

Affordability of Housing Association Rents: Rent-to-Income Ratio vs. Residual Income

Summary

Introduction

This briefing paper examines residual income measures to investigate the impact of housing association (HA) rents on individual household's capacity to afford an adequate standard of living. It compares these findings with those for the rent-to-income measure which look only at housing affordability. Rent-to-income ratio and residual income measures for new tenants in general needs dwellings are examined by region, household type and bedsize from 2002/03 to 2007/08. Then, rent-to-income ratio and 'after housing costs' for existing tenants by region and household type in 2006/07 are employed to identify the impact of low income and high rent on affordability in the sector.

Methodology

Two data sources are used to obtain information on household incomes and rents: the COntinuous REcording (CORE) system for new tenants and the Family Resources Survey (FRS) for existing tenants. The two datasets use different definitions of incomes. For new tenants, rent-to-income ratio is the proportion of net weekly rent to the total net weekly income (income excluding tax credits, housing benefit (HB), council tax benefit and interest from savings). For existing tenants, it is the ratio between the net weekly rent and the gross weekly income which is the total household income before tax, including earnings, investments, retirement pensions, income support, tax credits, benefits (HB, council tax benefit, disability benefits and other benefits). Two residual income standards are also used: 120 percent of Income Support allowances for new tenants and 60 percent median (equivalised) income for existing tenants. New tenants who have residual income (the net weekly income left after the net weekly rent) and existing tenants who have 'after housing costs' (included gross rent, water rates and sewerage charges) below the standards are regarded as poor.

Key findings

Rent-to-income ratios for new tenants in 2002/03–2007/08 using CORE

- With the exception of London, all regions experienced improved affordability of HA rents as rent-to-income ratios declined between 2002/03 and 2007/08.
- London was the only region where affordability deteriorated. Affordability ratios increased from 0.44 in 2002/03 to 0.46 in 2007/08 before HB. This was because average rents for new tenancies in London rose fastest while average incomes of London's new tenants increased slower than average rents.
- Rent-to-income ratios, both before and after HB, were higher for households with only one adult (single elder, single adult and single parent) than they were for those with two or more adults (two elders, two adults and two-parent families). Rent increases for smaller properties (i.e., bedsits and properties with one or two

bedrooms) were quite consistent between 2002/03 and 2007/08, but the much slower growth of incomes, in contrast to rents, led to increased affordability ratios during this period. By contrast, rent increases for larger properties (i.e., those with three or more bedrooms) slowed while average weekly incomes for households living in larger size properties were steady, leading to a reduction in affordability ratios over the period.

Residual incomes for new tenants in 2002/03–2007/08 using CORE

- On average, new tenants in England enjoyed 18 percent growth in residual incomes in the period 2002/03–2007/08. In 2004/05, about 53 percent of new tenants in England had residual income below the 120 percent Income Support standard. This proportion increased slightly to 56 percent in 2007/08.
- New tenants in London had the lowest residual incomes, and their average residual incomes increased the least, seven percent, between 2002/03 and 2007/08. This is mainly because London's new tenants had the second smallest increase in average incomes, after Yorkshire and the Humber. Thus, London was the region having the largest proportion of new tenants (61% in 2004/05 and 63% in 2007/08) below the standard, confirming the fact that average incomes of new tenants in this region were falling over time.
- Families with children were most likely to have affordability problem. Most importantly, lone parents, having the largest rent-to-income ratios, not only had the smallest amount of residual income amongst families with children between 2002/03 and 2007/08, but also had the largest proportion (around 88%) with residual incomes below the standards.
- For couples without children, two elders were more likely to have residual incomes below the standards (over 60% in 2004/05 and 2007/08).
- Within single person households, non-elderly adults (those below 60 years old) were more likely to have the problem. Single non-elderly adults had the smallest increase in incomes amongst all new tenants over the period 2002/03 to 2007/08. They also had the largest rent-to-income ratios and were more likely to have residual incomes below the standards.

Rent-to-income ratios and residual incomes between existing and new tenants, 2006/07, using FRS and CORE

- FRS uses gross incomes and CORE uses net incomes. Thus affordability ratios for existing tenants were all below 0.25 in 2006/07. But for new tenants, ratios were all above 0.30, with London having the largest ratio of 0.47.
- At national level, proportions of households with incomes below the 60 percent median (equivalised) income were 18 percent for Before Housing Costs and 39 percent for After Housing Costs in 2006/07. The Eastern region had the largest proportion of existing tenants (43%) with incomes below the standard the After Housing Costs standard.
- London had the largest gap between Before Housing Costs (14%) and After Housing Costs (41%). In 2006/07, proportions of households below the standard in London and the Eastern region were very close to those in the North West and the Yorkshire and the Humber.
- In terms of household type, over half of families with children in 2006/07 had incomes well below the standard Before Housing Costs with 60 percent having incomes below the After Housing Costs standard. This particularly affected lone parents with two children (58% Before Housing Costs compared to 72% After Housing Costs).

Conclusion

The residual income measure complements the rent-to-income ratio measure. Together they confirm that HA tenants in London and lone parents in England are most likely to face the dual problem of high affordability ratios and low residual incomes. This is mainly because of falling average incomes and the rapid rise in HA rents.