



# Spatial Economics Research Centre

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## Rental contracts

[Posted by Prof Henry G. Overman]

I've been incredibly busy with the new [What Works Centre for Local Economic Growth](#) so haven't had as much time as I would like to engage with policy debates. However, Labour's call for a [Commons vote on banning letting agent fees](#) did prompt me to take another look at their plans on rental agreements. I confess to being slightly puzzled.

I've always had the impression that the letting agent 'industry' is a pretty competitive business (certainly judging by the frequency with which estate agents pop up in my neighbourhood). This must mean that fees are set at a level that would roughly cover the cost of providing the service to landlords plus a profit mark-up for estate agents. If you make landlords cover these costs, instead of them being paid upfront by tenants, they will simply increase rents to cover the cost that they now incur. I can't see that this does much to change the cost of renting.

The effects of three year tenancies are equally unclear. If, as Labour propose, you use them as a mechanism for capping rent rises then this transfers price risk from tenants to landlords. The way that landlords will compensate for this risk is by setting higher average rents at the start of the tenancy leaving the risk adjust rate of return unchanged. This is similar to the way banks charge higher interest rates for fixed interest rate mortgages - the high average rate compensates the bank for the fact that it holds the interest rate risk. This will mean larger rental jumps for those at the end of three year tenancies. Regulating away this effect would require the government to fully determine rents (which isn't going to happen). So three year tenancies would appear to tradeoff short run rental increases for higher average rents and larger periodic rent increases. I have no idea whether this is preferable. I guess it might be if annual rent increases were currently very high - but they are not. Indeed, in 2012/13 the [English Housing Survey](#) showed average private sector rents decreasing (in contrast to social renters from local authorities or housing association who saw a 7% increase).

Will these measures help deal with 'rogue' landlords who use the threat of terminating tenancies to mistreat tenants? Possibly, but it is hard to know whether this is a big issue. [Shelter](#) have some figures that suggest that 12% of renters have not asked for repairs to be carried out in their home, or challenged a

rent increase in the last year because they fear eviction. As I've just suggested, on average the price effect of this doesn't seem to be very large. The repairs issue deserves further consideration - although note that this is the 'fear' of eviction that is claimed to be driving behaviour. How big a problem is this in practice? According to Shelter: "One in 33 renters have been evicted, served notice or threatened with eviction in the past five years because they complained to their local council or their landlord about a problem in their home.

This is the equivalent to 324,172 renters every year". That sounds like a lot of renters but I can't figure out how Shelter have calculated this. The 1 in 33 figure suggests that around 230,000 renters (out of 7 million in England) have been threatened sometime in the last five years which is around 46,000 per year. That is still a lot of individual misery, but it represents less than half a percent of renters. Of course, the complaint rate is endogenous so perhaps a better indicator are Shelter's figures suggesting that 1 in 20 tenants feel they have rented from a rogue landlord in the previous 12 months. Although given the tendency for disagreements between tenants and landlords this presumably represents an upper bound. Even if they represent 5% of the sector, one might think that there are more targeted ways to tackle the problem.

Overall, then, it seems to me that the impact of these proposals is likely to be quite modest, involving slightly higher average rents, and less frequent, but larger price increases. In short, as with so many housing initiatives, no big deal and certainly [not a solution to the housing crisis](#).

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