How local authorities can foster investment by corporate landlords in new private rental housing

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A report prepared for
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Foreword by Sigma Capital

Corporate landlords, as opposed to buy-to-let landlords, are providers of housing who retain ownership of substantial portfolios of properties and manage the letting of them: they build to let, constructing purpose built new homes for those looking to rent high quality and well managed houses and flats.

Corporate landlords are largely composed of two categories – those that acquire completed units for investment purposes and those that develop Private Rental Sector (PRS) properties as a form of housing tenure. The former are often institutional investors taking a long-term view whilst the latter are normally property companies taking a medium-term view but managing a greater degree of risk. Sigma is a specialist private rented sector and regeneration company occupying a key position in the latter category. It has built 2,000 new PRS homes, the majority being for families and helped to regenerate former local authority housing estates in the north of England. These are let on one year renewable leases which give Sigma's tenants the flexibility they want. Sigma has also recently established a Real Estate Investment Trust (REIT) raising £250m in 2017 (which when geared will increase to £450m) for the long term ownership of these new family homes. The REIT is the first one which is wholly concerned with PRS and this places Sigma firmly in the leading group of specialist PRS companies. Sigma also has the support of Government through its new agency, Homes England, the successor body to the Homes & Communities Agency.

Sigma is keen to work with local authorities to help create a new build-to-rent private rented sector that will better meet the needs of those seeking rental accommodations than the homes provided by many buy-to-let landlords. It commissioned Tony Crook and Peter Kemp, two leading experts on the private rented housing sector, to prepare this report. In it they explain the recent changes to demand and supply into the private rented sector and the potential of newly built private rented sector dwellings to meet the growing demand to rent. Importantly they spell out the advantages of a long term investment model for PRS and how local authorities can help create this new build sector and thereby secure many of their own housing objectives. Sigma is at the forefront of creating high quality, institutional, well managed family housing reflected in its innovation in forming the first PRS REIT and in its own fund.

We have prepared a number of case studies illustrating how together with partner local authorities, we have delivered good quality build to rent housing and the impact that delivery has on both local economic and social dynamic. Finally we would like to thank Professors Crook and Kemp for their hard work in putting this report together.

Duncan Sutherland
Regeneration Director

Introduction

In the last two decades there have been fundamental changes in housing tenure and supply. New house-building has fallen and is currently far below what is required to meet needs. Over the same period the social rented housing stock has declined; and, over the last decade, so too has the number of owner occupied dwellings. Meanwhile, there has been a marked growth in the private rented sector (PRS).

As a result, the PRS is now meeting a very wide range of housing needs including an increasing number of families with children.

But PRS growth has not involved the construction of many new homes. Instead, existing dwellings that were once owner occupied, and many that had originally been sold under the Right to Buy, are now privately rented.

Buy-to-Let landlords (BTL) own the vast majority of PRS dwellings, but most of them have only one or two lettings. They tend to be more interested in capital gains than in long-term rental income. Almost all private tenancies are short-term lettings, not the longer term ones that some PRS households would prefer.

In contrast to BTL, a more modern form of private landlordism would involve corporate owners operating on a substantial scale who invest long-term in purpose designed and built homes that are managed to high professional standards and let on long-term tenancies.

Until recently, attempts to create this modern form of private landlordism have met with little success. But most of the ingredients are now in place to foster the growth of this new PRS. There is now significant long-term investor interest. As a result, an increasing number of new dwellings specifically constructed for private renting are now being built. Partnerships between local authorities and the private sector could harness this new interest and unlock substantial new investment in good quality general needs rental housing.

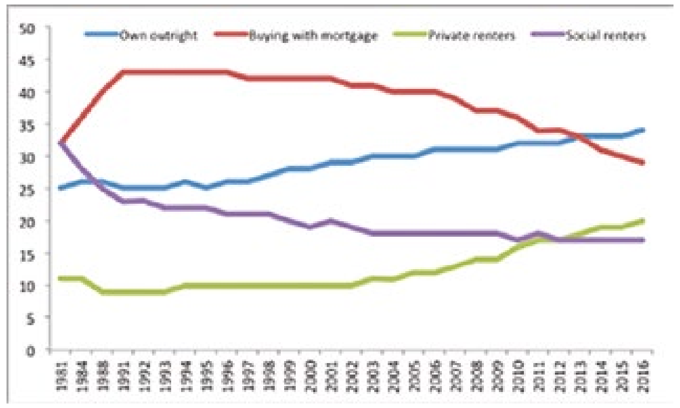
This paper therefore explains why and how local authorities are well placed to help create this modern PRS. By entering into partnerships with investors and developers, local authorities can help corporate landlords to raise the funds for newly built, good quality homes let to tenants from all household types, thereby helping meet key local housing needs.

Why are more people renting privately?

Key points:

- The number of households living in the PRS has doubled since the year 2000;
- One in five households now live in the PRS and growth is projected to continue;
- Growth is due to changes in demographic, migration, and financial factors as well as the decline in social rented housing.

Figure 1: Households by tenure (%)



Source: DCLG English Housing Survey

The number of households renting privately has almost doubled since the turn of the century. During the 1990s, about one in ten households lived in the PRS, but now one in five does so (Figure 1).

This trend is likely to continue. Indeed, projections by PwC (Price Waterhouse Coopers) suggest that a quarter of all households in the UK are likely to be renting their home from a private landlord by 2025[3]. Knight Frank's estimate is that 24% of households will be private renters by 2021.[4]

The growth of private renting has occurred for a variety of demographic, economic, and financial reasons. The decline of social rented housing is also a key factor.

Demography

The PRS has always been an important source of accommodation for young people under 25 years of age. But the propensity of young adults to rent privately has increased.

- The proportion of recent school leavers going into higher education has risen since the early 1990s. Most students live away from home, in university halls of residence, purpose-built student blocks owned by private companies, or shared houses and flats let by small-scale private landlords.
- The shift in student funding from grants to fees and loans, and the trebling of student fees in 2011, has reduced the effective demand for owner-occupation among recent university graduates. As they need to repay student loans once their earnings reach £21,000, graduates have less money to save for a deposit on a house.
- Young people tend to stay single for longer, and more often cohabit before marriage, than in the past. And the average age of marriage and of first having children – life events that often prompt a first house purchase - have both increased, thereby raising the average age of first-time buyers (FTBs).

Economic migration

The increase in economic migration to the UK, especially since the enlargement of the European Union in 2004, has been an important driver of PRS growth.

[3]Price Waterhouse Coopers (2015) Economic outlook 2015: Housing Market (London: PWC).
[4]Knight Frank (2017) Multifamily 2017: Tenant Survey (London: Knight Frank)

- Many economic migrants are young people for whom the flexibility of private renting is just the type of accommodation they need. Many share accommodation, often with other economic migrants from their country of origin.
- Among economic migrants who are older or have children, owner-occupation is often either not financially viable or not suitable for their needs.
- Some economic migrants are living in the UK only temporarily or wish to maximise their ability to save up or to send remittances to family members in their country of origin.
- Most economic migrants are not initially eligible for social rented housing.

