To quantify the value of the subsidy to social renters through below-market rents, we need to estimate what would be the market rent for each social renter observed in our base data and compare this with the (observed) rent they actually pay.

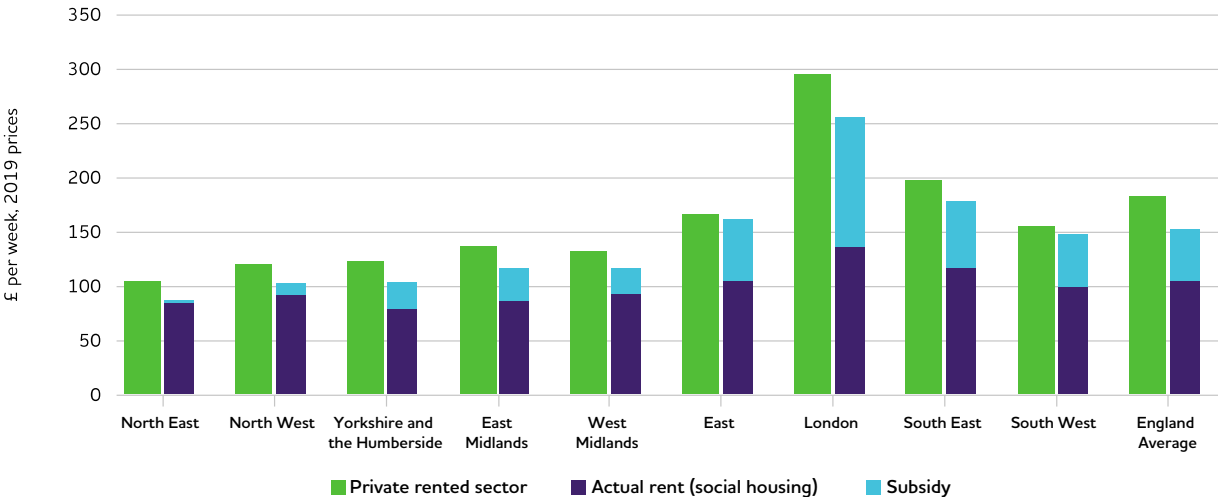
Following a methodology originally designed by Professor Steve Wilcox (2009), we first estimate the would-be market rents by multiplying estimates of the value of social rented properties collected as part of the exercise to calculate 'target rents' (described above) by estimates of the net rental yield on private residential property. These are obtained from the data and analytics company MSCI from 2001 onwards, as this is the earliest year for which consistent data are available. For earlier years, we assume that the spread of net rental yields over index-linked bond yields would have been the same pre-2001 as it has been on average since 2001.⁷ We then add on average maintenance and management costs in the social sector obtained from housing association global accounts. A more detailed account of the calculation of each of these elements is given in Appendix A.

Results

Our methodology enables us to estimate what the rents of social housing would have been (by region and property size) had these properties been rented out in the private rented sector. Merging this information with Family Expenditure Survey/Family Resources Survey (FES/FRS) data on actual social housing rents by local authority and property size, we can compare these estimates of market rents for social sector properties with those for similar properties in the private sector, and with the rents actually paid by social tenants (Figure 3).

In 2019–20, our estimated market rents for social properties were around 15% lower than rents prevailing in the private rented sector in each region for similar properties. This is not surprising given the nature of social properties (typically of lower quality than average and in less desirable locations). The extent of the subsidy to market rents varies significantly by region. In the North East of England, the rents charged to social tenants were close to our estimate of the market level (only 3% lower). But in London, the effective subsidy to social tenants was much larger: social rents were scarcely half of market levels.⁸

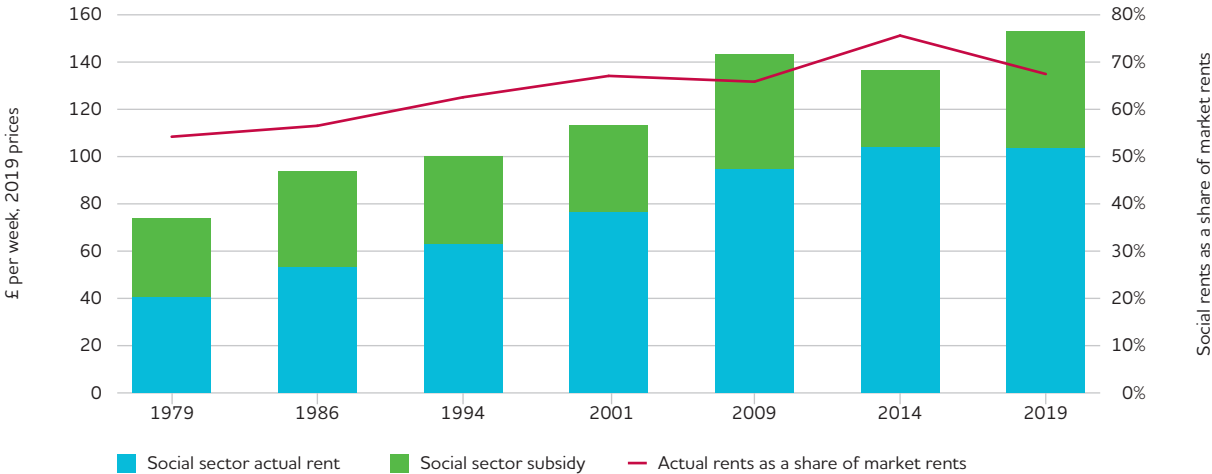
Figure 3: In 2019–20, social rents were around two-thirds of market values, but with significant variation by region



Source: TBI calculations using 2019–20 HBAI and FRS data and methodology described in the text.

How has this subsidy level changed over time? First, social rents have moved closer to market levels, in line with the policies of various governments (Figure 4). However, there has been a slight exception to this trend in recent years due to 1% nominal rent cuts each year between 2015–16 and 2019–20, more than offsetting the greater use of the intermediate 'affordable' rent in the sector over this period. Note that we do not calculate market rents for all years – this is both to keep the analysis tractable (manageable) and because our methodology works less well during housing booms when rental yields fall well below their long-term average relative to index-linked bond yields. We therefore avoid the years around the late 1980s and the mid-2000s.

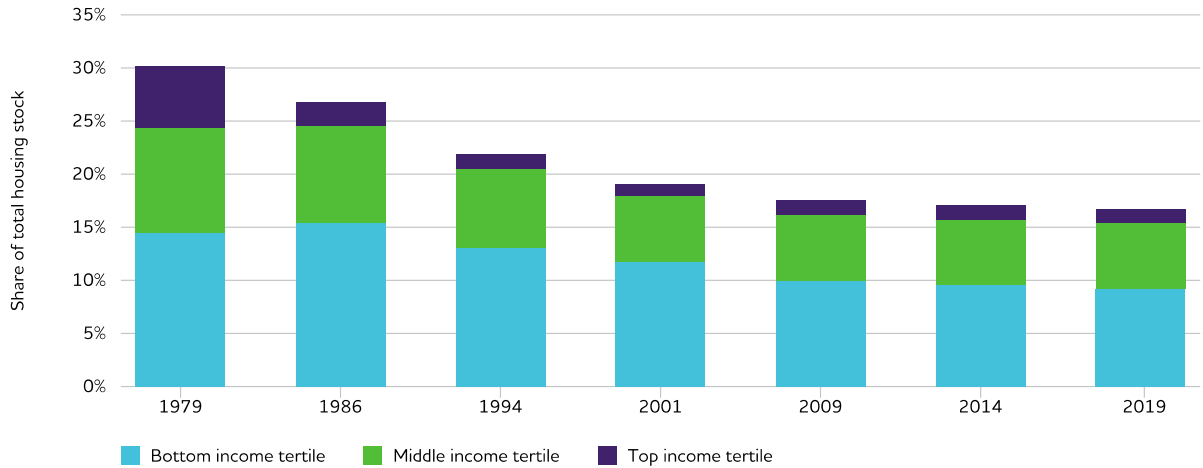
Figure 4: Social rents have moved closer to market levels over time



Source: TBI calculations using HBAI, FES and FRS data, various years, and methodology described in the text.

The second change is that following the introduction of the right to buy in 1980, the social rented sector has shrunk substantially from over 30% of the total housing stock to around 17% (Figure 5). A smaller share of tenants therefore benefits from the sub-market rents associated with social housing.

Figure 5: Income levels of tenants in the social rented sector, 1979–2019



Source: TBI calculations using HBAI data, various years, and methodology described in the text.

Finally, the targeting of social housing towards lower-income households has also changed over time. Social renting was much more common among higher-income groups in 1979 than it is today, but those with high incomes were easily able to take advantage of the right to buy in the early 1980s whereas those with lower incomes were left behind, making the remaining social housing more targeted towards the poor.

However, social housing has become less well targeted on lower-income households since 2001. With relatively few social properties becoming available, many of those with lower incomes who would have previously been offered social housing are stuck in the private rented sector. 46% of 25 to 45-year-olds in the lowest-income third of households were in social housing in 1979. This fell to 40% by 2001 and just 32% by 2019–20.

The total subsidy to tenants from sub-market rents for social housing has thus fallen over the last 40 years. Social housing not only represents a smaller fraction of the total housing stock than in 1979, but social tenants also receive a less generous discount relative to the market rent.

Housing benefits

Expenditure on housing benefits has increased significantly over the last 40 years, but cash support for housing costs has also experienced several structural changes.

Cash support for housing costs has long been a thorny policy issue. The wartime Beveridge report identified the 'problem of rent' – that differential housing costs by region made a flat-rate allowance impossible, but paying actual housing costs incentivised people to move to more expensive accommodation before they retired. But it did not come up with a satisfactory solution.

The solution devised was to provide means-tested support for housing costs through National Assistance, which thus became a larger part of the system than Beveridge had intended. Rent rebate schemes were also introduced by local authorities: by the late 1960s, there were around 3,000 such schemes, with 1,500 unique sets of rules (Reddin, 1968). Many of these were poorly designed and often created situations where the withdrawal of means-tested support meant that an increase in income could leave someone worse off.

