in Association with the NLA

the rent check

Issue 6: Autumn 2015 – covering England & Wales

PRS Barometer

32% — 32% of landlords anticipate rental growth over the next 6 months (up 6%)

17% — of landlords purchased at least one property in the 3 months to September (up 3%)

41% — of landlords saw tenant demand increase over the last 6 months

4% — of landlords have lowered rent across their portfolio in the last 12 months (unchanged)

24% — of landlords intend to purchase at least one property in the next 12 months (down 5%)

75% — of landlords say the Government Budget decisions are mainly bad news

Regional Snapshot

Average 2 bed flat pcm

	Q3 2015	annual change
London (zones 1-2)	£1,550	+£70
London (zones 3-6)	£1,155	-£5
South East	£800	+£50
South West	£670	+£15
East England	£625	+£50
East Midlands	£575	+£35
West Midlands	£555	-£15
Yorkshire & Humber	£550	+£20
North West	£540	+£15
Wales	£530	+£15
North East	£500	+£10

Regional Snapshot

Average 3 bed house pcm

	Q3 2015	annual change
London (zones 3-6)	£1,425	-£35
South East	£1,000	+£10
South West	£870	+£5
East England	£775	+£55
West Midlands	£685	-£30
East Midlands	£660	+£5
North West	£640	+£10
Wales	£615	+£35
Yorkshire & Humber	£610	-£25
North East	£560	-£10

Rounded to the nearest £5 pcm

6 in 10 landlords will increase rents as a result of the tax changes

1 in 4 landlords will sell property as a result of the tax relief changes

2.5 years is the average tenancy length (down 0.2 since Spring)

The Rent Check interviewed 2,689 landlords across England & Wales over the six months to September 2015.

introducing

the **rent** check

The Rent Check is a collaboration of expertise from BDRC Continental – the UK's largest independent market research consultancy – and Allsop LLP – one of the leading property consultancy firms and advisors on the residential property market.

The Rent Check is a unique measure of the rents being agreed by landlords for Private Rented Sector tenancies across England and Wales. This research tracks the experience of a large sample (2,689 in the six months to September 2015) of members of the National Landlord Association (NLA), providing a statistically robust overview of the rental market - covering 20,485 properties.

This data provides insight previously overlooked by rental indices tracking 'average' prices for all properties marketed and reflects actual rents agreed; which, as the Rent Check finds, are different to the asking rent initially advertised for 24% of all lettings.

The Rent Check is supplemented by the 'Tenant Panel' in order for us to gain the perspective of the tenants. This provides us with an inclusive outlook of the private rental sector that other indices do not cover.

These surveys will continue to track movements and evolutions in the private rented market each six months, analysing movement in agreed prices, regional variations and providing unique landlord and renter insight.

The Rent Check is a survey forming part of the BDRC owned 'Landlords Panel' which will provide supplementary analysis on future rental trends, tenant profile and landlord confidence in future survey releases.

the integrity of

the **rent** check

The data included in the Rent Check has been analysed and scrutinised by BDRC Continental's research analysts and draws on their experience in the consumer research arena. BDRC Continental has a seven year history of conducting research with residential landlords and have carried out focused research on the buy-to-let market and private rental sector on behalf of a wide range of clients and interested parties.

the methodology of

the **rent** check

BDRC Continental's Landlords Panel is the only regular, commercially available study of the UK's private rental and buy-to-let sectors. Established in 2006 and run in partnership with the National Landlords Association, the subscription based study provides important insight into the market dynamics of this multibillion pound industry. Each quarter more than 1,000 online landlords across the UK are interviewed about the key aspects of their letting activity, as well as general economic indicators including optimism and market outlook. Results are independently analysed and published by BDRC Continental.

The Tenants Panel will be carried out quarterly, with around 1,000 private tenants participating in the survey each wave. For sake of clarity, the tenants are randomly selected from commercial lists within which participants self-select by declaring that they are private tenants. They are not connected to NLA members, although we do not rule out that some may coincidentally rent from them.