For all these reasons, economic migrants tend disproportionately to live in the PRS.

Although a 'hard' Brexit may reduce migration from the EU27, the need for key workers in social care, the NHS, engineering, farming and other occupations is likely to limit the reduction in immigration.

Financial

House prices increased sharply from the mid-1990s – and rose even faster after the turn of the century – and at a much higher rate than average earnings. By 2007 the ratio of house prices to earnings had increased to an all-time high and was especially high for FTBs.

- In the mid-1990s the average house price was about double average earnings, but by 2007 it had risen to five times average earnings.
- Although house prices fell in 2008, they have increased strongly since 2013 across much of the UK and are well above 2007 levels.

The marked growth in house prices since the mid-1990s has had a corresponding affect on the amount of deposit that FTBs need in order to obtain a first mortgage.

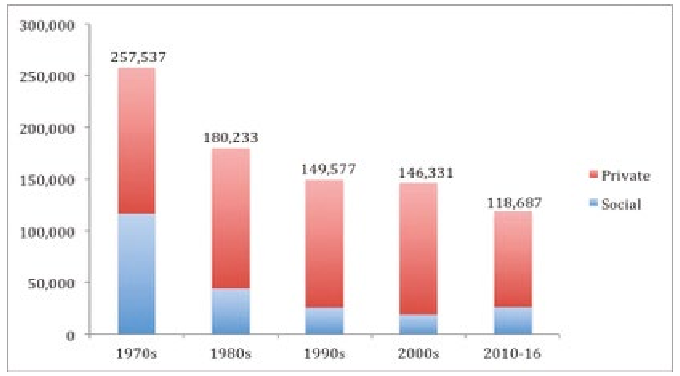
- According to analysis conducted by PwC, the average size of FTB deposits has increased almost five-fold since the late 1990s, rising from £10,000 to around £50,000.
- As a result, the number of years that prospective FTBs need to save for a deposit has increased sharply. The Resolution Foundation calculated that, for low to middle income households, it has gone up from 5 years in 1983 to 25 years in 2007 when house prices peaked.

As house prices surged out of reach for many prospective FTBs, they had to rent from a private landlord, at least for the time being. The difficulty of saving for a deposit has been compounded by the tighter mortgage lending constraints that have followed in the wake of the global financial crisis.

- Following the Mortgage Market Review, lenders are required to place more emphasis than previously on borrowers' ability to pay. They are now expected to conduct close scrutiny, not only of prospective borrower's income, but also of their spending habits.
- These more stringent lending criteria exclude some marginal prospective FTBs from homeownership, leaving them little option but to rent privately.

The principal underlying cause of the long-term growth in real (inflation-adjusted) house prices is the under-supply of new homes. The construction of new homes is currently about half what it was in the 1970s (Fig. 2). Estimates produced by the leading experts indicate that housing construction in Britain needs to double in order to meet population and household growth.

Figure 2: Housing completions (annual averages by decade)



Source: Dept of. Communities and Local Government live tables on house building completions for Great Britain.

Decline of social housing

It is not just the decline in the FTB market that has led to the growth in private renting. An important driver of the increase has been the long-term fall in the number of social rented homes.

- This decline began in the early 1980s and has continued under successive governments (Conservative, Labour and Coalition).
- The proportion of households living in social housing has halved since 1981, falling from one in three to only one in six.

Most of the fall in house-building (Figure 2) is due to the decline in the construction of new social rented homes. In the 1970s, social housing on average accounted for 45% of new homes completed in England. But in the 1980s, it accounted for only 24% and in the 2000s for only 13%.

This decline in social housebuilding largely involved local authority housing, the output of which fell from over 100,000 new homes pa in the 1970s to only 1,300 pa since 2010.

The share of output accounted for by social housing providers has risen since 2010, but this revival may be short-lived because of the planned demise of social housing grant for housing associations and the rent decrease of 1% pa in real terms for four years announced in the summer 2015 Budget. Meanwhile, the changes to the Right to Buy, including the 'voluntary' RTB (vRTB) for housing association tenants, will result in a further decline in the existing stock of social housing.

The 2017 Housing White Paper, Fixing Our Broken Housing Market, signalled the possibility of an expansion of local authority housebuilding. But the potential increase in output is likely to be offset by the effects of the vRTB and the partial shift of housing association construction away from 'affordable' rental housing and towards shared ownership and 'starter homes', which were announced by the government.

The net result is that low-income and moderate-income households, who in the past would have been able to obtain a council or housing association home, increasingly have to look instead to private landlords to provide them with accommodation.

Preference

Although owner-occupation is the preferred tenure for most households, some households would rather rent their home. Among private renters interviewed for the 2014/15 English Housing Survey who do not think they would ever buy somewhere, only 64% said this was because they were unlikely to be able to afford it. Reasons for not buying included not wanting that sort of commitment, preferring the flexibility of renting, liking where they are currently living and not wanting to be in debt.

What housing needs does the new PRS meet?

Key points:

- Increasing numbers of people aged under 45 (who used to buy) are now in the PRS;
- More household with young children now live in the PRS;
- There has also been an increase in low income households living in the PRS.

Generation rent

The PRS has not just doubled in size since the turn of the century, the roles that it performs in the housing market have also begun to change.

In the recent past, the PRS was largely a tenure for young and mobile households. Very often, it was only a temporary staging post while households saved up for a deposit on a house or waited for the offer of a social housing tenancy. But over the past decade, private renting has become more important among households of working age and especially among young people (Table 1).

The last decade has seen increasing discussion about 'Generation Rent'. This term refers to the marked increase in renting from private landlords among (1) young adults aged under 25 years and (2) 'young middle-aged' people aged 35-44 years.

This rise of private renting has been accompanied by a correspondingly sharp decline in owner-occupation among these age groups (Table 1).

The emergence of Generation Rent began in the 1990s, but the trend accelerated in the early 2000s and became even more evident in the wake of the global financial crisis.

The PRS is now the dominant housing tenure for new households. At the turn of the century, two in five new households lived in the PRS, but by

Table 1: Tenure by age of household head 1981 to 2016 (%)

		Owner occupiers	Social renters	Private renters	All
Aged 18-24	1981	32	36	32	100
	1991	36	28	36	100
	2001	22	31	46	100
	2016	10	26	64	100
Aged 25-34	1981	62	26	12	100
	1991	67	21	13	100
	2001	61	20	19	100
	2016	38	16	46	100
Aged 35-44	1981	69	23	7	100
	1991	78	15	7	100
	2001	73	18	9	100
	2016	56	17	26	100

Source: DCLG

the time the house price boom reached a peak in 2007/08 it had increased to one in two. Currently, three out of five new households rent from a private landlord.

