



Vital role of the Private Rented Sector

November 2024

Executive summary

The new government has made clear its priorities to build more homes and to improve the rights of tenants who rent in the private sector. The new administration has also announced its intention to introduce legislation which would require all private rented sector (PRS) properties to achieve an energy performance certificate (EPC) rating of at least a C by 2030.

This report examines these proposed regulatory changes in detail. Whilst many of the measures are no doubt intended to increase renters' security of tenure and treatment by their landlords, there is a risk that the balance of rights and responsibilities may be shifted too far and cause unintended consequences.

The major problem which the government faces is a chronic shortage of supply/surplus of demand in both the owner-occupied and private rented sectors. So far as the PRS is concerned, we would urge the government to remember that where measures are proposed which could cause private landlords to exit the sector, this will reduce the (already insufficient) supply of rental properties still further – causing tenants to suffer from the lack of supply and higher rents.

To this end we put forward the following recommendations:

- **Give greater recognition to the importance of the PRS, which provides homes for just under 20% of UK households.**
- **Acknowledge that small landlords form the backbone of the sector.**
- **Recognise that, as with any industry, increased regulatory costs will push up prices.**
- **Accept that increased risk for landlords will require higher returns.**
- **Acknowledge the ability of the market to drive up standards in the PRS.**
- **Apply policy more fairly across tenures**

1. Policymakers reshape the housing landscape

1.1 The changing nature of government intervention in housing

For more than a century, the UK housing market has been subject to far-reaching government intervention. One common theme across this period has been the desire by policymakers to keep the cost of housing down for ordinary working people. This was achieved through rent controls during the world wars and then by a large social housing construction programme in the decades following World War II. In more recent decades, with rent controls out of favour and the social rented sector diminished due to council house sales and low rates of investment, the government has increasingly relied on the benefit system to ensure that housing costs remain affordable for lower income households.

As the social rented sector has shrunk, government has relied increasingly on private landlords to house those in receipt of benefits. This is a shift from so-called bricks and mortar subsidies, where the government finances the building of new homes for rent at subsidized (non-market) rents, to one where the government accepts that it will meet market costs for those who need financial assistance to keep a roof over their heads.

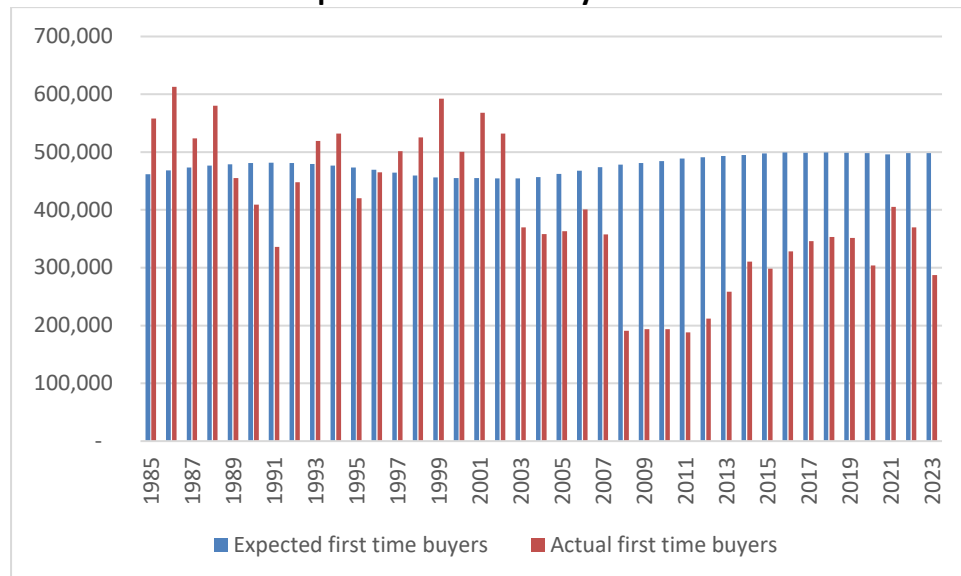
With the UK population rising substantially over the past three decades and housebuilding failing to keep pace, the shortage of housing has become cumulatively worse. This in turn has driven market house prices and rents up, increasing the government's housing benefit bill, which keeps rising. In 2022/23 it reached £23.4 billion, with 2.6 million households receiving this benefit in England alone.