Changing Times for Landlords

Undoubtedly, 2015 has been a pivotal year for landlords. The demand for privately rented accommodation seems unrelenting, and, as the Rent Check reports, rents are certainly increasing, with an average increase across England and Wales of 2.0% over the last six months. However, Government intervention and added regulation are squeezing landlords' returns and matters of compliance are increasing. The press continues to focus on reports of poor landlords and unsatisfactory conditions for tenants.

Strong rental growth to continue

As our rental figures for quarters 2 and 3 of 2015 show, rents have increased across the country over the last six months. The east of England has seen the greatest growth in tenant demand according to landlords and has seen rents on two bed flats rise 5.0% over the last six months (8.7% over twelve months). Increases in the east have outstripped those in the South East over twelve months (of 6.7%). Rents in Outer London (zones 3-6) are rising for two bed flats but at a steadier pace (4.0% over the last six months), with rents on larger three bed properties relatively static (a slight decline of 0.7%).

Rents outside the East and South East are also experiencing growth, with average rent estimated to have increased by a significant but lower level of 2.3% over twelve months. Interestingly, in several of these regions larger 'family-sized' three bed housing has seen greater growth than typical two bed flats offered for rent, indicating greater competition as families have looked to move over the summer months. Indeed, families are now the most frequently mentioned tenant type across the UK's private rental sector.

Putting this in context, the Retail Prices Index (which includes housing costs) has hovered around 1.0% or below, during 2015 and wages according to the latest ONS statistics increased 2.0% only over the twelve months to September. As demand continues to push rents ahead of other costs and with little supply entering the market, we expect the pressure on rents to continue over the next two years. Forecasts for future housing demand suggest continued expansion of the private rented sector will be required. Indeed, some market commentators suggest that the proportion of households renting privately could overtake those owning with a mortgage by 2025.

__41%__ of landlords saw tenant demand increase in the last three months alone

__43%__ of landlords surveyed have raised rents in their portfolios over the last 12 months

__32%__ expect to raise rents over the coming six months

Landlord optimism is on the slide…

Over the last three months, landlord satisfaction has been on a rapid downward spiral and the largest, 'professional' landlords appear to be most disgruntled of all. Whilst all the indicators suggest continued strong rental growth in the sector, recent changes to legislation and compliance requirements are making landlords' operations and obligations more difficult to manage and, squeezing profitability. Landlords tell us the changes will deter them from investing further in the future and in many cases they will vote with their feet by leaving the rental sector or significantly reducing their portfolios.

__1 in 3 landlords__ with over 20 properties are planning to divest within the next 12 months

With house price growth still relatively steady across much of the country and buy-to-let lending criteria tighter and more comprehensively monitored, it is the income yield from their investments which is of greatest importance to landlords in 2015. Savings rates are at a low level and rate rises are not expected until 2017. Portfolio income generation is the primary motivator for most landlords to stay in the market currently, particularly so in areas without strong capital growth prospects. Yet, although rents are expected to rise further, it is net income that is under the most pressure following the 2015 Budget changes.

__49%__ of landlords stated rental yield performance as being most important to their financial returns over the next 12 months

With the Chancellor's Budget focussed mainly on increasing housing destined for home ownership, the changes introduced for the private rented sector were, along with many other sectors on the Government's agenda, aimed at increasing Government revenue rather than encouraging investment into the sector. The phasing out of tax breaks on mortgage interest payments for landlords in the higher-rate income tax

Changing Times for Landlords

(Continued)

band was the most unpopular policy implemented. Although steady in its introduction, this will see landlords in this bracket receive a reduced income return after tax.