But it is not just among new households that private renting has increased. The propensity to live in the PRS has increased more generally among young people and among 'young middle-aged' households. Thus, compared with 1981, private renting has:

- doubled among people aged 18-24
- quadrupled among 25 to 34 year olds
- trebled among people aged 35-44

Most of these increases in private renting have taken place since the turn of the century (Table 1).

The proportion of households aged 45-54 years who are renting privately also increased over the last decade, rising from 6% in 2006 to 15% in 2016.

Meanwhile, the owner-occupation rate among this age group fell from 80% to 67%.

More households with children in the PRS

Another fundamental change in the roles performed by the PRS is the marked growth in families with school age children living in the sector (Table 2).

In the recent past, the great majority of households with children were either owner-occupiers or social housing tenants, with very few living in the PRS. But this has begun to change.

- The number of families with dependent children renting their home from a private landlord has increased by 1 million, rising from 0.6 million in 2004 to 1.6 million in 2016.
- Over the same period, the number of owner-occupier households with children actually fell by 0.7 million.
- There are now more children living in private rental housing than in social housing (1.6m compared with 1.2m).
- Currently, a quarter of all families with school age children are private tenants. This proportion is likely to rise over the coming decade.

More low-income households

Another important trend, which reflects the decline in the social housing stock, is that an increasing number of low-income households are now looking to the PRS for their accommodation. In other words, the new PRS is playing a vital role in accommodating, not only people who might previously have become owner-occupiers, but also low-income households who in the past would have rented their home from social housing landlords.

Some of these low-income private renters are living below the poverty line.[5] In fact, over a third of private tenants are living in income poverty. They account for about a quarter of all poor households. Indeed, when household characteristics (such as age, gender, ethnicity, disability and employment) are taken into account, the odds of private tenants being poor are the same as for social housing tenants.[6]

In the PRS, three out of five lone parents, and two out of five couples with dependent children, are poor. About half of all private tenants living in poverty are workless – for reasons such as disability, caring responsibilities and unemployment - or else retired. The other half are in low-paid work.

The growth of the 'gig economy' - people working on zero-hours contracts or in other types of self-employment - has made private renting a more realistic option than owner-occupation for those whose income is too low or insecure to take out a mortgage.

Table 2: Households with children by tenure (%)

	2004	2016	Change
Owner occupiers	70	57	-13
Social renters	22	19	-3
Private renters	9	25	-16
Total	100	100	

The 2016 total does not sum to exactly 100% due to rounding
Source: DCLG

[5]Defined as having a disposable income after housing costs that is less than 60% of the national median.
[6]P.A. Kemp (2011) 'Low-income tenants in the private rental housing market'. Housing Studies, Vol. 26, pp.1019-34.

How well does the existing supply in the PRS meet housing needs?

Key points:

- PRS has a new image, with improved conditions and dwellings in a wider range of neighbourhoods than in the past;
- Satisfaction with PRS is much higher than in the past;
- PRS works well for households who want short-term tenancies;
- But where provided by BTL landlords, it currently works much less well for those wanting longer-term tenancies.

Improved image and better conditions

In the 1970s and 1980s, after decades of decline, the PRS was largely seen as a housing tenure for people who were not yet able to buy their home or who were waiting to be allocated to a social housing tenancy. Renting from a private landlord was widely regarded as a tenure that was suitable mainly for young and mobile people.[7]

At that time, many dwellings in the PRS were sub-standard and suffered from high levels of disrepair. Property management and maintenance, particularly at the lower end of the market, were often poor. And concerns existed about a minority of 'rogue landlords' whose practices were dubious or even illegal.

But the revival of private renting has witnessed a significant change in both the image and reality of the sector. Renting from a private landlord is now seen as a more mainstream form of housing provision.

Dwelling conditions have improved and a smaller proportion of the stock is very old or in disrepair.

Although most of the growth in PRS dwellings has resulted from purchases of formerly owner-occupied dwellings, a notable feature of the revival has been the influx of some newly built apartments and houses.

PRS dwellings are no longer predominantly inner city properties constructed in the nineteenth century and instead are more geographically dispersed. The new PRS is also located in new central city developments, as well as in suburbia and small towns throughout the UK. It is very often not possible to tell from the outside whether a property is owner-occupied or privately rented.

And as we note in the next section, the arrival of corporate landlords in the PRS seems likely to produce a transformational improvement in the quality, management and security of accommodation provided to private tenants.

High tenant satisfaction

For some time, surveys have consistently shown high levels of satisfaction among private tenants.

- The English Housing Survey (EHS), for example, found that 82% of private tenants were satisfied with their accommodation. Although this was lower than for owner-occupiers (94%) it was comparable to satisfaction levels in social housing (81%).
- Satisfaction levels in the PRS were high not only among single people living on their own and sharers. They were also high among most other demographic groups including lone parents (76%), couples with dependent children (76%) and the poorest households (80%).
- However, satisfaction with their tenure was much lower among private tenants than among owner-occupiers or social housing tenants. This reflects important differences from the other two main housing tenures.

[7]P.A. Kemp (2004) Private Renting in Transition (Coventry: CIH).

- Owner-occupiers have the possibility of making untaxed capital gains and social housing tenants benefit from below market rents.
- And while owner-occupation and social housing generally provide strong rights of occupation, the short-term leases that predominate in the PRS offer only limited security of tenure.

PRS works well for short-term renters

In general, the PRS currently works well for young and mobile households and especially for those who intend to rent for only a short period.

- Fixed-term one-year and six-month assured shorthold tenancies provide young and mobile households with the flexibility they want. They are not tied to one dwelling or area for long and can move elsewhere should they wish to do so.
- And, where such tenants wish to remain in the accommodation at the end of the fixed term, landlords are very often willing to either allow the tenancy to roll on or grant a new fixed-term tenancy.

PRS currently works less well for those wanting longer-term tenancies

But not all BTL landlords are willing to renew the tenancy when the existing tenant's fixed term has come to an end. Some decide to sell their property or let it to someone else. Hence:

- Tenants who wish to stay in their current home are therefore faced with uncertainty about whether their landlord will renew the lease at the end of the fixed term.
- The fact that, in the end, many BTL landlords do agree to grant a new tenancy does not mitigate the uncertainty or anxiety facing sitting tenants who wish to stay.

Frequent, enforced residential moves are especially a problem for tenants with dependent, school-age children. Particularly when accompanied by a change of school, such moves can negatively affect children's educational progress. They can also disrupt children's friendship networks and potentially harm their mental health.

Tenants moving home incur very substantial financial and other costs.