1.2 Today's housing policy environment and its drivers

Where does this leave housing policy today? There is something of a consensus that investment in social housing should rise, to reflect the reality that many households cannot afford either a full market rent or the cost of owning their own home, especially as the housing shortage has left house prices so high. There is also a political consensus that homeownership deserves encouragement, given the advantages it provides by promoting long-term financial stability, wealth accumulation and the broader non-financial benefits that homeowners report. These include access to schools, long-term ability to register with GP surgeries, resulting in better health care, and sense of community leading to overall well-being – benefits which are not readily available to tenants who may have to move frequently, and/or away from a familiar area.

In June 2024, IMLA published *The mortgage affordability paradox updated* – which revisited an earlier report first published in October 2019. This estimated that 3.1 million households who would have been expected to purchase their own home based on previous trends had failed to do so since the financial crisis (see Chart 1).

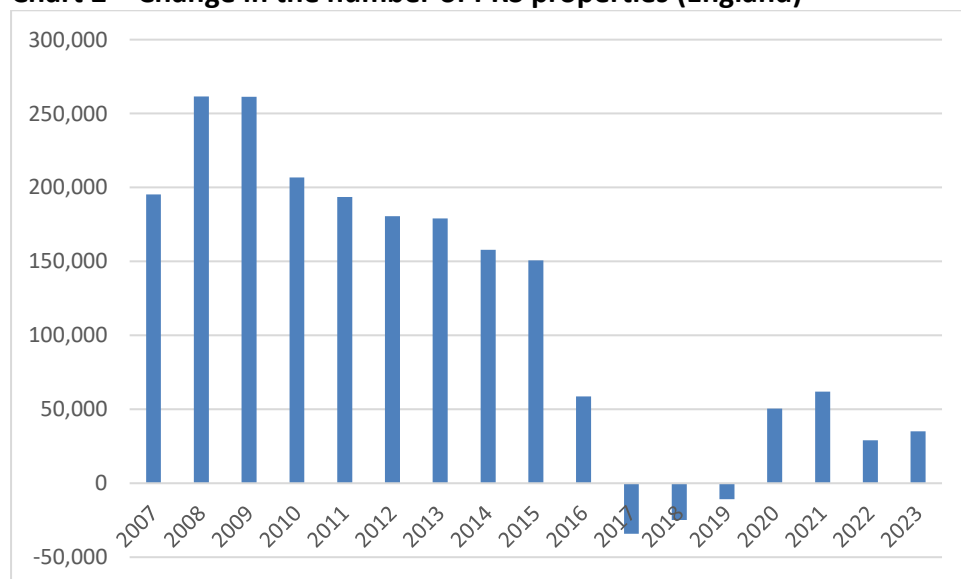
Chart 1 – Actual and expected first time buyers



Source: ONS, UK Finance, IMLA estimates

The most prominent feature of today’s PRS is chronic excess demand/insufficient supply. When an industry faces chronic excess demand, policymakers would normally be expected to concentrate on ways to stimulate supply, such as encouraging private investment through tax breaks or reduced regulation. In the PRS, however, we have seen the opposite, with greater regulation since the Housing Act 2004 and, since 2015, adverse tax changes specifically aimed at landlords, with mortgage tax deductions restricted to the basic rate of income tax and capital gains tax kept at a higher level for rented residential property until October 2024 when the rate on other assets was raised. The October 2024 budget also increased the stamp duty surcharge for property investors and second home owners by a further 2% - from 3% to 5%.

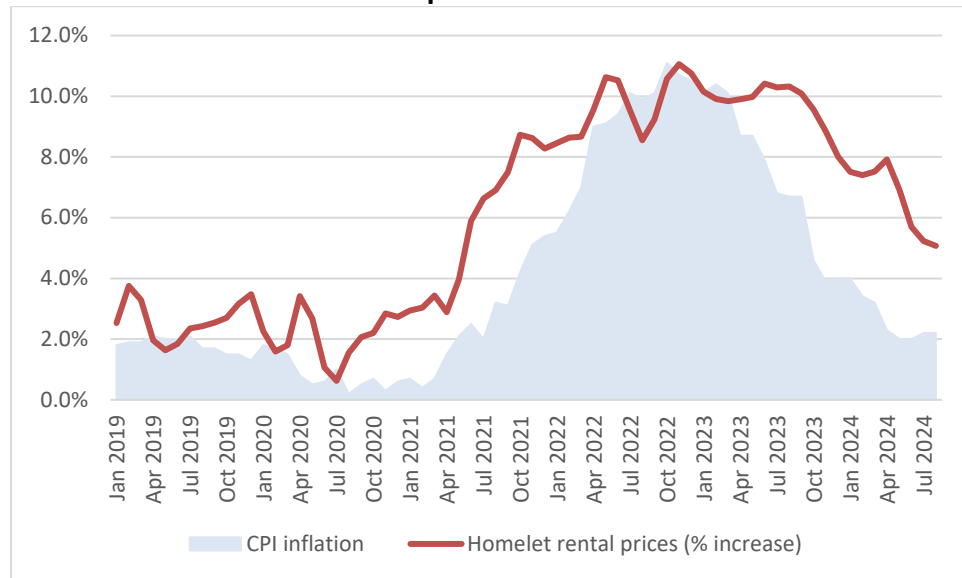
Chart 2 – Change in the number of PRS properties (England)