A model scheme of rent rebates and allowances was introduced in 1972 to alleviate these problems. Support for housing costs was also available through Supplementary Benefit (a generalised minimum income benefit similar to Income Support). But this caused problems as families could receive a different amount of support depending on which form of support they claimed. Families often chose the 'wrong' benefit: in 1975, the Department for Health and Social Security estimated that around 300,000 claimants of Supplementary Benefit would have been better off claiming housing benefits, and around 100,000 claimants of housing benefits would have been better off claiming Supplementary Benefit (NAO, 1984).

A reform in 1983 sought to address these problems but did not fully integrate the schemes for those in and out of work and was beset by administrative difficulties (House of Commons Social Security Committee, 2000). Full integration of support for housing costs for those in and out of work was only achieved following the Fowler reforms of 1988, which introduced the Housing Benefit system that still exists today.

While rents in both the social and private rented sector were deliberately kept low, Housing Benefit entitlements were low and represented a small share of benefits spending. This changed as social rents were increased during the 1980s, a large portion of the social rented stock was sold off, and private sector rents were deregulated from 1989. The inevitable result was that Housing Benefit expenditure jumped, with spending doubling in real terms between 1988–89 and 1994–95.

In the face of rapidly rising expenditure, attempts were made by governments to limit benefit entitlements. In 1996, a series of changes was introduced for new claimants in the private rented sector. First, the maximum amount payable was limited to the 'local reference rent' – the average rent for a property of that size in the locality. Second, single people under 25 were only allowed to claim for the cost of a room in a shared house rather than their own property. These reforms reduced the size of average benefit awards by about 10%, though there was some evidence that tenants were able to negotiate their rent downward in response to the changes. Previously, tenants had little incentive to negotiate their rent downwards as it would be covered by Housing Benefit unless deemed to be higher than the market rent for the property (Gibbons and Manning, 2006).

The introduction of Local Housing Allowance in 2008 was the biggest change during the Labour Government's time in office. In an attempt to encourage tenants to choose cheaper properties or negotiate harder with landlords, tenants were allowed to keep up to £15 a week if the allowance amount for their area was above the amount they paid in rent. The allowance was also paid to tenants in most cases rather than directly to landlords.

A series of cuts to Local Housing Allowance was introduced after 2010: the £15 excess was scrapped, and the allowance rates were reduced from the median local rent to the 30th percentile in 2011. There was little evidence that these changes reduced the rents paid by tenants: they tended to make up the difference from other income when benefit entitlements fell rather than being able to negotiate a

reduction in the rent payable (Brewer et al, 2019). Subsequently, the maximum rents that can be claimed in LHA have not kept pace with inflation: they were increased by just 1% in nominal terms in 2014–15 and 2015–16 and then frozen in cash terms until 2020–21. During the pandemic, rates were increased to the 30th percentile of local rents again, but since then have again been frozen in cash terms.

The last 10 years have also seen a far more radical change to the structure of housing benefits. Housing Benefit is one of six means-tested benefits in the process of being integrated into Universal Credit. This does not change the maximum amount of support that can be claimed but does alter how support with housing costs changes as income rises, as all means-tested support is withdrawn in a single taper (Brewer et al, 2012).

Methodology

The Department for Work and Pensions' benefit expenditure tables provide statistics on aggregate spending on Housing Benefit in Great Britain over the period we are looking at. Breakdowns for the three constituent nations are only available since 1991–92, so we attribute 85% of spending in Great Britain to England before this, in line with the breakdown in 1991–92.

We also need to add support for housing costs through Universal Credit (UC) to this figure. The DWP benefit expenditure tables only include this spending for 2019–20 despite the rollout of UC starting in 2014–15. To estimate support for housing costs through UC in earlier years, we use the tax-benefit microsimulation model UKMOD (Richiardi et al, 2021). UKMOD calculates benefit entitlements for households in the Family Resources Survey data we use in our analysis, and explicitly models the transition to UC. We calculate the housing element of UC for each household by modelling their entitlements under a scenario where the housing element of UC is switched off. This enables us to estimate growth in total spending on cash support for housing costs over the period from 2014–15 to 2018–19. This method gauges growth in total spending between 2014–15 and 2019–20 quite precisely, so we can be confident that it provides an accurate assessment of the path of spending over the previous four years too.

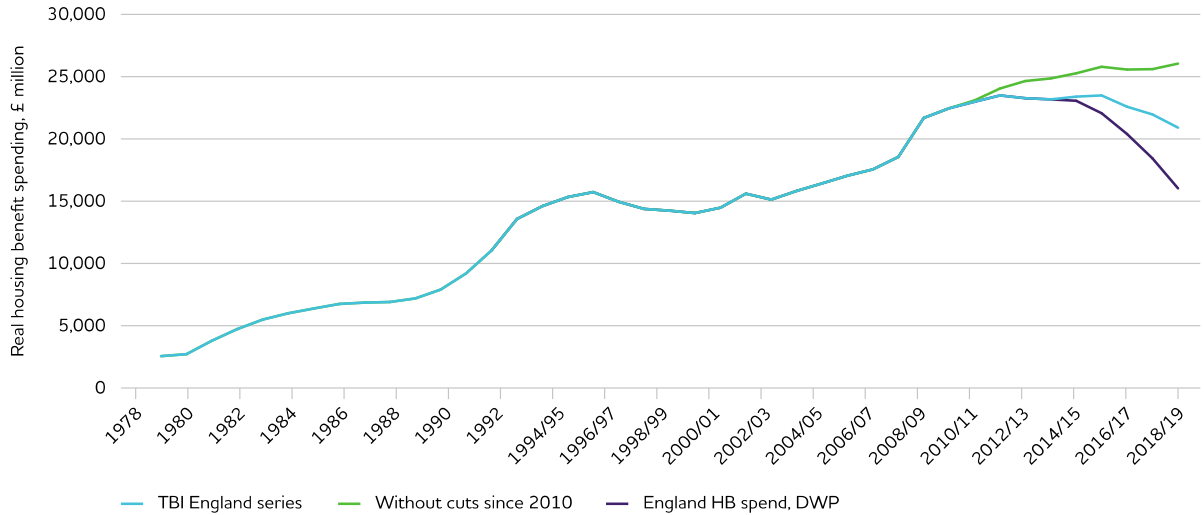
The benefit expenditure tables provide data on total spending, but not on the distribution of spending between income groups and regions. The HBAI data we use does contain this information, but it is well known that this data under-records total expenditure (DWP, 2022). This remains the case when we use UKMOD to estimate entitlements to Housing Benefit and the housing costs element of UC in the years covered by UKMOD (2005 onwards). We therefore scale up spending for each English region and income group to match our measure of total expenditure derived from the benefit expenditure tables.

Results

With a smaller social rented sector and rents having been increased, the need for housing benefits to help low-income tenants with their higher private rented sector housing costs has increased substantially. It was a deliberate policy decision of successive governments to shift the balance of subsidies in this way to better target them on those with the lowest incomes, and it is not surprising to see increased expenditure as a result.⁹

Our time series of total expenditure on Housing Benefit and the housing element of UC is shown in Figure 6. It shows the big expansion in spending during the 1980s and 1990s as rents were increased in both the social and private rented sectors, and slower growth during the 2000s. The impact of recessions in the early 1990s and late 2000s, increasing benefit spending, is also apparent. In recent years, spending has remained flat or fallen slightly. This is partly because wage growth has been weak, reducing upwards pressure on rents, but also because of cuts in the generosity of the scheme. Using the Office for Budget Responsibility's (OBR's) estimates of the savings from these changes, we can see that without them, spending would have continued to grow.

Figure 6: Spending on cash support for housing costs in England, 1979 to 2019–20

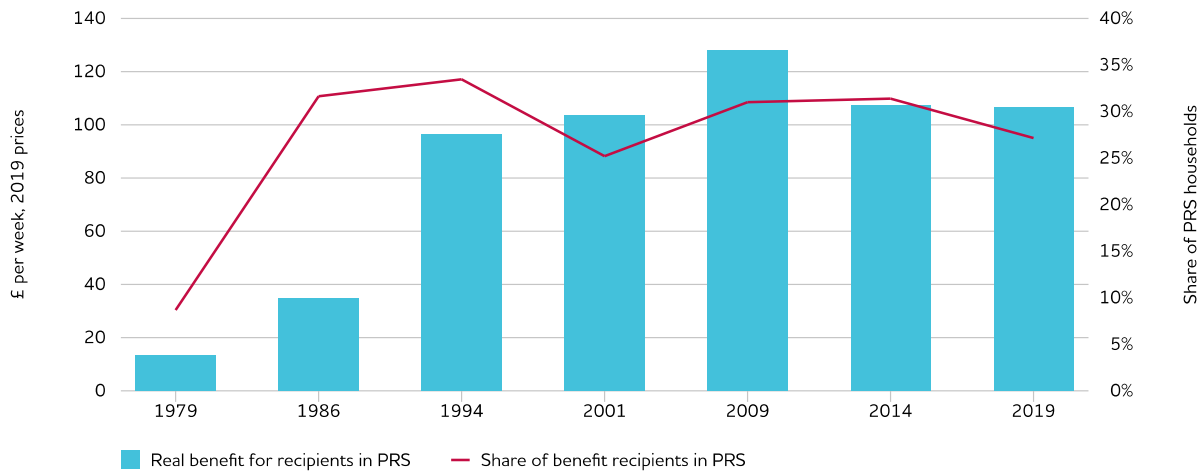


Source: TBI calculations using DWP benefit expenditure tables, OBR policy measures database and UKMOD run on the Family Resources Survey 2014–15 to 2019–20. The results presented here are based on UKMOD version A3.5+. UKMOD is maintained, developed and managed by the Centre for Microsimulation and Policy Analysis at the Institute for Social and Economic Research (ISER), University of Essex. The results and their interpretation are the sole responsibility of TBI.