- Although deposits can be recycled from the old to the new landlord or letting agent, in a minority of cases they are withheld, for one reason or another.
- Landlords typically also require the payment of rent in advance.
- Letting agents currently charge prospective tenants fees for a range of items such as 'administration', credit checks and reference chasing (though the Government has proposed making such charges illegal).

Crossing the threshold of their new home, therefore, can cost tenants in excess of several thousand pounds in payments to letting agents and landlords. In addition, tenants may also have to pay for the hire of a van or for a removal firm.

For tenants whose move is voluntary, these financial outlays may be worth the benefits deriving from moving to their new accommodation. But for those who moved is enforced, the cost, hassles and other disadvantages of moving may be much less palatable. For tenants living on a low income, these costs may also be very difficult to afford. Moreover, a substantial minority of tenants in receipt of Housing Benefit (HB) report having difficulty in finding BTL landlords who are willing to take them when they move home.

In contrast with most BTL landlords, financial institutions and other long-term corporate landlords are able to provide more secure, long-term tenancies to those who need them including families with children and older private renters.

Who are the new investors in the PRS?

Key points:

- A key government aim is to increase corporate ownership, including with funding from financial institutions such as pension funds;
- Until recently there has been very little investment by corporate landlords; the building of new homes for the PRS has been limited;
- PRS has grown through investment in the existing stock by small scale 'buy to let' landlords;
- There are more professional managers, but much of the PRS is still self-managed by landlords who are poorly informed about management matters.
- There is now new interest and active investment in build to rent by corporate landlords

Why attract more corporate landlords?

Over the past quarter century, successive governments have wanted to encourage corporate landlords and financial institutions to invest in the PRS. Their aims are to attract large-scale long term investment in new high quality dwellings, let to high professional standards on long term tenancies. Corporate landlords' portfolios would be large enough to achieve economies of scale and to manage market and business risks better than small scale BTL landlords.

The Conservative government's 2017 housing White Paper endorsed the aims of attracting major institutional investment in 'large-scale housing which is purpose-built for market rent...to help provide more stable rented accommodation for families'.[8]

Because previous governments had recognised it would take time for corporate landlords to be attracted to the PRS immediately after rent deregulation in 1989, they established four initiatives to create new companies. But very few were created by these initiatives because tax and legal impediments made it difficult to set them up and the dwelling portfolios they needed simply did not exist.[9]

Although some new companies were established, these tended to be limited partnerships and property unit trusts with restricted investor liquidity and serving only niche markets, such as student housing.

The growth of individual landlordism

PRS supply growth, especially since the turn of the century, has been due to three factors, which have made rental housing attractive to individual investors.[10]

- The very rapid growth of house prices up to 2007 offered the prospect of substantial capital gains;
- Specialist BTL mortgages became available on attractive terms, making geared investments very competitive, especially as interest rates were relatively low.
- Alternative investments (including bank deposits and equities) became less attractive, especially to those investing for their own pensions. At the same time, the income from annuities declined as long-term interest rates fell.

For much the same reasons, the PRS continues to be very attractive to individual investors today. Recent changes to pensions legislation and pensions tax relief have further helped to make BTL an attractive part of pension 'pots' for some investors. However, the recent changes to mortgage interest tax relief will reduce the after-tax returns on rental income for BTL landlords (see below).

[8] *Department of Communities & Local Government (2017) Fixing our broken housing market. Cm 9352 (London: DCLG)*
[9] *A.D.H. Crook & P.A. Kemp (2011) Transforming Private Landlords (Oxford: Wiley Blackwell).*
[10] *A.D.H. Crook &P.A. Kemp (2011) Transforming Private Landlords (Oxford: Wiley Blackwell).*

Moreover, because of Bank of England concerns that BTL lending and investment is pro-cyclical and hence may be a macro-prudential risk for the economy, its Financial Policy Committee has made BTL lending subject to macro-prudential regulation. Regulated lenders are now required to place limits on BTL mortgages in relation to loan to value ratios and interest cover ratios. [11] This means BTL landlords will need to charge higher rents, secure cheaper loan finance, or put more equity into PRS investments.

Who are landlords today?

The PRS has become increasingly dominated by individual landlords (Table 3).

- In England the proportion of PRS dwellings owned by individuals rose from just over half in 1976 to over seven in ten by 2010
- The proportion owned by companies fell from 29 to 15 percent.
- Very few new landlords are property companies.

Table 3: Proportion of PRS addresses owned by different types of landlord in England

Type of landlord	1976	1993	2003	2010
Individuals & couples	55	61	67	71
Companies	29	20	17	15
Other	16	19	16	14

Source: Crook & Kemp, 2014

Average portfolio sizes have also fallen (Table 4):

- The percentage of PRS dwellings owned by landlords with less than 5 dwellings rose from 31 to 61 percent between 1976 and 2010.
- Landlords owning just one property constituted 80 percent of all landlords in 2010; they owned 40 percent of the total PRS stock.
- The size of company portfolios has also fallen.

Table 4: Proportion of PRS dwellings owned by landlords with different portfolio sizes in England

Number of dwellings	1976	1993	2003	2010
1	14	26	33	40
2-4	17	17	22	21
5-9	11	12	11	8
10-99	34	26	23	19
100+	26	18	12	11

Source: Crook & Kemp, 2014

An increased proportion of dwellings are now owned for investment purposes. In 2010, two-thirds of rental properties had landlords who owned them for investment purposes (44 percent for capital growth).

However, there remains a significant share of properties (31%) owned for non-investment reasons, including homes let to employees or relatives.

Although there have been no new surveys covering landlords of a representative sample of all PRS dwelling since 2010, recent surveys of PRS landlords confirm the overall picture revealed by the 2010 survey.[12 13]

However, there are signs of a re-emergence of residential property companies and growing interest in new-build rental housing by financial institutions.

Limited new building for the PRS

Very little PRS growth has come from new construction, with only 10 percent of properties in 2010 being specifically built for the PRS or acquired newly built. Growth has mainly come from changes in the tenure of the existing dwelling stock.

[11] *HM Treasury (2016) New buy-to-let powers to help Bank of England enhance financial stability (London: HM Treasury) https://www.gov.uk/government/news/new-buy-to-let-powers-to-help-bank-of-england-enhance-financial-stability*
[12] *K.Scanlon, C. Whitehead & P. Williams (2015) Taking stock. Understanding the effects of recent policy measures on the private rented sector and But-to-Let (London: LSE London).*
[13] *Kath Scanlon & Christine Whitehead (2016) The profile of UK private landlords, (London: Council of Mortgage Lenders*

There has been some new PRS construction in recent years:

- Apartment blocks where new landlords have bought flats 'off plan'.
- Corporate investment in niche markets, especially student housing.