In addition, and possibly equally detrimental, was the announcement of a new 3% Stamp Duty surcharge for private landlords being introduced from April 2016. The direct consequences of this change will become apparent next year, but there has already been a great deal of speculation surrounding both the short and long-term impacts on the private rented sector. Potentially, there could be a rush of people snapping up properties over the coming months before the changes come into force, which in turn could lead to increases in house prices in the short term. It is also likely the extra charges incurred by landlords will be passed on to tenants of buy-to-let properties through higher rent expectations.

Looking further into the future, this change is likely to discourage new landlords coming into the market and investment in buy-to-let homes, potentially reducing the supply of rental properties leading to further increases in rents charged to tenants (as tenant demand remains very strong).

Furthermore, changes to the way furnished properties are treated under the 'wear and tear' allowance, mean landlords can no longer claim tax exemption to 10% of net rent for renew or repair of fixtures of fittings without specific justification of their expenditure. In future, landlords of furnished dwellings will need to account for the costs incurred and claim exemption on these items specifically.

Taken together, these recent changes could have a profound effect on the private rental sector, and look set to encourage a shift away from amateur landlords.

Voting with their feet

The impact of the Budget changes to landlord operations, together with a stream of increasing obligations aimed at raising sector standards (but with a range of very negative consequences) are making letting more complicated, more costly and ultimately more risky for investors. Those with the largest portfolios and particularly those who are self-employed (23%, with a further 19% self-employed in another sector as well) are most exposed to these changes. Perhaps unsurprisingly, many suggest this group will look to sell property as a direct result of the changes outlined. In fact, the number of landlords looking to sell over the next twelve months has more than doubled to 15% over the six months to September. At the very least, landlords expect to increase rents further in order to recover some of the income lost in increased tax.

69% of those in the higher rate tax band stated they would look to increase rents as a direct result of the squeeze on their returns

So what changes are landlords facing?

Change to 'wear and tear allowance':

Under current arrangements, landlords of furnished properties are able to claim relief up to 10% of net rent for the replacement of items provided as part of a furnished letting as required. This arrangement was regularly maximised by qualifying landlords. The proposed changes (due to apply from April 2016) will see landlords have to account for their actual expenditure for certain 'furnishing' items, requiring landlords to keep and supply records of such costs in order to benefit from the relief. The NLA suggests 47% of landlords will be affected.

Compliance and greater safety regulations:

Smoke and carbon monoxide testing came into force on 1 October 2015 requiring landlords to ensure at least one smoke alarm is installed and operational on every floor of their rental property and, where solid fuel heating sources are used, a carbon monoxide detector is installed in any room heated on this basis. Going forward, landlords will need to ensure these alarms are in working order at the start of each tenancy. Penalties for non-compliance are up to £5,000.

Legionella risk assessment is the responsibility of a landlord (being the person in control of a premises). Landlords are required to take suitable precautions to prevent and control the risk of their tenants becoming exposed to legionella, which in many cases may require them to employ an independent assessor to carry out the assessment on their behalf.

"Landlords feel that they've been hit with a triple-whammy by what they see as an increasingly anti-landlord Government"

Mark Long, BDRC Continental

Mandatory landlord registration is being adopted by an increasing number of Local Authorities in England and is now mandatory in Scotland, Wales and Northern Ireland. Such registration requires landlords to provide information about their lettings business and in the majority of cases to pay a fee for registering.

Changing Times for Landlords

(Continued)

Immigration status checks of prospective tenants were introduced in the West Midlands in December 2014 and are expected to be extended across the UK in the near future. This places the responsibility on landlords to check that any potential tenants or adults expected to live in their property are in the country lawfully prior to granting a tenancy. Penalties for non-compliance can be up to £3,000 per occupying adult.

Section 21 notices which are used to obtain possession cannot now be served in the first four months of a new tenancy. In addition in order to serve such a notice a landlord must have complied with the new smoke and carbon dioxide testing requirement and have previously supplied the tenant with an Energy Performance Certificate, Gas Safety Certificate and the most recent edition of the Government's 'How to Rent' booklet.