Thus, although housing benefits have ‘taken the strain’ as subsidies via sub-market rents for social housing and private sector rent controls have fallen away, more recently their generosity has decreased.

Cuts in generosity have primarily affected the private rented sector (Figure 7). The share of households receiving some support towards their housing costs through cash benefits has remained fairly constant since the mid-1980s, at between one-quarter and one-third, despite the growth and changing composition of the sector. However, the share of rent covered by housing benefits fell between 2010 and 2019. Average benefit awards peaked in 2009, reflecting higher numbers of workless claimants following the global financial crisis. As the economy recovered, the number of working claimants increased, lowering average awards: DWP benefit expenditure tables reveal that the share of HB claimants receiving no other out-of-work benefit doubled from 10% in 2008–09 to 20% by 2013–14. But reductions in the generosity of Housing Benefit also played a role. These measures reduced the cost of housing benefits by around £5 billion in 2019–20.

Figure 7: Average Housing Benefit awards in the private rented sector have remained steady as rents have increased since 2010

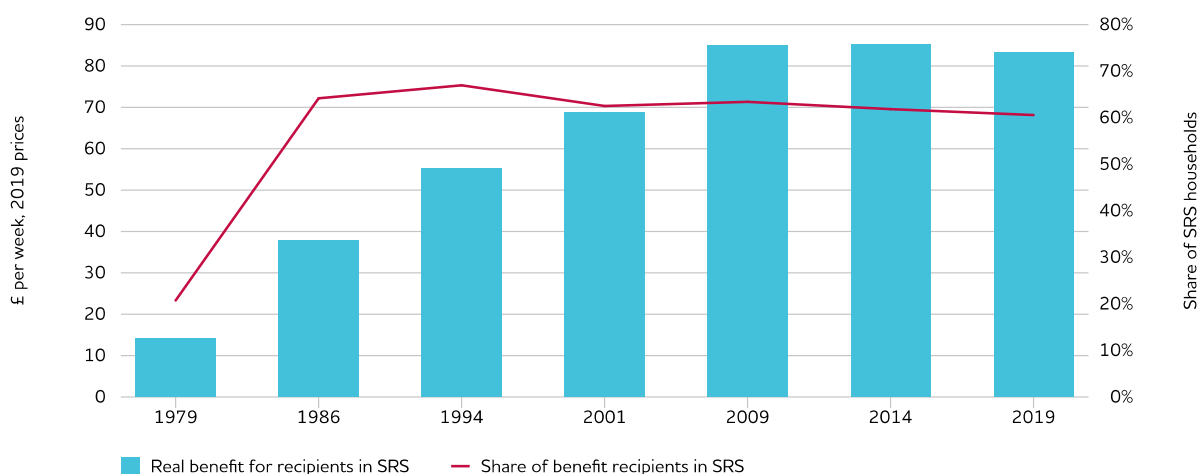


Source: TBI calculations using HBAI data, various years, and methodology described in the text.

In the social rented sector, by contrast, there was no effective reduction in the generosity of benefits since restrictions on the maximum rent that can be claimed tend to be above rent levels in the sector.

Both average benefits in the social rented sector and average benefits among recipients in the social rented sector have remained steady. Moreover, the share of households in the social rented sector that receive housing benefits has shown little change since the mid-1980s (Figure 8). The reduction in housing subsidies through housing benefits was thus concentrated in the private rented sector.

Figure 8: Average Housing Benefit awards among households in the social rented sector have been rising



Source: TBI calculations using HBAI data, various years, and methodology described in the text.

Rent controls

It is the private rented sector that has seen the most change since 1979. Forty years ago, almost all private rental property was subject to rent controls through the 'fair rents' system. Tenants could apply to have their rent registered at a 'fair rent' which was supposed to correspond to the rent that would apply in the absence of a scarcity of rental accommodation in the market. This was typically significantly below the market rate. A series of reforms in the 1980s allowed more frequent rent adjustments – two years rather than three between rent registrations – bringing rents closer to market levels.

This system dramatically changed in 1989, when the new assured shorthold tenancy was introduced. Rents could now only be reduced if they were significantly higher than any other comparable tenancy. No new tenancies were governed by 'fair rents', which rapidly disappeared. Properties with a 'fair rent' represented only 1% of the housing stock by 1994–95 according to HBAI data. Landlords were able to bring fair rents closer to market levels by pointing to rent levels in the unregulated market and the availability of properties to rent in the local market as evidence of a lack of 'scarcity' (Wilson, 2014). However, a small number of registered tenancies remain to this day, and some protections were introduced in the late 1990s to limit rent increases on them.

Rent controls are of course different from social housing and housing benefits in that they represent a transfer from private landlords rather than the government or some other public-sector body. There is no direct cost to the public purse from introducing them. Nevertheless, they still represent a wedge between the market rent and the amount tenants have to pay out of their own pocket and in this sense represent a subsidy to tenants through regulation. We therefore include them in our analysis since our aim is to estimate the total size of this wedge.

Methodology

To estimate the extent to which private sector-controlled rents were below market levels, for years before 1989, we use a very similar methodology to the one followed in the case of social housing. The aim is to estimate the market rent for properties subject to rent controls by applying rental yields on the property value. When comparing this with the actual regulated rent, we get the implicit 'subsidy', namely the difference between what the market rent would have been and the actual 'fair' rent.

As with our calculations of market rents for social housing in this period, we assume that the spread of net rental yields over the 20-year index linked gilt yield seen since 1989 would have applied in the 1980s. To estimate property values, we use data from a 5% sample of building society mortgages to obtain the average house price by number of rooms and region (DoE, 1988). We assume that average maintenance and management costs are the same as in the social rented sector. Using formula (1) in Appendix A, this gives us an estimate of the market rent to compare with the actual regulated rent, in order to infer the implicit 'subsidy' from landlords to tenants.

For years after 1989, our approach is simpler. We can observe the average non-regulated rents for similar properties (same number of bedrooms) in the same region in the HBAI data, so we can compare the unregulated rents to the actual 'fair' rents.

Results

In 1979, on our estimates, 'fair rents' averaged just 40% of market rent levels; in other words the very substantial subsidy given to tenants represented around 60% of the market rent (Figure 9). In contrast to social housing, there was no clear pattern in the extent of subsidy between regions: 'fair rents' in the private sector were between 30% and 50% of market levels across all the regions of England.

Figure 9: Decomposition of market rents by region in 1979



Source: TBI calculations using HBAI, Family Expenditure Survey, Family Resources Survey and 5% sample of building society mortgages data, various years, and methodology described in the text.

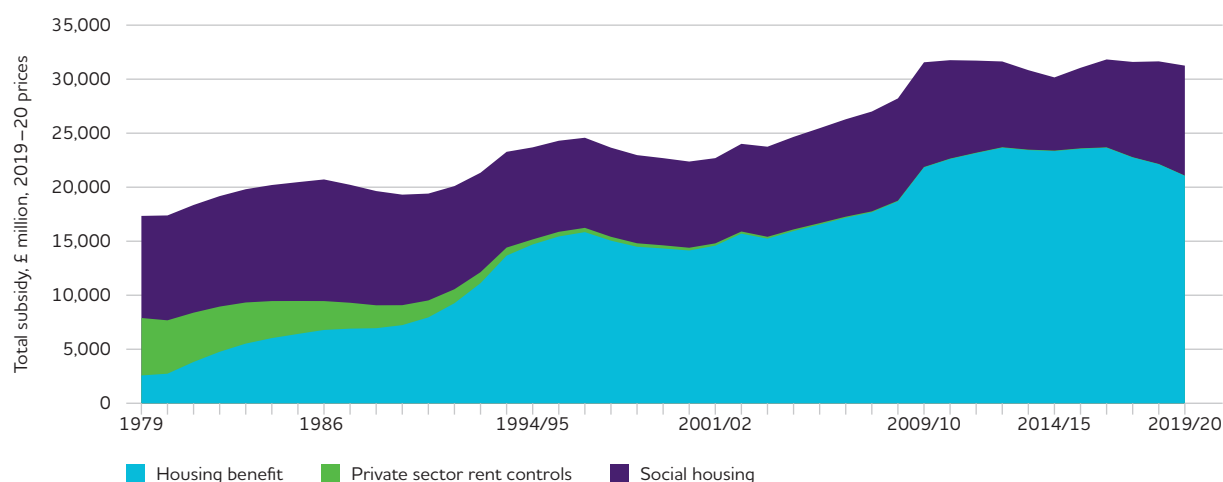
Regulation of rent levels in the private rented sector therefore represented a big subsidy for renters before 1989. When the sector was deregulated following the 1988 Housing Act, the share of properties subject to a 'fair rent' in our HBAI data fell from 7% in 1989 to little more than 1% by 1994–95, and the proportion has since declined further. This represents the removal of a subsidy that in 1979 was worth more than £5 billion in 2019–20 prices. This constituted a substantial transfer from tenants to landlords, more than doubling private sector rents as a proportion of tenants' incomes. While the previous system may have been unsustainable, deregulation undoubtedly squeezed housing affordability for many – a problem that has grown as the private rented sector has expanded.

3 The impact on affordability

Having estimated the aggregate level of subsidy from sub-market rents for social housing, cash support for housing costs and private sector rent controls, we can add these together to show how total subsidies for renters have changed over the period. In real terms, the aggregate subsidy to social renters through sub-market rents has remained roughly constant since 1979, subsidies to private rents through rent controls have disappeared, while cash support for housing costs has increased.