Unite and UPP, two of the largest providers of purpose built student housing, have raised significant funds and achieved competitive returns. Other companies have now entered this sub-market and 2015 was a record year, with transactions worth £5.9bn including funding from overseas sovereign wealth funds.[14]

Some landlords are not well informed

Although specialist student housing providers have professional housing management, this is not the case for most individual landlords.

- Many are new to BTL and hence have little experience of letting property. Only two in five landlords used managing agents in 2010. Two-thirds of individual landlords had no relevant professional experience or qualification.
- Only six percent belonged to professional or PRS trade bodies.
- Individual landlords tend to manage market and business risk by investing only in familiar places, close where they live and work, thereby limiting portfolio sizes.[15]

Most of the PRS is thus owned by landlords with little housing management expertise. Although some use managing agents, this is not a regulated activity and many agents are not members of trade or professional bodies with codes of conduct.

Competitive total returns

Market rents tend to rise in line with average earnings and are much less prone than house prices to short-term fluctuations.

Recent ONS data shows that, between January 2011 and May 2017, rents rose by 14.7 percent in Britain as a whole, while average weekly earnings rose by 10.8 percent over the same period, the faster rise in rents reflecting the current housing shortage.

Although net income returns (net rents as a percent of vacant possession value) have not generally been competitive compared with other investments (between 3 and 5 percent), total returns (net income returns plus capital growth) have been competitive. House prices rose by 31.5 percent between January 2011 and April 2017 making total returns on rental housing competitive with the returns from equities, bonds and commercial property.[16]

Changes to individual landlord taxation

The tax changes for individual BTL landlords being implemented from April 2017 onwards will reduce their rental returns. This is for two reasons:

First, the tax relief on individual landlords' interest payments will be restricted to the standard rate of tax. Higher rate taxpayers will therefore no longer receive relief at their marginal rate of tax (40% or 45%); it will instead be 20%, the same as for standard rate taxpayers.

Second, BTL landlord mortgage interest relief will no longer be offset against taxable income, but instead be paid as a tax credit.

- BTL landlords will thus be taxed on their turnover instead of their net profit.
- This could push some basic tax rate landlords into a higher tax band and/or mean that their after-tax return becomes negative.

It is possible, therefore, that these changes to individual landlord tax relief will prompt some BTL landlords to disinvest and some prospective landlords not to enter the BTL market. This will depend on the extent of landlords' debt funding and the returns from alternative investments.[17]

[14] *Savills (2017) Spotlight UK Student Housing, (London: Savills World Research)*
[15] *E.T Ferrari, A.D.H. Crook & P.A. Kemp (2012) 'Knowing the area: the management of market and business risks by private landlords in Scotland'. Urban Studies, Vol. 49, pp 3347-3363.*
[16] *Goodchild, R. & A. Stanford (2016) The case for UK Private Rented Sector, (London: Jones Lang LaSalle)*
[17] *K.Scanlon, C. Whitehead & P. Williams (2015) Taking stock. Understanding the effects of recent policy measures on the private rented sector and Buy-to-Let (London: LSE London).*

Even if they place their ownership within a company structure (which is not affected by these tax changes) this is costly because of the potential stamp duty land tax (SDLT) and capital gains tax liabilities arising from transferring properties to a company.[18] Although there is evidence of BTL landlords setting up limited companies,[19] they generally have small portfolios built up by acquiring existing BTL property and not by building to rent.

Changes introduced in April 2016 to SDLT will also increase all (including corporate) landlords' costs as a surcharge of 3 percent has been added to the SDLT liabilities of all purchasing additional properties.

Likewise, all residential property landlords who are not limited companies are now liable for an 8% capital gains tax (GCT) surcharge. This is because private rental housing was excluded from the cuts in CGT rates - from 28% to 20% (higher rate) and from 18% to 10% (lower rate) - introduced by David Cameron's government.

New investment by financial institutions and corporate landlords

There are now signs of new interest in build to rent:

- Announcements in the specialist property press showed that 27,683 new build to rent dwellings were contracted between January 2010 and April 2016. The British Property Federation's 'build to rent map' showed that, by quarter 2 of 2017, 83,650 had been completed, were under construction or were being planned.[20]
- And in 2015 the total invested in the PRS by property companies, other developers, financial institutions and other funders was £2.65bn.[21]

[18] J. Pickford (2015) 'Osborne tax revamp shakes buy to let to its foundations'. Financial Times FT Money Supplement. 17th October, pp 10-11.
[19] Evans, J (2017) 'Landlords set up as limited companies to beat tax rule', Financial Times, 17th April, p2.
[20] British Property Federation (2017) Build to Rent Map of the UK. http://www.bpf.org.uk/what-we-do/bpf-build-rent-map-uk
[21] Savills (2016) Spotlight Rental Britain, (London: Savills UK Research)

Why do property companies and financial institutions want to invest in the PRS and what barriers do they face?

Key points:

- The projected growth in demand for private rental housing will require substantial funding;
- There are significant opportunities for financial institutions and other funders to invest in the PRS;
- Many of these funders are major investors in commercial property, but not yet in residential lettings;
- The PRS offers important attractions to funders and developers, but there are barriers to such investment that need to be overcome;

Corporate landlords and their funding

New corporate owners and their funders include property companies and developers, banks, building societies, life funds, pension funds and fund managers, and also housing associations and housing management companies. They include sovereign wealth funds, venture capital as well as overseas investors lending via UK investment banks. Many of the latter have long invested in residential property in other countries.[22] And some UK companies have also invested in the PRS overseas, for example in Germany.

'City' funders, including (but not only) pension and life funds, are very important to the future growth and quality of the PRS:

- It was estimated that equity investment of £57bn pa was needed in 2016 (double the annual buy to let lending, excluding re-mortgaging, in the peak of 2007) if PRS supply was to meet demand.[23]
- Projections by PwC of the likely growth of the PRS to 25 percent within 10 years suggest similar future funding requirements.

Institutional investors, such as pension and life funds, have substantial funds to invest, recently estimated at £3tr in 2011, but only 0.9 percent of their £119bn invested in property was in housing.[24] However new investor interest has increased this. By 2015 PRS represented 5 percent of mainstream investors' total property investments, having risen from 2 to 3 percent of total PRS investment in the UK.[25]

PRS is now recognised as an asset class on its own, offering competitive total returns to financial institutions and other funders. Residential has not only outperformed commercial property and other UK asset classes over the long term but it has lower volatility and low correlations with these other classes, thus matching investors' needs for a mix of asset classes.[26] PRS provides:

- Income from rents (rising in line with earnings) and long-run real capital growth, each moving in different cycles.
- Assets meeting needs for a long-term and secure income matching their outgoings and other required returns.
- Investments with a lower volatility profile than other assets (e.g. bonds, equities, commercial property) and good risk diversification because PRS performance is lowly correlated with these other asset classes.