Source: Ministry of Housing, Communities & Local Government

The impact of the adverse tax changes introduced by the Conservative government of 2015-19 are not hard to see. Chart 2 shows the dramatic reduction in the growth of the PRS following the tax changes introduced in 2015.

Chart 3 – Rental and consumer price annual inflation rates



Source: ONS, Homelet

Economists would expect a decline in supply relative to demand to lead to higher prices. And as Chart 3 illustrates, this is exactly what has happened in the PRS, with the price of new rental contracts rising 42% between January 2019 and August 2024, as compared with a 26% increase in consumer prices.

2. Proposed regulatory changes

2.1 Renters' Rights Bill

The Renters' Rights Bill currently before Parliament is a flagship policy of the new Labour government. It replicates a number of proposals which had been included in the previous Conservative government's Renters' Reform Bill, which failed to reach the statute books before the General Election was announced on 22nd May.

Taking its measures together, the new Bill will significantly impact landlords' ability to control their businesses as they see fit. It will also impose a higher regulatory burden, while at the same time raising risk and costs. The Bill is clearly intended to give greater protection to tenants – but there are risks that the delicate balance between tenants' and landlords' rights may be upset – to the detriment of the former. Recent figures from Rightmove show that 18% of homes currently for sale were previously available on the rental market, the highest proportion on record, while property platform Upstix reported a 33% increase in enquiries from property investors in the week after the Renters' Rights Bill was published. Loss of properties from the rental stock can only exacerbate the over-riding problem facing the PRS: that of excess demand, with inevitable increases in rental levels.

Changes proposed in the Bill include:

Abolition of Section 21 evictions

This key policy change will abolish fixed-term contracts or so-called “no-fault” evictions. Tenancy agreements will become periodic, with no end date at which the landlord can regain possession: instead, they will only be able to remove tenants for one of a number of prescribed reasons.

This provision has been widely welcomed by organisations representing tenants – but it is a significant departure from what has, since 1988, been the dominant form of tenancy agreement in England and Wales. The Assured Shorthold Tenancy (AST), created by the 1988 Housing Act, provides tenancies for a defined period of time, at the end of which the tenant has no right to remain in the property unless the contract term is extended by a new contract. This gives greater reassurance to landlords that they will be able to recover their properties if they wish to do so. For tenants, the fixed-term nature of the AST means that they cannot be certain that their landlord will be willing to enter into a new contract, but landlords are incentivised to renew contracts for tenants who are abiding by the terms of their contract as this limits voids.

The prescribed grounds for eviction under the new Bill will include cases where the landlord wishes to sell or move into the property or where there are rent arrears or evidence of anti-social behaviour. However, enforcement of these grounds is likely to require a potentially lengthy court process.

Critics of Section 21 (“no-fault” evictions) have argued that it allows landlords to evict based on a subjective decision about a tenant's behaviour and to retaliate against

tenants who complain about conditions in the property. This may be true in some cases, but requiring landlords to go to court to evict tenants who genuinely cause problems for the landlord and/or other tenants in the same property is likely to make life more difficult for good tenants. While currently the landlord can decline to renew a disruptive individual's contract. This will no longer be the case under the new law.

Another scenario which was greatly helped by the introduction of ASTs relates to homeowners who had to leave their home for a year or two because, for example, their work had temporarily posted them elsewhere in the UK or abroad. Before the introduction of fixed-term tenancies in the 1988 Housing Act, many were reluctant to rent out these homes for fear that it might require a lengthy legal process to get them back. This problem is likely to reappear as a result of the abolition of Section 21 – and many properties may simply be left empty, when they could be providing valuable homes for good tenants.