But adjusting the aggregate level of subsidy by general inflation offers a misleading picture. Housing subsidies are obviously intended to pay the costs of housing services. Hence it is more meaningful to quantify the generosity of support in terms of the housing services those subsidies provide.¹⁰

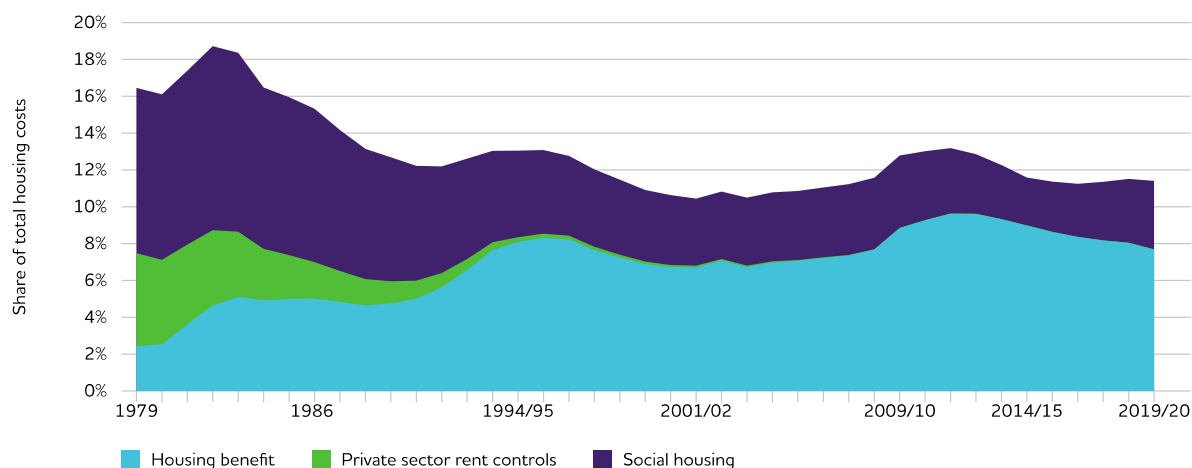
Figure 10: Total rental subsidies, 1979 to 2019–20



Source: TBI calculations using DWP benefit expenditure tables, Family Expenditure Survey and Family Resources Survey, various years, and methodology described in the text.

To make a more meaningful comparison of the generosity of housing subsidies over time, we should express them as a share of total housing costs (Figure 11). From an economic perspective, the cost of housing services is the cost of renting accommodation. For renters, this is the market rent for their home. For owner-occupiers, it is the rental income they forgo by living in the property themselves rather than renting it out. National accounts aggregates for these actual and 'imputed' rents are available for England since 2009 and for the UK since 1986. For the years from 1986 to 2009–10, we assume that total actual and imputed rent in England represents 89% of the level for the whole of the UK, and for years from 1979 to 1986 we assume that total actual and imputed rent grew in line with average household disposable incomes as measured in HBAI. (Note that although the 'Housing benefits' series includes all data points, the social housing and rent control figures only include those years shown in Figure 4 with linear interpolation in between.)¹¹

Figure 11: Housing subsidies as a share of total actual and imputed rent, 1979 to 2019–20



Source: TBI calculations using DWP benefit expenditure tables, Family Expenditure Survey and Family Resources Survey, various years, and methodology described in the text.

In these terms, the value of housing subsidies has fallen from 16.5% of total housing costs in 1979 to 11.5% in 2019–20. Although the aggregate subsidy from social housing has remained constant over time when adjusted for general inflation, this has represented a reduction in the share of total housing costs covered by subsidies from 9% to less than 4%. The disappearance of the rent-controlled private rented sector has essentially eliminated a subsidy that amounted to 5% of total housing costs, equivalent to £14 billion in 2019–20. Indeed, the value of the transfer created by rent controls would have been significantly higher today on account of the substantial growth in the private rented sector in recent years. On the other hand, total housing benefits have increased from 2.5% to 8% of total housing costs.

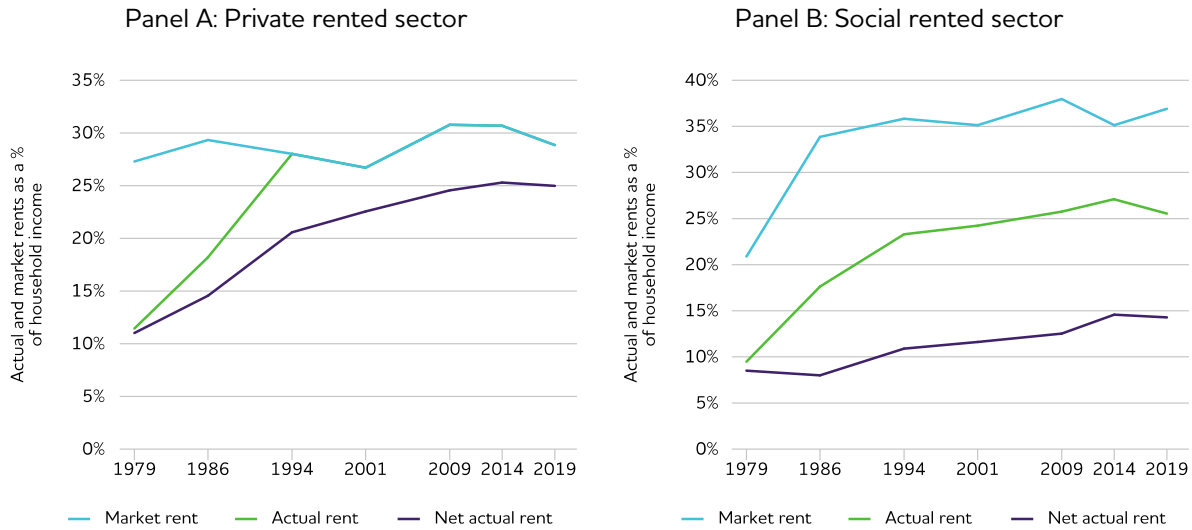
Putting this all together, if subsidies from these three sources had remained at their 1979 levels as a share of total housing costs, they would have amounted to £45 billion in 2019–20 rather than their actual level of £31 billion. It is therefore unsurprising that housing affordability has come under pressure.

A corollary of this is that total housing costs have not risen relative to household incomes since 1979. Using ONS estimates of total actual and imputed rents and HBAI income series, we see that housing costs have in fact risen more slowly than HBAI incomes since 1985 when this series starts: average housing costs per household have increased by 88% relative to general price inflation, whereas real mean before housing cost (BHC) income has increased by 97%. Consequently, average housing affordability has in fact improved over a period when policy changes have had stark distributional consequences.

Using our methodology, we can simulate what the housing affordability chart shown in Figure 1 would look like if we remove the affordability-enhancing effect of the three major subsidy policies explored above. In the private sector, whereas actual rents rose substantially as a share of tenants' incomes during the 1980s and early 1990s, underlying market rents were already higher. Market rents have remained fairly stable as a share of tenants' incomes, with the difference explained by the erosion of subsidies. The declining share of rents covered by housing benefits since 2010 can also be seen.

A similar story holds for the social rented sector from the late 1980s. (We see a jump in rent relative to incomes in the early 1980s due to changing composition of social tenants as better-off households took advantage of the right to buy.) Since the mid-1980s, housing benefits have become more important for social tenants as rents charged have increased relative to incomes. Actual rents net of housing benefits have risen less than actual rents, though still significantly more than market rents, again showing a decline in subsidies overall.

Figure 12: Rents for private renters have increased as subsidies have waned

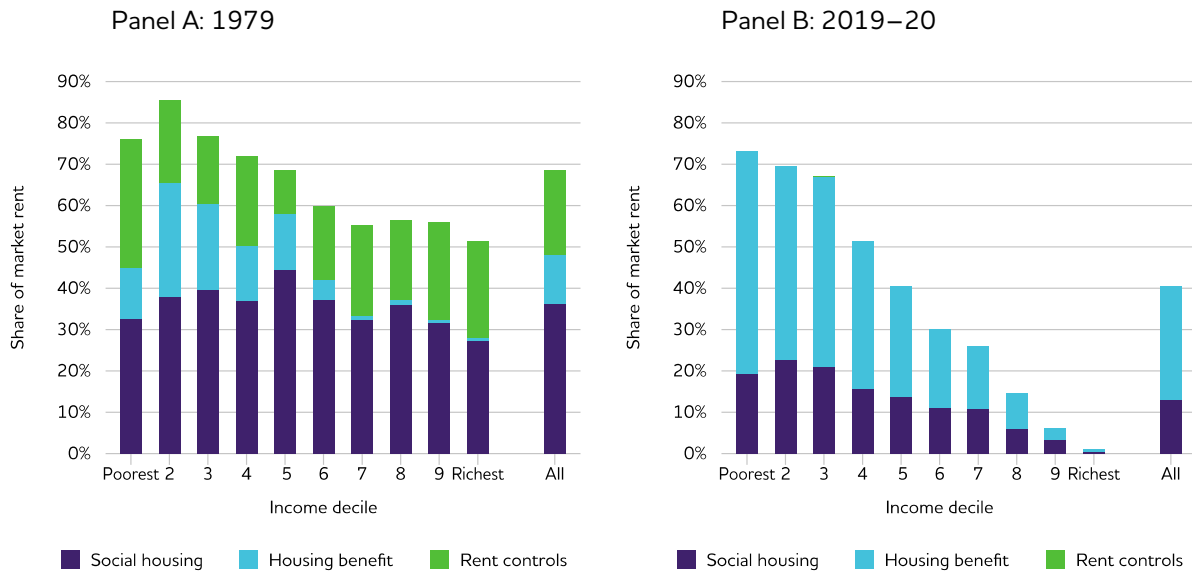


Note: Figure 12 shows actual rent, actual rent net of housing benefits and imputed market rent as a proportion of households' incomes. In all these series, 'rent' includes water rates, community water charges and council water charges, ground rent and service charges.

Source: TBI calculations using HBAI data and methodology described in the text.