Better total returns than equities, gilts and commercial property, with the latter outperforming residential only in the boom years of 2004 to 2007.[27] Because potential PRS funders

[22] A.D.H. Crook & P.A. Kemp (2014) (eds) Private rental housing: comparative perspectives (Cheltenham: Edward Elgar).
[23] Jones Lang LaSalle.
[24] Property Industry Alliance.
[25] Investment Property Forum (2016) Size and structure of the UK Property Market. End 2015 Update, (London: IPF)
[26] Goodchild, R. & A. Stanford (2016) The case for UK Private Rented Sector, (London: Jones Lang LaSalle).
[27] Investment Property Databank.

are interested in long-term returns, they are not focused, like many buy to let landlords, only on providing short-term tenancies but principally letting on longer term ones. It has been estimated that long-term tenancies improve returns, especially if rents are indexed to RPI.[28]

Barriers to corporate PRS investment

Given these competitive returns, why have property companies and funders been reluctant until recently to invest in the PRS? There are six main reasons.

1. Portfolios matching corporate owners' needs do not yet exist.

- There is not enough new PRS stock in relation to the capital available to invest.

Investors want good quality newly built dwellings in desirable locations, in sizeable tranches (to create management economies), each worth £30m to £50m and in different locations (to spread market risk);

- But financial institutions are not themselves developers, wanting instead to acquire property already fully let and showing competitive returns; this is why property developers are key to getting new build PRS 'off the ground', although financial institutions are now more willing to 'forward fund' and thus share the financing of the initial development phase;

2. Net income returns are not yet adequate.

- The market has delivered substantial total returns (i.e. income plus capital gains) but not the income returns that corporate landlords need, partly because management and maintenance costs take up to a third of gross rents.
- Un-geared net income returns have been running at 3 to 5 percent, below the 6 to 7 percent currently required (although with a maturing market the latter could fall to 5 percent).
- Total returns are more competitive for investors, especially in comparison with current alternatives, including a less competitive commercial property market, lower interest rates, and less attractive bond markets.
- To make total returns competitive landlords need to realise capital growth by selling vacant poorly performing dwellings; large portfolios are needed to generate an adequate flow of vacancies. Trading in this way also ensures the long term continuation of a competitively performing portfolio.

4. Poor liquidity.

- Establishing residential property companies (including REITs) is important if the PRS is to be a liquid investment with shares traded on the stock markets.
- As PRS becomes a more established asset class institutions investing directly into PRS through the direct ownership of dwellings will find it easier to dispose of these portfolios to other investors.

5. Political and reputation risk.

- Political risk for investors, developers and property companies (that the PRS will be wholly re-regulated) is now no longer a barrier to investment (with few investors concerned about mandatory three year leases) and the once wholly negative images of landlords are also mainly a distant memory;
- But the continued existence of poor conditions and bad management in some parts of the PRS poses a reputation risk for property companies and their funders, keen to protect their reputations.
- Local authorities have now been given additional powers to enforce standards and to deal with 'rogue' landlords, including increasing fines.

6. There are some remaining tax disadvantages.

- REITs removed one of the barriers by ensuring tax transparency, especially important to pension and life funds indirectly investing in residential property companies; and rules that had prevented new residential REITs getting started were changed in 2012.
- Whilst SDLT on bulk purchases was changed in 2011, significantly reducing the tax 'hit' on transactions costs, the imposition of the 3 percent surcharge (see above) has increased tax charges on purchases;
- There is now an 8% CGT surcharge on residential rental property owned by individual landlords and partnerships (but not on commercial rental property);
- There are still some remaining tax barriers, specifically irrecoverable VAT (lettings are VAT exempt), including payments to property managers.

Overcoming the barriers

The above summary shows that some steps have been taken to remove but others remain. Overcoming them requires:

- Constructing high quality dwellings, purpose built for the PRS;
- Reducing land, construction and management costs;
- Tackling 'rogue' landlords, to ensure the PRS becomes a reputable investment;
- Local authorities accepting the need for new build for PRS and using planning legislation and their land holdings to encourage provision;
- Central government providing continued stability in the regulatory framework so that developers and funders can invest long term.

[28] *Jones Lang LaSalle.*

How can the barriers to creating a new build PRS be removed?

Key points:

- Many barriers have been tackled by recent government initiatives;
- But development costs and risks remain a major barrier;
- Local authorities and developers are well placed to overcome these;
- Designs should take account of the variety of market demand;
- Improving PRS reputation by eliminating poor management;
- Separating those who did initial development and letting from long term ownership would remove development risk for long term owners;
- Local authorities and housing providers could play a crucial role in facilitating and undertaking the development stage.

The government has recently taken a series of steps to tackle the barriers to PRS investment.

Montague review

The government set up the Montague review in 2012 to examine how new corporate investment could be attracted. It concluded that:

- Large scale PRS developments were attractive, because total returns were competitive;
- Land, development and management costs had to be reduced because net income returns were too low;
- Planning was critical, as land valuations assumed completed dwellings were sold to owner occupiers while planning obligations requiring affordable housing meant including PRS within a scheme made it unviable;

Removing development risk

Other reviews also argued that removing development risk was critical and would deliver good long term total returns:

- Accessing public sector land (including that owned by local authorities and the Homes & Communities Agency), perhaps with deferred payment, is important, plus funding from local authority pension funds and requiring the inclusion of PRS housing in S106 planning obligations;[30]
- Housing associations with strong balance sheets, development and housing management experience could build and let new PRS schemes and then refinance them by selling onto funds, while keeping the management role;[31]
- By careful site selection and construction and efficient management, returns from geared investments would be competitive.[32] Forward funding of construction and pre sales of PRS units can achieve better returns for developers than speculative building for owner occupiers.[33]

[29]Department of Communities & Local Government (2012) Review of the barriers to institutional investment in private rented homes: report of the 'Montague' review (London: DCLG).
[30]House of Commons (2012), Financing of new housing supply, Eleventh Report of Communities & Local Government Committee, Session 2010-12, House of Commons Paper 1652, (London: The Stationery Office).
[31]Building & Social Housing Foundation (2012) Building New Homes for Rent, Creating a tipping point (Coalville, The Foundation).
[32]Resolution Foundation (2012), Making institutional investment in the private rented sector work, (London: The Foundation).
[33]Investment Property Forum (2015) Mind the viability gap: achieving large scale build to rent housing, (London: IPF).

Government support for new build PRS

The 2010 to 2015 Coalition Government:

- Set up a £1bn 'build to rent' fund for new PRS developments; Public sector bodies, including local authorities, were eligible; A DCLG task force was set up to help broker deals;
- A £3.5bn guarantee fund (plus £3bn in reserve) was created to underpin fixed income debt for PRS development;
- Speeded up the identification and release of public sector land.