Ensuring possession grounds are fair to both parties

The threshold for eviction will be increased from 2 to 3 months' arrears and the corresponding notice period from 2 weeks to 4. Where the landlord wants to move into or sell their property, the notice period will be extended to four months. While these may not seem like major changes, they are part of a cumulative list of increased costs and reduced flexibility for landlords. This is likely to lead landlords to increase rents. In the case of tenants who fall into arrears, tenants who do pay their rent on time will ultimately pay for higher costs associated with those who do not pay.

Provision of stronger protections against backdoor eviction

Tenants will be allowed to appeal rent increases to an independent tribunal to prevent landlords from using excessive rent increases as a backdoor way to force them out. This is a logical step given the abolition of section 21, however, landlords will no doubt watch closely how these rent tribunals operate. If experience of tribunal decisions leads landlords to conclude that below-market rents are being imposed on them, they may decide to sell.

Introduction of a new PRS Ombudsman

The government says that a new PRS Ombudsman "will provide quick, fair, impartial and binding resolution for tenants' complaints about their landlord". This will bring tenant-landlord complaint resolution on par with established redress practices for tenants in social housing and consumers of property agent services." Prompt dispute resolution – and the emphasis should be on "prompt" - should be a positive for both tenants and landlords as long as it is deemed to adjudicate fairly and provided the costs do not fall disproportionately on landlords.

Creation of a landlord database

A mandatory landlord database has not been universally welcomed amongst landlords but it does provide a tool for better enforcement and weeding out rogue landlords.

Giving tenants strengthened rights to request a pet in the property

Landlords will be prevented from “unreasonably refusing” to allow tenants to keep a pet but will be able to require that pet insurance covers any damage to their property. It is unclear what “unreasonably refusing” will mean in practice and most pet insurance will not cover property damage so there is some uncertainty about how this will work in practice. Moreover, it is unclear how landlords will be compensated for the increased wear and tear that pets can create through the gradual degradation of carpets for example, which is not an event that can be claimed on an insurance policy.

Application of the Decent Homes Standard to the PRS

Most of the specific requirements of the Decent Homes Standard already apply to PRS properties so for most landlords this should make little difference. The responsibility for enforcing the law will lie with local authorities – many of which already currently face considerable financial challenges - and it is not clear that they will be given the necessary resources to fulfil their increased obligations.

Application of ‘Awaab’s Law’ to the PRS

The government describes this as “setting clear legal expectations about the timeframes within which landlords in the private rented sector must take action to make homes safe where they contain serious hazards”. The law currently applies only to social housing and was introduced following the tragic death of Awaab Ishak from a severe respiratory condition in December 2020 caused by mould after repeated failures by the landlord, Rochdale Boroughwide Housing.

All tenants deserve to live in safe housing conditions regardless of whether they are in the social or private sector. Enforcement will be key, however, and there are concerns amongst landlord organizations that not enough is being done to police rogue landlords.

Making it illegal for landlords and agents to discriminate against prospective tenants in receipt of benefits or with children

Not all property is equally appropriate for families with children and it is likely to be a concern to some landlords that they may be asked to house families with children in properties they do not feel are appropriate. Landlords may also have differing attitudes towards renting to tenants who are on benefits. This may in part reflect individual landlord experience, and the role played by the relevant local authority in resolving any problems caused by tenants for whom they are responsible. Some landlords will feel better equipped/more confident than others to accept prospective tenants who are in receipt of benefits.

Landlords cannot be expected to rent out property at a loss to themselves – and must therefore be able to charge a reasonable rent. The Local Housing Allowance paid to significant numbers of tenants is often insufficient to cover the cost of renting, which means that tenants must be able to make up the shortfall from other sources. Where they are unable to do so – arrears will start to build up. Landlords who have experience of this may understandably be reluctant to repeat the experience. Smaller landlords may well depend on rental income for their own day-to-day living expenses

in a way that a larger corporate landlord does not. It does not therefore seem reasonable for government to restrict landlords' right to control their business and make what they see as commercially sensible decisions. As with the other issues discussed above, increasing landlords' risk and potentially reducing their returns should be expected both to increase rents and reduce supply. Once again, this can be expected to negatively impact tenants, giving them less choice and causing rents to be pushed higher.

2.2 Minimum EPC rating of C

In October 2008, the government introduced a minimum EPC rating of E for all rented properties in England and Wales. A consultation paper published by BEIS in December 2020 then proposed that this minimum should rise to a C rating for new tenancies by 2025 and to all tenancies by 2028. This target was widely viewed as unachievable given the short timeframe and the Prime Minister (Rishi Sunak) announced in September 2023 that it would be "scrapped".