Of course, the distribution of subsidies matters, not just the aggregate level. Figure 13 shows the distribution of subsidies in 1979 and 2019–20 for renters in each income decile as a share of their market rent. We can see that the biggest declines in subsidies have come at the upper end of the income scale – those with higher incomes who lived in social housing were swift to exercise their right to buy in the early 1980s – but cuts at the lower end were significant too. For example, a reduction in the subsidy received by the second income decile from 86% to 70% of the market rent represents a doubling in the housing costs they have to pay out of their own pocket. This explains why housing has become significantly less affordable for lower-income groups over the past 40 years.

Figure 13: Distribution of housing subsidies, 1979 and 2019–20



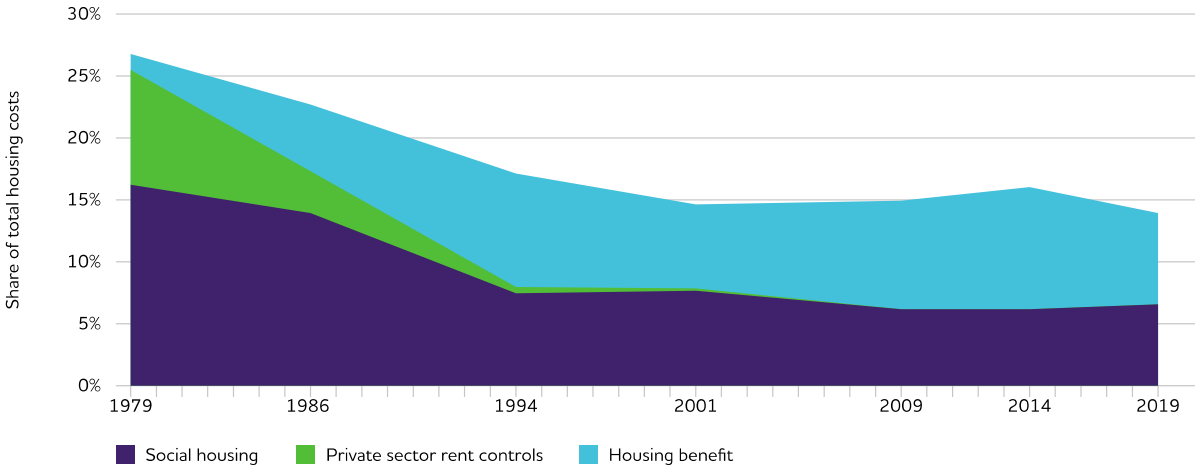
Source: TBI calculations using 1979 Family Expenditure Survey and 2019–20 Family Resources Survey and methodology described in the text.

Trends between regions have been different too. Subsidies as a share of housing costs have declined everywhere, but the size of the decline differs. The Midlands and the South West experienced the biggest

decline, from 15% in 1979 to 7% in 2019 – a decline of more than half. By contrast, in the North and in Yorkshire the decline was much smaller – from 18% in 1979 to just under 13% in 2019.

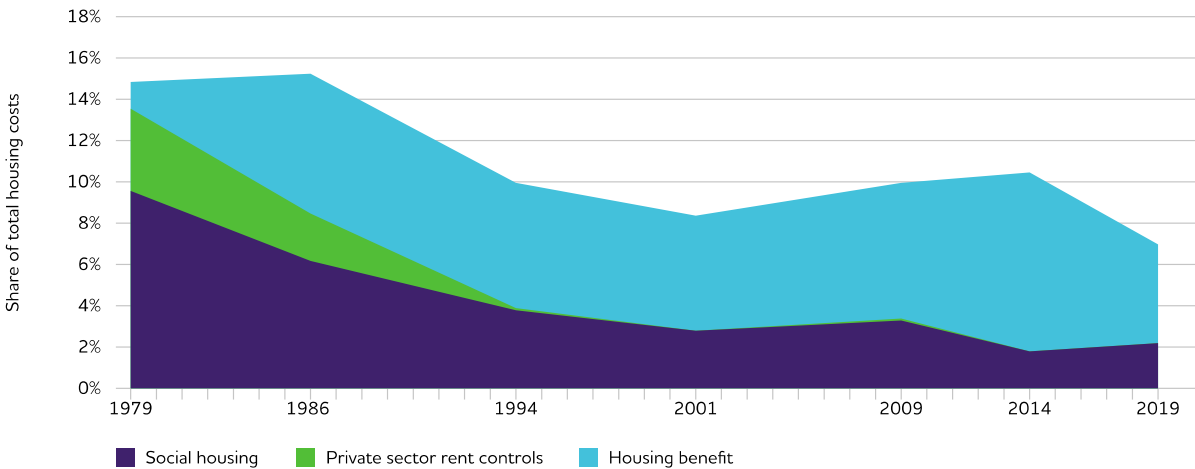
Examining the changing mix of subsidies seen in the different regions can tell us more about the factors driving these trends. Social rents remain well below market levels in London and the South and East of England (where the subsidy arising from sub-market social rents is almost 7% of aggregate housing costs). But with rents elsewhere now much closer to market levels, subsidies from this source are much smaller in the Midlands, the South West and the North of England, having fallen from almost 10% to just over 2% in the Midlands and the South West and from 10% to just over 2% in the North and Yorkshire. The size of the social housing stock has held up better in London than elsewhere, too. Given that rent controls have disappeared everywhere, housing benefits are now the principal form of housing subsidy. Renters in the North of England are the most likely to be in receipt of housing benefits: total housing benefits increased from 2% to more than 10% of total housing costs in the North of England, but to just 7% of aggregate housing costs in London, East Anglia and the South East and 5% in the Midlands and the South West.

Figure 14: Subsidies in London, East Anglia and the South East as a share of housing costs



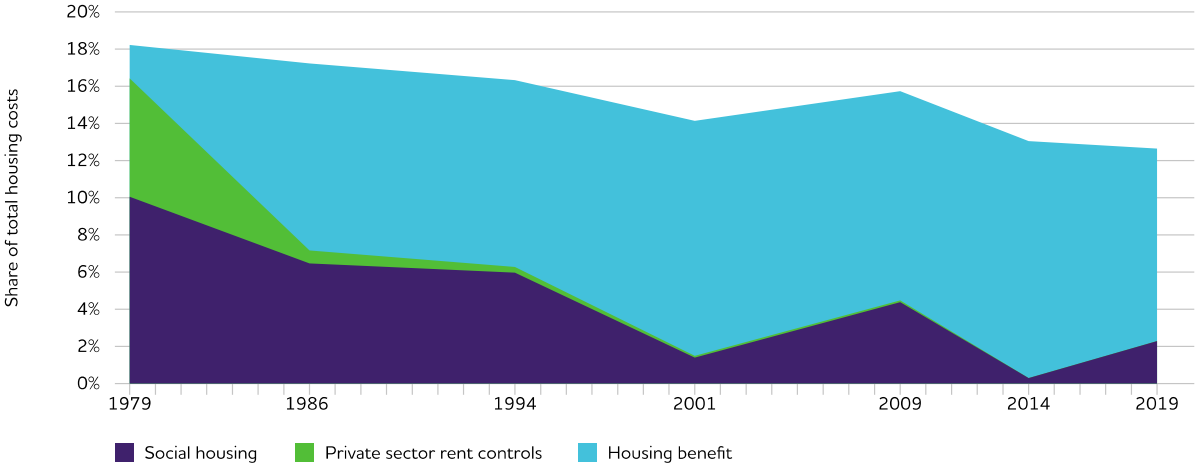
Source: TBI calculations using HBAI, Family Expenditure Survey and Family Resources Survey data, various years, and methodology described in the text.

Figure 15: Subsidies in the Midlands and the South West of England as a share of housing costs



Source: TBI calculations using HBAI, Family Expenditure Survey and Family Resources Survey data, various years, and methodology described in the text.

Figure 16: Subsidies in the North of England as a share of housing costs



Source: TBI calculations using HBAI, Family Expenditure Survey and Family Resources Survey data, various years, and methodology described in the text

In summary, our results show that the total value housing subsidies for renters has fallen significantly since 1979. This largely explains the deterioration in housing affordability for renters over the period. It also suggests that it is future changes in housing subsidies, rather than shifts in general housing supply, that will have the largest effect on the affordability of housing for renters in the years ahead.

4 What is the optimal mix of housing subsidies today?

The analysis in the previous section was purely descriptive. It showed that housing subsidies now buy significantly less housing services than they did a generation ago, which largely explains the deterioration in housing affordability for renters over the past 40 years. But if we wanted to improve housing affordability it would not be appropriate to recreate the housing policies of 1979, which would simply reproduce many of the problems that led to that regime's demise. So what would be the right combination of policy levers to use?

This section offers a framework for thinking about the optimal policy mix. In particular, in what conditions is social housing a better option than housing benefits and what does that mean for the optimum stock of social housing? To address these questions, we first set out the different characteristics of the existing housing subsidies and assess the existing policy mix.

We restrict our analysis to comparing cash transfers to households to the provision of housing at sub-market rents by government or other social landlords. We do not consider the prospect of returning to the rent controls that existed before 1989 and which some tenants still benefit from today.

Although the prospect of lower rents might be attractive to today's private renters, controls on the level of rents in the past led to an unsustainable lack of rented housing and poor quality in the sector. Owners of rent-controlled properties could make a better return by selling to an owner-occupier and investing elsewhere, so most landlords tended to sell up if their property became vacant (Crook, 1988).

Landlords also had little incentive to improve their properties as, with rents kept below their market-clearing levels (the level where supply would equal demand), there was no shortage of tenants. In 1981, 18% of privately rented houses built before 1919 still lacked basic amenities compared with 8% in the owner-occupied sector and 26% were unfit, compared with 13% in the owner-occupied sector (Thomas and Hedges, 1986). Most private rented accommodation was occupied by pensioners – in 1985, 44% of private tenants were aged over 70 – and young people had to choose between buying their own property, living with their parents or short-term low-quality rentals (Bovaird et al, 1985; Boleat, 1997; Crook, 1988) Although the private rented sector is probably now above its optimal size (Baxter-Clow et al, 2022), returning to a situation that benefited 'insiders' but left 'outsiders' without access to housing would not be desirable.