Reducing tax relief on mortgage interest payments:

As announced in the Summer Budget, changes to tax relief on mortgage interest payments are to be phased in from April 2017, this will see 'higher-rate' tax payers receive the same rate of relief as 'basic-rate' tax payers by 2020. Those in this band and with high mortgage debt on their rental properties will pay substantially more tax as a result, with the worst affected paying twice as much under the arrangements.

Pressure on supply

If landlord intentions do come to fruition and with 'would-be' investors likely to be deterred by the changes made to the sector, the country is facing a possible contraction in the supply coming to the rented market. In the short term at least, upward pressure on rents may also come from a reducing level of stock as well as the anticipated increase in demand. For those remaining in the sector, those in the lower tax band and those with mature portfolios able to weather the changes, strong rental growth will be welcome news. However, ultimately for the country, such a shortage of rented property will inevitably exacerbate the housing crisis unless further investment can be attracted.

Build to Rent: part of the solution?

The key source of new supply hoped to release some of the pressure, will be the much anticipated 'Build to Rent' purpose built rental product, which we are starting to see gather some traction across UK cities. Pioneer schemes have this year started to see units released into the market and many financial institutions have now committed funds to the growth of the sector. These schemes will look to deliver rental product at scale, in purpose built blocks of in excess of 100 units, bolstering rental supply levels in city centres, and, we anticipate in future, more suburban or peripheral locations. Whilst the level of this investment is high, estimated by some to be in the region of £30bn (according to the BPF) if all the expected capital were committed, it is likely to take several years before many of these large-scale schemes are released.

Build to Rent was supported by a number of Government initiatives during the last parliament, which included the introduction of a Government-led PRS task force and Build to Rent lending fund. This work is now beginning to pay off in schemes being delivered and planned further developments in city centres across the country are expected to increase choice, affordability and quality for tenants once complete.

Turbulent times but a positive outlook

The level of investment being discussed for the new 'Build to Rent' sector is only one piece of the puzzle. For rents to stabilise, growth in the number and appetite of small-scale investors will need to be encouraged, particularly outside of urban areas. Rental growth prospects have, however, rarely been so positive and with landlords still of the opinion that residential property offers them better returns than equities, bonds and bank deposits. It may be that once the changes imposed have been worked through that further investment can be attracted at this level.

Best prospect for financial growth in the next years?	
Rental yields	49%
Capital Gains	25%
Stocks & Shares	8%
Investment products (e.g. bonds)	2%
Savings accounts from banks / building societies	1%
Don't know	14%

In terms of rents, we see no reason why the growth seen over the last six and twelve months will not continue into 2016. The limiting factor to such growth is likely to be the continual squeeze on household income while wage growth continues to be slow, particularly in the South East where housing costs account for a high proportion of household expenditure. In lower value areas, housing benefit levels will continue to provide a glass ceiling on the rents achievable (the Rent Check has found no growth in rents to these tenants over the past two years), and with Government policy aimed at restricting welfare costs, this is likely to persist going forward.

Outside of this though, for much of the country, the pattern of increasing rents will, we expect, continue until a greater stream of supply to the rental market can be established.

the rent check

To subscribe to the rent check please email: **rentcheck@allsop.co.uk**

To join the Landlords Panel please contact the National Landlords Association on **020 7840 8900** or at **info@landlords.org.uk**

the rent check team:

Paul Winstanley
Partner
07789 405 627
paul.winstanley@allsop.co.uk

Beth Mitchell
Associate
0113 243 7951
beth.mitchell@allsop.co.uk

Mark Long
Director
07966 454 958
Mark.Long@bdrc-continental.com

Bethan Cooke
Associate Director
020 7400 1019
Bethan.Cooke@bdrc-continental.com

Please contact Mark or Bethan at BDRC if you would like details of their proprietary or bespoke research services within the PRS.

allsop

@allsopllp
www.allsop.co.uk

bdrc continental

@BDRCContinental
www.bdrc-continental.com