In August of this year, the new government announced it was reintroducing the minimum C rating with a deadline of 2030. No details are yet available. The six-year timeframe for meeting the requirement in full is actually tighter than the previous one and must be challenging given that, according to Savills, 2.9 million properties in the PRS are rated less than C. No similar requirement has been set for the social rented or owner-occupied sectors. Private landlords with properties below a C rating may well question the fairness of this. They will also be anxious to know whether there will be a cap on what they can reasonably be expected to spend on making the necessary improvements to their properties. The previous (2020) BEIS consultation proposed that landlords' expenditure on energy improvements would be capped at £10,000. It is not yet clear whether a similar provision would apply under the new government's proposals.

3. IMLA's recommendations for a more effective policy framework for the PRS

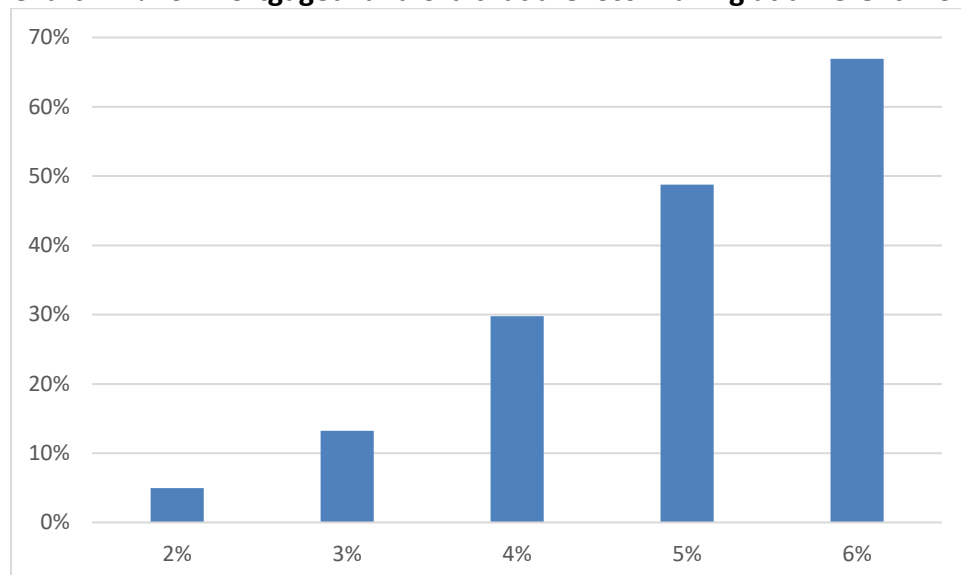
Section 1 above outlines our view of how government policy has shaped the PRS in the past and how regulatory and tax changes since 2004 have increased the cost burden on the sector, driving down supply and increasing rents. Section 2 examines some of the new government's proposed changes to the sector, suggesting that these follow the pattern of the interventions of the past two decades and are likely to increase costs and risks for landlords. If our analysis is correct, the inevitable result will be even lower supply and higher rents for tenants.

We believe that in order to achieve better outcomes for tenants, the government should:

- **Give greater recognition to the importance of the PRS, which provides homes for just under 20% of UK households.** The current imbalance between the private and public rented sectors means that the former is needed to fill the yawning gaps left by the latter. But private landlords are not responsible for providing public services and are often very small operators. While it is fair to expect them to treat their tenants decently, a one-size-fits all approach to all private landlords will cause anomalies and unfairness.
- **Acknowledge that small landlords form the backbone of the sector.** Our landlord survey (published in December 2023) showed that 80% of landlords own either one or two rental properties. Only 13% are classed as portfolio landlords, owning four or more properties and these providers own 39% of the stock meaning 61% is in the hands of smaller suppliers. It also showed that landlords accept modest returns, with an average net rental yield of 3.8% and return on equity of 3.7% excluding capital gains, a modest figure.
- **Recognise that, as with any industry, increased regulatory costs and risks will push up prices.** The PRS is now subject to over one hundred regulations, most of which have been introduced since 2004. The cost of these regulations will vary but there can be little doubt that they have had a marked impact across the sector, contributing to the increase in rents. Some of the regulatory changes being proposed in the Renters' Rights Bill may be justified but it is inevitable that the additional costs that these regulations impose on landlords will be passed on to tenants in higher rents.
- **Accept that increased risk for landlords will require higher returns.** One of the basic tenets of investment theory is that the more risk investors perceive in any given investment, the higher return they will demand on the capital they are deploying. The most extreme policy risk for landlords is rent controls, which remove their ability to price as they see fit. Until recently, the threat of rent controls seemed a distant prospect. But this changed with the Covid pandemic, when the Scotland government introduced rent controls in the form of a temporary rent freeze and the Mayor of London also called for the power to freeze rents. The Scottish government is now proposing long-term rent controls.