Further, as the distributional analysis of the previous section showed, rent controls do not target their subsidy on lower income households very effectively. Most of the redistributive goals that we might have for rent controls could be more effectively achieved using either cash transfers or social housing.

In comparing the benefits and downsides of housing benefits and social housing, we consider a range of criteria:

- Stability of tenure. Tenants obviously value the stability of their tenure, that is, confidence that they will be able to remain in their home for as long as they want without the risk of eviction.
- Work incentives. As is the case with any sort of means-tested support, there is a trade-off between targeting the most vulnerable and providing strong work incentives. Subsidies that are less directly related to current income will typically offer stronger incentives to work.
- Tenant choice. Housing subsidies that are tied to living in a particular property reduce the ability of tenants to live in the location and type of property they would prefer.
- Exchequer cost. Different forms of housing subsidy differ in the amount of housing services obtained for a pound of public expenditure.

Stability of tenure

Stability of tenure is an important characteristic of social housing in England. From a social perspective, we would put a very high premium on stability for some types of household. For example, it is far from ideal for families with children to have to move their children to a different school if they are forced to move by a private landlord.

Social tenancies even today are still typically for life and can even be passed on to family members if they have been living in the property for more than a year at the time of death. This contrasts sharply with the private rented sector, where assured shorthold tenancies are typically for six months and tenants can be evicted at the end of the term for no reason by issuing a Section 21 notice.

There is nothing inherent to either private or social renting that requires them to be at such extreme ends of the tenure stability spectrum. Indeed, attempts have been made to move them both away from these two extremes in recent years. As discussed above, fixed-term social tenancies have been in place since 2012. And the Government's recent White Paper on the private rental market proposed abolishing Section 21 'no-fault' evictions through a shift to periodic tenancies that can only be ended by the landlord on specified grounds (eg because they want to sell the property or live in it themselves) (DLUHC, 2022). Similar reforms have recently been introduced in Scotland, and if introduced in England they would bring the private rented sector closer into line with its counterparts in other Western European countries (Scanlon, 2011).

Nevertheless, it is unlikely that stability of tenure in the private rented sector could ever rival that in the social sector. Private landlords are unlikely ever to be able to offer lifetime tenancies in the same way that social providers do. There is a trade-off between the security of the tenant and the property rights of the landlord that if pushed too far in one direction would make the ownership of rental property unattractive. And moving the other way by ending lifetime tenancies in the social rented sector has proved difficult both in England (as discussed above) and elsewhere. Other OECD countries that have sought to review social tenants' eligibility on a periodic basis have found it difficult to increase transitions out of social housing, and England and Australia are the only two OECD countries to have attempted fixed term tenancies (OECD, 2020).

Work incentives

All types of means-tested subsidies in theory create disincentives to work: if housing benefits or social housing are allocated on the basis of income, incentives to work or to increase earnings will be weakened. However, once a tenant has been allocated a social property, there is typically no link between their rent and their income, which strengthens work incentives.¹²

Institute for Fiscal Studies (IFS) research from 2015 quantifies the impact of both Housing Benefit and sub-market rents for social housing on work incentives for social tenants in England (Adam et al, 2015). The authors found that, if social rents were set at market levels, Housing Benefit would increase the average participation tax rate (that is, the proportion of earnings that are lost to higher taxes or withdrawal of means-tested benefits when entering work) among social tenants by nearly 15 percentage points, from 42% to 57%. Withdrawal of HB is therefore an important component of the wedge that the tax-benefit system creates between the amount somebody earns and the amount by which their net income increases on entering work. However, with social as opposed to market rents, this impact is reduced by three percentage points to 54%, a not insignificant reduction. Placing someone in a social property with sub-market rents will therefore typically give them a stronger incentive to enter paid work.

As with other characteristics of cash transfers and social housing, these features are not immutable, though in practice cash transfers are always likely to be more responsive to current income than the level of discount to market rents in social properties. In principle, it would be possible to strengthen work incentives for recipients of housing benefits by making cash payments less responsive to current income, for example through benefit run-ons for a period after a household's income rises, though no OECD country has a system that works along these lines.¹³

There have been tentative steps to make social rents more responsive to income with the 'pay to stay' programme, but some other OECD countries adjust social tenants' rents when their income changes in a

more comprehensive way. A number of OECD countries increase social tenants' rents when their income exceeds the threshold that establishes eligibility for social housing in the first place. An extreme case is Canada where rents are immediately increased to market rates.¹⁴ But less extreme versions also exist, for example in The Netherlands where those with income above a threshold face a larger rent increase each year to provide a gradually strengthening incentive to move out of social housing (OECD, 2020).

It is also important to bear in mind that the strength of financial work incentives only matters if people respond to them. The economic literature tells us that some groups are more responsive to financial work incentives than others (Meghir and Phillips, 2021). For example, women with school-age children and people approaching retirement age are relatively responsive to these incentives, whereas others are less responsive. Men aged between 25 and 50 do not appear to reduce their labour supply in response to weaker incentives, and the elderly and people with disabilities that prevent them from working are unlikely to move into work no matter how strong the financial incentive. Again, this points to the importance of targeting different types of subsidy towards those who will benefit from them the most.

Tenant choice

Whereas cash benefits can be claimed for any property, when tenants are allocated social housing their choice of property is rather limited, and it is harder for them to move to a different property. Although there are opportunities for social tenants to swap properties, this requires a double coincidence of wants – for one person to move from one property to another requires someone else to want to move the other way. It is not possible for social tenants to move into any vacant social property as is possible in the private rental market.

This appears to have an impact on mobility. One study has shown that social tenants are less likely to move than other groups, even taking into account that they have different socio-economic characteristics that would also affect mobility (Cho and Whitehead, 2013). This might reduce a social tenant's ability to take up new job opportunities outside their local area and hence limit their ability to increase their earnings. It would be difficult to change this feature of social housing. Providers would not be able to reconcile tenant preferences and choice while maintaining sub-market rents. Setting rents below their market-clearing level inevitably leads to excess demand and prevents properties being allocated to those who value them most.

Whether this observed lack of mobility should be a concern for policy-makers is questionable. Cho and Whitehead argue that since most house moves are not job-related and that only higher-skilled individuals, who are less likely to be social tenants, tend to move large distances for work, it should not be. Nevertheless, this is a drawback that would become more significant if the social housing stock expanded significantly in size. Hence on the grounds of choice especially, housing benefits for private renters must remain a critical part of the optimal policy mix.

Cost

Finally, the cost to the exchequer of providing a household with the level of housing services they require is an important consideration.

Housing benefits simply involve the state making a contribution towards a tenant's rent. The rent is the cost of housing services, so the cost of one pound of housing services provided through cash transfers is always a pound.

Social housing, by contrast, involves the state building or buying an asset which it can then let out at a sub-market rate. This involves a large up-front outlay, which can be financed by borrowing, which in turn attracts interest.

The cost comparison therefore depends on the difference between net rental yields in the residential housing market and interest rates on government debt. To see why this is the case, consider a tenant living in a particular property and receiving a 100% rental subsidy. If the property was owned by a private landlord, the cost to the state would be the market rent, calculated in line with equation (1) in the appendix – that is, the market value of the property multiplied by the net rental yield plus management and maintenance costs. If the property was bought by the state (directly or indirectly via loans to housing associations), management and maintenance charges would presumably be unchanged, but instead of

paying the rental cost, the government would have to pay the gilt rate on the purchase price of the property.¹⁵

This calculation suggests that social housing is on the whole a more efficient policy tool today since net rental yields for private residential property are usually significantly higher than gilt rates. This arises because the cost of borrowing for the government is significantly lower than for private landlords. In 2019–20, gilt rates were less than half the level of net private rental yields. Typically, therefore, the government can save money by borrowing to buy a property for any household on housing benefits.¹⁶

We might qualify this claim by noting that some households currently on housing benefits will see their incomes rise in future, reducing their entitlement to means-tested cash transfers. If they were in social housing, by contrast, under current rent-setting and tenancy policies, they would continue to receive the subsidy associated with a below-market rent. But this does not alter our conclusion on the relative cost to the public purse of social housing versus housing benefits. So long as the rent being paid by those social tenants not entitled to any housing benefits is sufficient to cover management and maintenance charges and the government's interest costs, there will be no net cost to the exchequer.

Does this cost advantage imply that there are no circumstances under which we should prefer housing benefits over social housing? There are several reasons for caution.

First, greatly expanding the government's balance sheet to allow a very large expansion of social housing in a short period could present a risk to the sustainability of the public finances. If borrowing costs were to increase, as is currently happening, interest payments would rise and it is likely that the value of properties bought would fall. This risks leaving the government unable to cover the cost of servicing the debt incurred to buy social housing even by increasing rents to market levels, and unable to fully repay the debt by selling it off. In short, a large-scale shift from private renting to social housing would effectively transfer this risk from private landlords to taxpayers.

Second, significantly increasing the national debt to increase the social housing stock would also reduce fiscal space, that is the ability of the government to respond to negative shocks by borrowing more. This might have left the government unable to introduce the measures it has implemented over the last few years to support households during the Covid-19 pandemic and in response to high energy prices.

Finally, following our earlier discussion, lower rents are not the only feature that distinguishes social housing from renting in the private sector. The lack of choice for tenants in where they live and in what kind of property is both intrinsically undesirable and potentially economically damaging. The very nature of a system of housing offered at sub-market rents makes it difficult to reconcile with tenant choice.

It follows that, while social housing is typically the cheapest way of providing housing services to those in need and one that enhances work incentives, its implications for fiscal risks, choice and labour market function put limits on its appropriate scale. Housing benefits for people in the private rented sector remain a critical component of a well-designed subsidy regime for these reasons. The key, then, is to target social housing and private sector housing benefits on those groups who will benefit most from the desirable features of each form of support.

