

# **Impact on public finances of unfreezing Local Housing Allowance rates in London**

September 2023

# Summary (1/2)

## Background

Local Housing Allowance (LHA) rates serve as the upper limits for housing support in private rented properties, applicable to claimants of Universal Credit and Housing Benefit. These rates are determined by the Department for Work and Pensions drawing on data provided by the Valuation Office Agency (VOA). LHA rates are set at the 30th percentile for market rents compiled by VOA but have remained stagnant since 2020/21. In other words, the LHA rates today are determined by the 30th percentile of the 2020/21 market rents.

## Objective

Alma Economics was commissioned by London Councils to estimate the impact of ending the freeze in LHA rates on public sector finances, specifically, the additional public expenditure required to fulfil the higher LHA rates and financial savings from reduced levels of homelessness. Estimates are calculated for London only<sup>1</sup> during the six-year period from 2023/24 to 2030/31, assuming that LHA rates are updated each year at the 30th percentile of market rents.

## Findings

The average annual cost of the policy change is estimated between £630 and £857 million per year whereas the average annual savings are estimated between £80 and £107 million per year. The savings are quite modest, representing only 12.5% of the costs. The costs and savings estimates above relate solely to the impact on public finances and do not take into account the benefits to households. If the wider social benefits were taken into account alongside the public sector cost savings, we anticipate that this would far outweigh the cost (see next slide).

1. Indicative estimates of the costs for Great Britain are also provided in the Appendix

## Summary (2/2)

There are additional social welfare benefits associated with the LHA rate unfreeze that have not been quantified. These include welfare gains from better accommodation conditions, and reduced levels of poverty and homelessness. With regards to the latter, it is estimated that an additional 16,500 to 22,000 London households will become homeless over the next six years if the rates freeze continues.<sup>1</sup>

A [2019 Alma Economics study](#) estimated the social benefits of a similar policy change for Great Britain as a whole. While it was not possible to fully replicate this analysis for London, a high-level estimate based on the 2019 study implies that the social benefit for London could be in the region of £1.2 billion.<sup>2</sup> Taken together with the estimated savings to the public purse, the total benefit of ending the freeze is likely to be greater than the estimated cost.

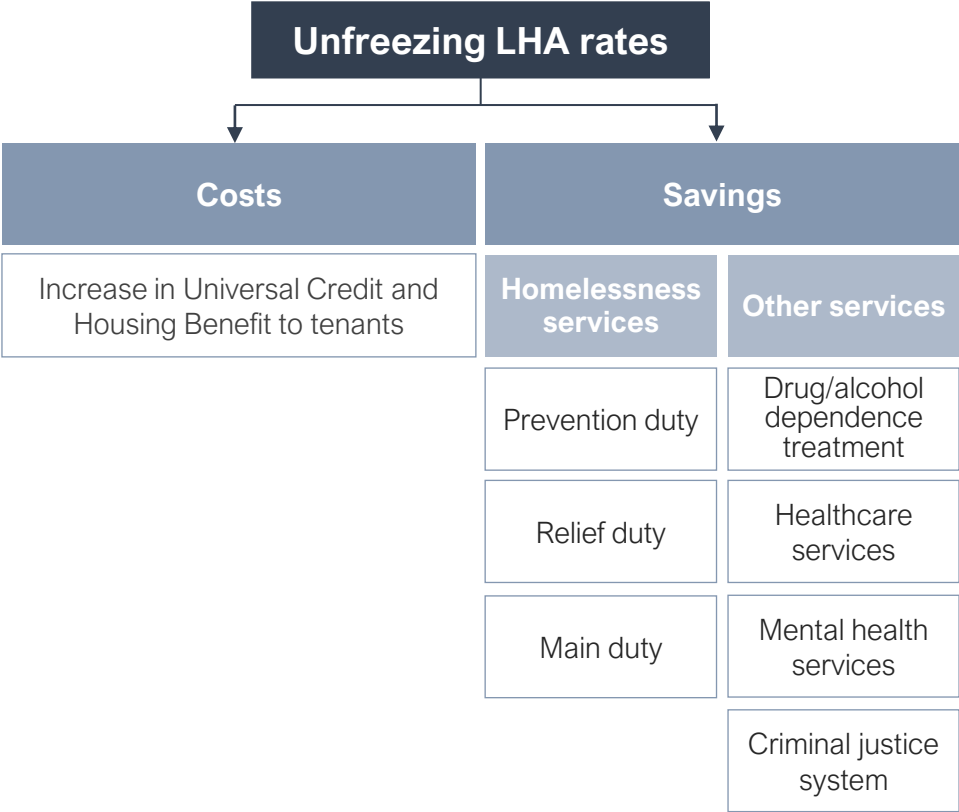
1. In the report, homelessness is the statutory homelessness which refers to households that approach their local authorities for assistance when they find themselves at risk of being homeless.
2. The social benefits capture the welfare created from income redistribution and reflects, by and large, the welfare gains from poverty and homelessness reduction.