The risk associated with this policy is likely to deter some new investors while causing some existing landlords to exit the sector. But for those who remain, it will raise the required rate of return, meaning higher rents for tenants - the exact opposite of the intended outcome of the policy.

Chart 4 – % of mortgaged landlord that are loss-making at different mortgage rates



Source: IMLA landlord survey

To show the financial pressure already in evidence at the time of our survey, for this report we have calculated the mortgage rate at which individual respondents would tip into losses on an operating basis (i.e. rental income versus current expenditure). The results are shown in Chart 4. At a relatively modest mortgage rate of 4%, 30% of the mortgaged landlords in our survey would have incurred trading losses, rising to 49% at 5%. This is the kind of information we would hope government would take into account when setting policies for the PRS, as loss-making landlords may be more likely to exit the market if further costs or risks are imposed on them.

- **Acknowledge the ability of the market to drive up standards in the PRS.** The greatest safeguard against substandard housing is the tenant's right to shop around and find the best accommodation that fits his or her budget. When new regulatory requirements drive rents up, they reduce the range of properties that fit within any given tenant's budget. Indeed, if supply is so constrained that tenants are forced to compete for any accommodation they can find this is bound to undercut the objective of raising standards.

Ironically, this intense competition for properties and the corresponding necessity to compromise on the quality of accommodation, has driven calls for even more regulation. If that then causes some landlords to leave the sector, reducing supply, it will only exacerbate the plight of tenants still further, driving a kind of vicious circle of regulation, worse tenant outcomes and more regulation.

- **Apply policy more fairly across tenures.** The proposed minimum EPC C rating for PRS properties alone discriminates against the sector and has the potential to reduce supply, as landlords of low-rated properties can sell into the owner-occupied sector where no such rules apply.



4. Conclusion

In this report we have reiterated a call we have been making for some time for policymaking for the PRS to recognize that the sector is comprised of suppliers and consumers and can only function effectively if the suppliers are confident enough to maintain their investments. In contrast, the approach of both Conservative and Labour governments has been, since 2004, to add more and more regulation so that now there are over one hundred different rules landlords need to be aware of.

The regulations introduced over the last twenty years have always been presented by government as attempts to improve the tenant experience. Yet the outcome we see today is a tenant experience dominated in most parts of the country by an acute shortage of available accommodation and rising rents. Despite the accumulating evidence that landlords are failing to invest enough to meet demand, policymakers have consistently ignored landlords' concerns with the consequence of a chronically inadequate supply of properties to meet tenant demand.

The inevitable conclusion of this and many other studies into our PRS is that while it currently plays an essential role in housing some 19% of British households, disproportionate demands and expectations are being put on it to prop up what should be a much larger **public** rented sector. Continuing to put the size of the private rented sector at risk, while doing nothing to expand the public rented sector, will not solve the problem.

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About IMLA

The Intermediary Mortgage Lenders Association (IMLA) is the trade association that represents mortgage lenders who lend to UK consumers and businesses wholly or predominantly via the broker channel. Its membership of 53 banks, building societies and specialist lenders include 18 of the 20 largest UK mortgage lenders (measured by gross lending) and account for approximately 93% of gross mortgage lending.

IMLA provides a unique, democratic forum where intermediary lenders can work together with industry, regulators and government on initiatives to support a stable and inclusive mortgage market.

Originally founded in 1988, IMLA has close working relationships with key stakeholders including the Association of Mortgage Intermediaries (AMI), Building Societies Association, UK Finance and the Financial Conduct Authority (FCA).

Visit www.imla.org.uk to view the full list of IMLA members and associate members and learn more about IMLA's work.

About the author

Rob Thomas is a Director of Research at Instinctif Partners. He previously served as an economist at the Bank of England (1989-1994), a high profile analyst at the investment bank UBS (1994-2001) and as senior policy adviser to the Council of Mortgage Lenders (2005-12). He was also the project originator and manager at the European Mortgage Finance Agency project (2001-05) and created the blueprint for the government's NewBuy mortgage scheme and Deposit Unlock.