Targeting social housing and housing benefits towards the most appropriate groups

We can apply the above framework of advantages and disadvantages of the private rented sector and social rented sector to four broad groups of households. For families with children who need subsidy to be able to afford housing, stability of tenure is typically the most important consideration. Strengthening work incentives for a group who may be marginal between working and looking after children is another factor favouring social housing for this group.

These factors are less important for those without children who are not disabled. Instead, encouraging labour mobility would seem to make cash subsidies for use in the private rented sector more suitable.

For those who are disabled, the choice is less clear cut and probably depends in part on the level and type of a person’s disability. Stability of tenure is likely to be of greater importance to this group than the non-disabled given a desire to remain close to local support networks. Similarly, this group are unlikely to want to move long distances for work, though in some cases financial work incentives may be an important consideration. The social rented sector is able to provide for those who need specially-adapted accommodation, but it is unlikely to be available in the private rented sector.

Social housing is likely to be more suitable for pensioners: they would tend to prioritise stability of tenure offered, while work incentives and labour mobility are not relevant considerations. For those with care needs, the social rented sector offers sheltered housing that is not available in the private rented sector.

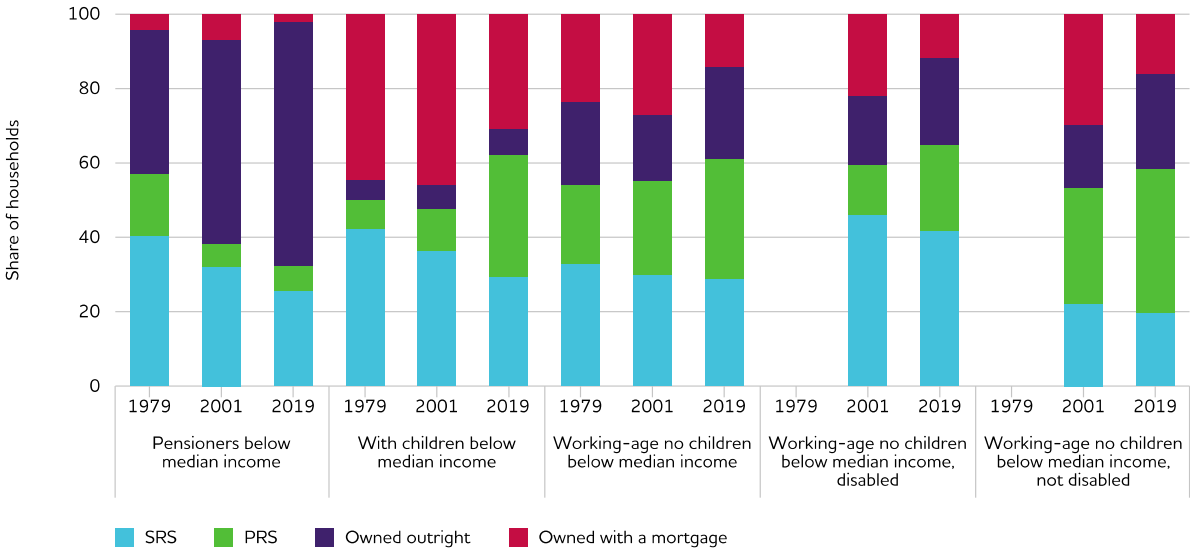
Table 1: Which is the most appropriate form of subsidy for different lower-income groups?

	Working-age with children	Working-age without children, non-disabled	Working-age without children, disabled	Pensioners
Stability of tenure	***	*	**	***
Work incentives	***	**	***	
Labour mobility	*	***	**	
Appropriate tenure?	SRS	PRS	SRS	SRS

*** very important, ** moderately important, * not very important, no stars – not important at all.

How does the status quo compare with these conclusions? Focusing on the lower-income half of households, who are the intended beneficiaries of housing subsidies (Figure 17), our data shows that 1.9 million households who would benefit from the stability of social housing were renting privately in 2019–20.

Figure 17: Housing tenure for different groups, 1979, 2001–02 and 2019–20



Source: TBI calculations using HBAI data, various years, and methodology described in the text.

The majority of these were families with children. The share of working-age households below median income with children who are renting privately has increased enormously even since the start of this century from scarcely one in ten to nearly a third. This is an undesirable trend and was not the intention of the government of the day. When measures to expand the private rented sector were introduced in

the late 1980s, the intention was to improve the supply of rental accommodation available to young people and job movers, not for the private rented sector to become a common tenure for families (Crook, 1988).

This change has come about predominantly as a result of a decline in homeownership among this group, which is now significantly below 50%, but also because of a decline in social renting. As we have argued elsewhere, mortgage market reform could help to increase homeownership levels among this middle-income families (Mulheirn et al, 2022). But social renting also used to be much more common among this group – in 1979, 42% of families with children below median income benefited from social housing compared with just 29% today – so greater availability of social housing is also surely part of the solution.

Returning to the 1979 level of social renting among this group would require around half a million additional social housing units. These need not necessarily all be at a traditional social rent. Some of these families will contain middle earners, so an intermediate or 'affordable rent' may be more appropriate in these cases. Recent JRF analysis suggests that an 'affordable rent' would be affordable for some, though by no means all, of those low-income private renters currently paying more than 30% of their income in rent (Elliott and Earwaker, 2021).

For working-age people without children, social renting is much more common among those with a disabled household member than those without, in line with the conclusions in Table 1. Shifts in tenure have been less dramatic, though there is a move towards private renting with correspondingly lower rates of homeownership and social renting. Of course, there remain some households in the 'wrong' tenure: nearly a quarter of those with a disabled household member are renting privately and around a fifth of those without a disability are in social housing. This suggests a role for greater social housing provision for people with disabilities. An additional 225,000 social housing units would enable the share of working-age disabled people living in private rented accommodation to be reduced below 10%.

Following the arguments in Table 1, one might argue there is a case for lower social housing provision for childless working-age people without disabilities, but we should be wary of drawing this conclusion. Social renters in this group are typically older – 62% are aged over 50 – whose children have left home and who are unlikely to move into homeownership as they will not be able to repay a mortgage before retirement.

Finally, few (7%) lower-income pensioners were private renters in 2019–20 and this has changed little since 2001–02. Although the share living in social housing has decreased since 1979 from 40% to 25%, this has come as a result of greater homeownership rather than more private renting (which is lower than it was in 1979 despite growth in this sector overall). This is not surprising bearing in mind that many of those who took advantage of the right to buy in the 1980s and 1990s are now retired. However, it may not stay that way as cohorts with lower home ownership rates approach retirement.

This analysis suggests there is a strong case for a significant expansion of the social housing stock on both social and economic grounds. But it also suggests that a better-functioning private rented sector remains critical.

For households better suited to the private rented sector, reform is overdue. Policy-makers should look to reverse some of the cuts to housing benefits that have been introduced since 2010. In particular, ending the LHA freeze and bringing rates back into line with the 30th percentile of local rents should be a priority on principle. And introducing the reforms to the private rented sector outlined in the recent 'fairer private rented sector' White Paper would improve tenant security, bringing England closer in line to other European countries. Together these two steps would enhance the experience of renting in the private sector and therefore take some pressure off the already substantial need for additional social housing.

5 Conclusion

Housing subsidies have long been part of the policy landscape in the UK. It is likely that it will always be necessary to help poorer households with their housing costs and ensure that they are adequately housed. This is because market housing costs are closely tied to the typical incomes that can be earned in a given location, hence people with limited earning power will always struggle to pay market rates.

Attempts to improve housing affordability for poorer households simply by increasing market housing supply are unlikely to make a significant impact on this dynamic. The relationship between market rents and additional housing supply is too weak for affordability to improve more than marginally at any plausible rate of building.

As a result, housing affordability for lower-income renters can only realistically be advanced through strengthening housing subsidies. But, as we have seen, for much of the past 40 years we have been moving in the opposite direction as at various times the subsidies offered by social housing, rent controls and housing benefits have been cut back.

Rather than going back to the failed system of 1979 or retaining the unaffordable housing system we have today, we propose a re-examination of the housing subsidy regime. A better policy mix would include, at a minimum, a significant increase in social housing provision for lower-income families with children and those with disabilities. But it is also past time to make a positive case for the critical role of housing benefits and re-link entitlements to housing costs for tenants of a reformed private rented sector.

Notes

1. Note that the trends in Figure 1 reflect both changes in housing costs and the relative incomes of those in different housing tenures. Some of the trends therefore partially reflect the fact that poorer or richer groups have moved into or away from particular forms of tenure over this period (composition effects). The introduction of Right to Buy encouraged better-off council tenants (and to a lesser extent housing association tenants) to move into homeownership. Rents were a higher share of income for those who remained. Had incomes of council tenants increased as quickly as incomes overall since 1979, council rents would represent 16% of average incomes of council tenants in 2019–20 rather than 24%. (The equivalent figures for housing association tenants are 22% and 26%). Similarly, some higher-income groups have moved into the private rented sector in recent years, dampening the increase in rents as a share of income for this group. If incomes among private tenants had only increased in line with incomes in the overall economy since 1979, average rents would represent 34% of tenants' incomes in 2019–20 rather than 28%.
2. Out-of-pocket costs include rent, water rates, community water charges and council water charges, ground rent and service charges. These payments differ from the economic cost of housing for reasons described below.
3. Source: DLUHC Housing Statistics, live table 104.
4. Source: DLUHC Housing Statistics, live table 104.
5. Note that since the FES was collected on a calendar year basis and the FRS on a financial year one, our results are for calendar years before 1994 and financial years since then.
6. See DLUHC Statistics, live table 682.
7. We use index-linked bond yields as our comparator since they would appear to be the closest asset to residential property with consistent data going as far back as 1982. As a real asset, residential property values would, unlike non-index-linked gilts, be protected against inflation like index-linked gilts, which is not the same for non-index-linked gilts.
8. Note that by using a single net rental yield across England, our results may be exaggerating the difference in subsidies across regions. It is likely that in reality net rental yields are higher in the North of England and lower in London, so we may be underestimating market rents and hence subsidy levels in the North and overestimating them in London.
9. For example, in response to a question on rising housing association rents, the then Housing Minister Sir George Young said, 'Housing Benefit will underpin market rents – we have made that absolutely clear. If people cannot afford to pay that market rent, Housing Benefit will take the strain.' See Hansard HC Deb 30 January 1991 vol. 184 col. 940.
10. Economic theory suggests that, all else equal, in particular if the housing stock is keeping pace with household formation, we would expect housing costs to rise in line with household incomes. In practice, while housing costs have risen faster than general prices, they have risen a little slower than household incomes since 1979: average housing costs per household have increased by 88% relative to general price inflation, whereas real mean before housing cost (BHC) income has increased by 97%.
11. It is also important to bear in mind that subsidies to owner-occupiers also fell during this period. Spending on MIRAS exceeded £10 billion in 2019–20 prices in the mid-1980s or close to 10% of total actual and imputed rents but is now essentially zero. See NAO, Report by the Comptroller and Auditor General: Life Insurance Premium Relief at Source (LIPRAS) and Mortgage Interest Relief at

Source (MIRAS), 1986. MIRAS remains in place for a small number of elderly borrowers who took out loans as part of a home income plan before 1999.