The government expected the Build to Rent fund to produce 10,000 new PRS dwellings. By May 2016 3,824 PRS dwellings were planned in contracted schemes. Later that year the fund was made part of the Homes & Communities Agency's Home Building Fund with no specific PRS targets. By then PRS had become more attractive to private funders. Developments were attracting forward funding as well as long term finance.

In its 2017 housing White Paper the government announced a consultation on changing the National Planning Policy Framework to include Build to Rent as an explicit form of housing to be identified in local plans. It is also consulting on using planning obligations to require developers to provide 'affordable private renting' let on 'family friendly' three year tenancies as an alternative to other forms of affordable housing.[34]

Purpose-designed new build PRS housing

The design of new PRS is crucial to reducing construction costs in ways consistent with meeting demand:

- creating designs that minimise maintenance and wasted space in apartments (but consistent with demand);
- maximising tenant demand, including offering additional amenities and creating a sense of place and community;
- Apartment blocks in city centres close to public transport nodes will meet the requirements of young professional households;
- Traditional dwellings, car parking and adequate garden space for playing and relaxing in more 'suburban' neighbourhoods is also needed because the modern PRS includes households with children;
- Build to rent also offers scope for modern methods of construction including off-site manufacturing, something that has been critical to the success of purpose built student accommodation. Legal & General have already invested in such a facility.

New government support for improving quality of existing PRS homes

The government's recent initiatives include:

- banning 'rogue' landlords and lettings agents, allowing local authorities to impose fines of up to £30,000;
- extending licensing of houses in multiple occupation;
- requiring transparency about fees lettings agents charge prospective PRS tenants and proposing to ban them altogether;
- consulting on requiring lettings agents to protect clients' money and cap deposits at one month's rent;
- consulting on introducing mandatory electrical safety checks (only gas safety checks are currently obligatory);

[34]Department of Communities & Local Government (2017) Fixing our broken housing market. Cm 9352 (London: DCLG)

The potential contribution of new-build PRS homes

Key points:

- New build PRS can support local housing strategies;
- It would increase housing supply and thereby help restrain price and rent increases;
- It provides long term lettings and better management of the PRS;

Local housing strategies

Facilitating the construction of new PRS homes by pension funds, insurance companies and other large-scale corporate investors and developers has the potential to make a major contribution to local authority housing strategies.

The impact of new build PRS

These corporate investors have substantial sums that they need to invest in relatively large-scale projects.

- Investment in purpose-built portfolios of new houses, or in blocks of apartments, could make a significant difference to the volume of new rental supply at the local authority level.
- And it could do so without draining off new dwellings produced by speculative house-builders in the open market for sale to owner-occupiers and buy to let (BTL) landlords.
- This new addition to supply could help to take the pressure of rising house prices and private rents in the locality, which would thereby benefit both FTBs and tenants in the PRS. In the latter case, it could also help minimise the rising cost of Housing Benefit.

Such investment would involve new dwellings that are purpose-designed for private renting, high in quality and well maintained.

Over time, sustained investment by corporate landlords could have a cumulative impact on the overall standard of private rental housing in the locality. It could also potentially help to raise expectations about what is an acceptable standard of accommodation in the PRS. The influx of private halls of residence by firms such as Unite and Opal (see above) has arguably had an effect along those lines in the student market.

Increased new build PRS will also enable local authorities to eliminate, through enforcement action, the minority of poor condition PRS dwellings owned by 'rogue' landlords without the risk of reducing overall PRS supply. It will also help local authorities secure investment on stalled brownfield sites especially in inner area regeneration areas where there will be demand by 'generation rent' and other tenants for PRS properties near city centre work and leisure opportunities.

Improved property management and greater tenant expectations

Large-scale corporate landlords need to protect not only the value of their investment but also their reputation. To pursue both of these objectives, they will use either their own in-house property management team or employ well-respected managing agents to provide it for them.

Again, this could help raise expectation levels among tenants about what they should be expecting from their landlord in property management, for example, in relation to the quality of repairs and the speed with which they are carried out.

Long-term lettings

A very important feature of investment in property by large-scale companies is that it is an inherently long-term venture (see above). And although the prospect of capital gains inevitably enters the investment appraisals made by corporate landlords, rental income is typically as important or more important.

This distinguishes them from most BTL landlords, whose investment horizon is often short-term and rarely long-term. Likewise, for many BTL landlords, capital gain is their main motivation for investment in the PRS. Corporate landlords are much less likely than BTL landlords either to sell out just because house price inflation has peaked or to get into financial difficulties because interest rates have gone up.

This capital gain orientation is likely to become even more important for BTL landlords following the reduction in mortgage interest tax relief announced in the summer 2015 Budget. This change will significantly reduce post-tax rental yields earned by BTL landlords who have geared up their investment by taking out mortgages. As a result, although taxed, capital gains will become a proportionately larger share of the (reduced) profits on private rental housing.

Corporate landlords are not affected by this change in mortgage tax relief, as they will continue to be taxed on their net profits (gross profits less eligible expenses including interest charges).

The fact that corporate landlords who invest in new purpose built PRS are long-term investors, and often focus more on rental income than capital gains, has important implications for the people whom they house.

- They will be much more willing than BTL landlords – and will prefer – to let their properties on long-term and not short-term lettings.
- Long-term landlords prefer long-term tenants because that results in fewer re-lettings than with short-term tenants. Re-letting properties typically involves:
  - additional expenditure by the landlord (for items such as administration costs, letting agent fees, and redecorations);
  - void periods and hence loss of rental income
  - business risk (for example, about whether the new tenant pays the rent, looks after the property and does not annoy the neighbours).
- By reducing these costs long term landlords can improve their net rental returns,

Meeting the needs of families and older people

From this perspective, families and older people, who are among the groups most likely to need long-term tenancies, will be attractive tenants for large-scale corporate landlords. Thus the need for long-term tenancies and residential stability that BTL landlords are often not willing or able to provide, could be provided by corporate landlords.

By providing purpose-designed and built rental dwellings, that are let and managed by reputable companies with a long-term horizon, corporate landlords could help to meet the housing needs of families no longer able to either obtain a social housing tenancy or buy their home. It could also take some of the pressure off social housing waiting lists in the local authority. This is a common practice in some other countries, especially Germany, where private landlords play an important role in providing social rented homes with long-term tenancies.[35]

[35] *A.D.H. Crook & P.A. Kemp (2014) Private rental housing: comparative perspectives (Cheltenham: Edward Elgar).*

What can local authorities do to bring investment in new build PRS housing to their areas?

Key points:

- Planning policy and planning obligations are key to securing land values that help make returns competitive;
- Selling surplus public sector land at prices that reflect returns from PRS development will also be important;
- Local authority pension funds are an important source of equity capital;
- Private developers are likely to be key partners;
- Local authorities should do more to enforce standards in the existing PRS as well as getting more supply through new building

Local authorities working with developers are critical to unlocking the £30bn of finance that developers and funders are prepared to invest to build 150,000 new build PRS homes.[36]

Local plans

Local plans (which all local planning authorities were required to have in place by 2017) can set out the need for new PRS dwellings. Paragraph 50 of the National Planning Policy Framework states that authorities "should plan for a mix of housing ….. and should identify the size, type, tenure [emphasis added] and range of housing that is required in particular locations, reflecting local demand".

- The national Planning Practice Guidance stresses (para 159) the importance of basing needs on Strategic Housing Market Assessments which should identify the scale and mix of housing and the range of need over the plan period. Local plans should have a delivery schedule and implementation strategy for the full range of housing.
- Authorities can also identify sites in their Strategic Land Availability Assessments that suit PRS development.

Planning agreements and obligations

Planning authorities can use S106 agreements to secure PRS housing. These have been widely used to secure contributions of affordable housing from private developers with the costs generally falling on landowners as lower land prices. As far as PRS is concerned:

- Because returns from PRS dwellings come over the long term, the initial capital values of new PRS homes will be less than if they were sold for owner occupied market housing; hence land for PRS is worth less than for owner occupation.
- Using S106 to require some PRS housing can help developers make a scheme with PRS housing viable because they can use these lower market land values in their negotiations with landowners. National planning practice guidance on viability encourages authorities to take the economics of PRS provision into account.
- Some authorities are already using S106 to secure provision of PRS. Wandsworth London Borough was the first authority to require this, taking PRS provision into account when assessing the viability of the planning obligations it sought from developers.

To ensure availability in the long term some planning authorities are requiring PRS covenants on S106 sites so that if any are subsequently sold into the owner occupied sector within a specific time frame payments can be made to the local authority for the loss of the PRS element.

[36] *Property Industry Alliance and British Property Federation*

Local authority land and pension funds

Local authorities can also make their own land available to PRS developers including on long term leases with ground rent income to local authorities.

- Public sector landowners have obligations to secure the best consideration when selling land but they also need to take account of proposed uses and do not need to sell for the very highest values that can be a secured on a site.
- This is important in setting land values that represent PRS use value rather than use for owner occupied dwellings, which is likely to be higher.
- It will help reduce the overall costs of PRS projects and deliver more competitive returns.
- Other options include selling land on a deferred purchase basis, enabling developers to work on land under a licence, with land sold (or leased, so the local authority gets a ground rent in the long term) at a PRS value when construction is completed and homes are fully let.

Local authority pension funds can also play key roles, by providing equity funding for completed developments.

- This is an opportunity for pension fund trustees to acquire a new asset class with returns that match their liabilities;
- It helps pensions funds meet local housing needs without breaching trustees' fiduciary duties.
- Some local authorities are considering joint ventures involving local authority land and pension funds, together with building and housing management companies.

Key partners

Successful projects will need developers willing to undertake development: acquiring land, constructing new dwellings, raising the funds to do so and then letting out and managing them.

- Some developers will want to continue owning and letting the new PRS dwellings and will seek long term debt and equity funding to replace the short term funds raised for the construction phase.
- Others will want only to take the initial development risk and make initial lettings but then sell on the completed project to a long term owner, including a REIT, a pension or a sovereign wealth fund.

Partnership arrangements

Local authorities have powers to engage in PRS derived from their general powers of competence provided they use powers reasonably.

- A key role for local authorities is to take the lead in building partnerships but if they engage in commercial activity they need to use 'vehicles'.
- Sometimes these will involve a contractual relationship between local authorities and partners,
- At other times, including when there are many partners involved, these can be structured on the lines of corporate joint ventures, including companies limited by shares and limited liability partnerships, the latter especially important to achieving tax transparency.

Dealing with poor conditions

Another important role for local authorities is to secure improved conditions in the worst parts of the existing PRS by enforcement led action. This is an important complementary step ensuring that, as overall supply expands, the worst conditions are dealt with, an important objective in its own right but also helping to improve the overall reputation of the PRS, which is important to funders' willingness to invest. The government has taken several steps (see above) to enable more to be done.

Conclusions

The PRS had doubled in size in the last two decades and now houses 1 in 5 of all households in England. It is increasingly the home of 'generation rent' and now also houses many households with young children.

The growth of the PRS has largely resulted, not from new construction, but from the transfer of formerly owner occupied and local authority owned housing. Most landlords are private individuals who operate on a very small-scale, mainly investing for capital gains and letting on short term tenancies. Although the PRS now has a much better reputation than in the past, with many dwellings in good condition, located across all types of neighbourhoods, and adequately meeting the needs of those seeking short term accommodation, there are still significant challenges.

Most BTL landlords do not have a long term investment horizon, which creates the risk that the PRS is a very volatile part of our housing supply. Few BTL landlords have the professional knowledge and skills needed to manage their tenants' homes properly; few newly constructed dwellings are coming into the PRS market; and the sector does not adequately meet the needs of those seeking longer term accommodation. Meanwhile, recent tax changes affecting individual landlords are likely to reduce BTL returns and therefore lead some existing landlords to disinvest and deter new landlords from entering the market.

What is now required is the development of a more modern form of private landlordism that involves corporate owners operating on a substantial scale and investing long-term in purpose designed and built homes that are managed to high professional standards and let on long-term tenancies, but meeting the needs of both short and long term tenants alike.

Many of the barriers that once prevented the emergence of this corporate sector have now been removed. The long term income returns that can be earned from an efficiently constructed and managed newly built sector are attractive to many developers and their funders (including pension and life funds because the long term returns match their liabilities).

Most of the tax and legal impediments to the emergence of this corporately owned PRS sector have been largely removed and the government has set up a special fund to help 'kick start' new building for the PRS. But potential investors cannot find the large scale well managed portfolios that they need to make their investments work. Nor do they want to take on the tasks and risks of creating these new developments themselves. What they want instead is to be able to acquire newly built and fully let portfolios producing the income returns they want.

What is needed to create this more modern PRS is a partnership to take on this 'development risk'. Residential property companies and local authorities are well placed to do this. Property companies can bring their development expertise and development finance to the partnership. Local authorities can bring their planning powers, their land banks and long term pension funding into the partnership.

Working together, local authorities and property companies now have the opportunity to create a portfolio of newly built PRS dwellings, meeting a wide range of housing needs. This will help local authorities to meet their strategic housing requirements and assist households who are unable to buy their home and are not a priority for social rented housing. A new-build PRS sector constructed through such partnerships will reduce overall housing shortages, thereby helping to dampen increases in house prices, rents and housing benefit payments. By adding to the housing stock in this way, local authorities will be better placed to remove the poorest PRS properties owned by rogue landlords because their tenants will have somewhere else – higher quality, more secure and better managed – in which to live.