12. Other than through 'pay to stay' which is not widely used.
13. See OECD tax-benefit tables, <https://taxben.oecd.org/policy-tables/TaxBEN-Policy-tables-2020.xlsx>.
14. Source: OECD Affordable Housing Database Indicator PH4.3, www.oecd.org/els/family/PH4-3-Characteristics-of-social-rental-housing.pdf.
15. In practice most new construction of social housing is done by housing associations, who typically attract a small premium over gilts.
16. Note however that this is not always the case. There are points in the economic cycle when a combination of high prices and rising interest rates would lead to the rent being insufficient to cover borrowing costs. With recent rises in the Bank of England base rate, a negative market reaction to the 23 September Growth Plan pushing up gilt rates and house prices remaining high, this is true at the time of writing.

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Appendix A: Methodology for calculating market rents for social housing

Our methodology begins from the observation that in the market sector, rents must cover the landlord's costs of managing and maintaining the property and provide an adequate return on their investment. Formally,

$$\text{Market rent} = \text{property value} \times \text{rental yield} + \text{management cost} \quad (1)$$

We can thus obtain an estimate of the market rent of a particular social property if we have data on these three elements. We now describe how we obtain this information in more detail.

Values of social rented properties

As described above, the Labour Government sought to rationalise social sector rents in the early 2000s by giving each property a 'target rent' to converge to. There was a formula for target rents, the elements of which were property value, property size and local earnings levels, thus:

$$\begin{aligned} \text{target rent} = & \text{£}53.5 \\ & \times \left(0.3 \times \frac{\text{property value}}{\text{average property value}} \right. \\ & \left. + 0.7 \times \frac{\text{average county earnings}}{\text{average national earnings}} \times \text{bedroom weight} \right) \end{aligned} \quad (2)$$

In other words, the national average rent of £53.50 a week in 1999–2000 was adjusted upwards or downwards for a particular property depending on its value relative to the national average value of social rented properties, earnings levels in the local area relative to the national average and its number of bedrooms.

The values used in this formula for 'average county earnings', 'average property value', 'average county earnings' and 'bedroom weight' are all publicly available. Thus, given the target rent for a property, its number of bedrooms and location, it is possible to calculate the 1999 property value used. As an example, a two-bedroom property in X with a target rent of £Y a week must have been valued at £Z in 1999.

We use data collected by the Cambridge Centre for Housing and Planning Research on average target rents by local authority and property size from the 2000s together with the number of social properties in each local authority to calculate the average social property value in 1999 by property size and region.¹ Finally, to get the property values for previous/subsequent years, we uprate/downrate to the respective year using the ONS House Price Index (HPI).

Net rental yields

The steps outlined above get us to a valuation of the social rented housing stock over time. But to understand the value of the annual subsidy this stock implied, we need to develop an estimate of the rental yield that would have prevailed on these properties had they been in a deregulated private sector.

We use average net initial yield data from Morgan Stanley Capital International from 2001 onwards, the earliest year for which consistent data is available. Before that, we assume the average spread over the 20-year index-linked government bond yield observed since 2001 remained the same (1.4 percentage

points). We use index-linked bond yields as our comparator since they would appear to be the closest asset to residential property with consistent data going as far back as 1982. (For 1979, we use the 1982 value as non-index-linked gilt yields were little changed between 1979 and 1982). As a real asset, residential property would have the same protection against inflation as index-linked gilts, which is not the same for non-index-linked gilts.

Management and maintenance costs

Average management and maintenance costs were calculated from global accounts of housing associations (adding together aggregate expenditure on management, routine repairs and planned maintenance and dividing by the number of properties) since 2007–08. Before that average local authority management and maintenance allowances are available; we used these for years between 1990–91 and 2007–08. For previous years where no information is available, we downrated the 1990–91 value in line with RPI inflation.

Note

1 Lower-level geographical identifiers are not available in the public-use versions of the HBAI data we use so we are unable to perform this analysis at the local authority level.

Appendix B: Robustness checks using the English Housing Survey

An alternative source of data for information on house values and Housing Benefit received is the English Housing Survey (EHS). This data is not available for all years, but the 2009–10 survey wave contained a housing valuation for all properties, including social rented ones. Using those valuations, we repeated our social housing analysis to derive the market rents (using the same estimates for net rental yields and maintenance and management costs) and the corresponding subsidies in order to provide a robustness check to our results.¹

When we compare property values for social housing with those derived using the target rent formula in our main analysis, we find that the property values in the EHS are 11% lower than the values we derived in our main analysis. The biggest difference is found in the East Midlands (17%) and the lowest in the North East (9%). Interviews with social housing experts conducted as part of this research suggest that there was some deliberate overestimation of property values as part of the process of calculating target rents. Social landlords wanted to have valuations taking planned improvements into account so as to boost rents which would in turn fund these refurbishments. It is therefore not surprising that unbiased valuations provided in the EHS are a little lower.

Figure 18: EHS house prices are about 11% smaller than the ones in our main analysis



Source: TBI calculation using English Household Survey, HBAI, Family Expenditure Survey and Family Resources Survey data, various years, and methodology described in the text.

Market rents obtained using EHS data are correspondingly 8% smaller than those in our analysis. Since our estimates of market rents depend on both property values and maintenance and management costs (which are the same as in the main analysis), percentage differences in market rents are smaller than those in property values. The regional variation is, as expected, similar to the one in house prices.

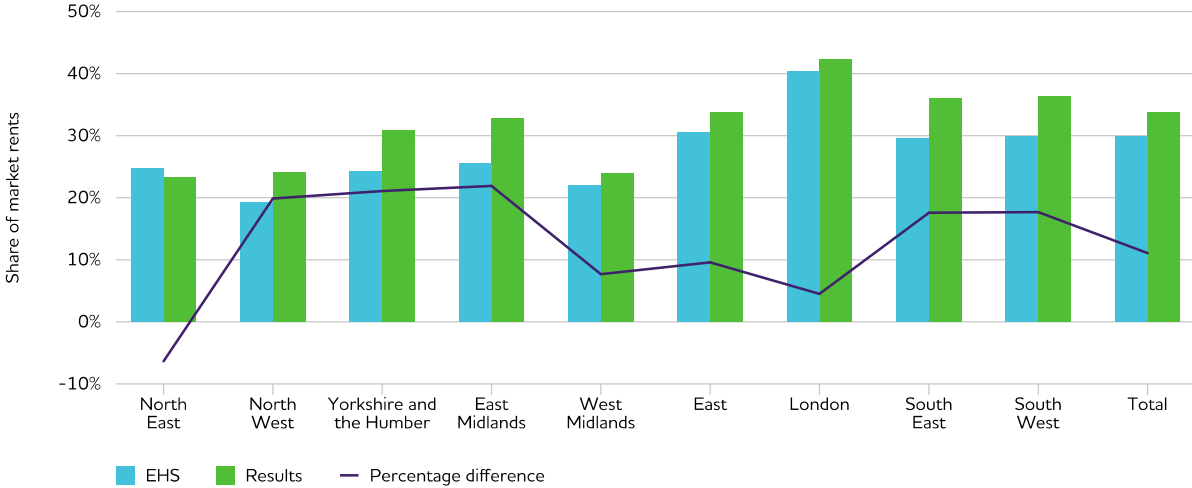
Figure 19: Market rents in the social rented sector are 8% lower in our robustness check



Source: TBI calculation using English Household Survey, HBAI, Family Expenditure Survey and Family Resources Survey data, various years, and methodology described in the text.

We can then compare these estimates of market rents with the actual rents recorded in the survey to estimate the size of the subsidy received by tenants. In our analysis, we found that the subsidy in the social rented sector represents 34% of the market rent. In this robustness check, the share is 30%, just 4% smaller. This is driven both by the difference in market rents but also by differences in actual rents (EHS actual rents are 3% smaller than those in our main analysis).

Figure 20: The SRS subsidy as a share of market rents



Source: TBI calculation using English Household Survey, HBAI, Family Expenditure Survey and Family Resources Survey data, various years, and methodology described in the text.

Housing benefits

Moving on to housing benefits, we compare the average Housing Benefit by region in the EHS dataset to that in our main analysis. We find that benefits in EHS data are 7% smaller on average than in the FRS. It should be noted that London is an outlier here: the benefits recorded in London are larger in the EHS than we obtain using UKMOD run on the FRS.

We find that housing benefits represent 16% of total housing costs, exactly the same number as the one we found in our main analysis.

Figure 21: The EHS housing benefit is 7% smaller on average



Source: TBI calculation using English Household Survey and HBAI data, various years, and methodology described in the text.

Note

1 It should be noted that properties under rent controls are not identified in the EHS and for this reason we could not conduct a robustness check for this part of our analysis,

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