# Methodology

Unfreezing LHA rates has two main implications for public sector finances:

- **Costs:** Unfreezing LHA rates will increase the Universal Credit and Housing Benefit awarded to tenants in the private rented sector and, therefore, public expenditure on housing support.
- **Savings:** Unfreezing LHA rates will reduce or eliminate shortfalls between private rents and housing support, increasing disposable income for most households claiming LHA. This increase in income reduces the number of households that would have ended up in homelessness in a “do nothing” scenario. The reduction in homelessness as a result of increased housing support will lead to:
  - Reduced expenses on homelessness services by local authorities (including prevention, relief and temporary accommodation duties).
  - Reduced spending on wider public services (including health care and mental health services).<sup>1</sup>

## Public sector costs and savings



1. For more details on the financial benefits associated with homelessness reduction, see the Appendix and [here](#).

# Cost estimates (London)

We used two scenarios for estimating the public sector costs:

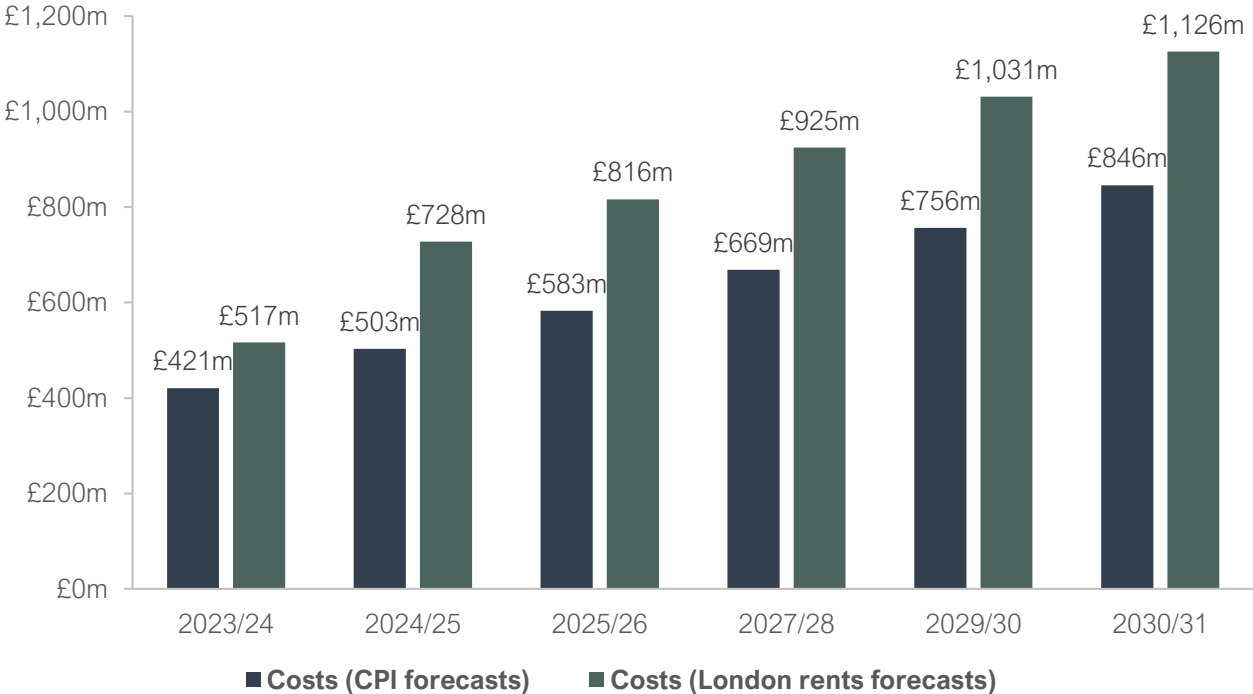
- LHA rates are uprated by the Consumer Price Index (CPI) inflation forecast each year for the following six years.<sup>1</sup>
- LHA rates are uprated by forecasted annual growth in London rents for the following six years.<sup>2</sup>

In the financial year 2023/24, the estimated cost of ending the LHA freeze ranges between £421 and £517 million. The annual cost is estimated to increase over time reflecting the expected increase in market rents. On average, the additional annual cost of the LHA rate unfreeze over the next six years is estimated between £630 and £857 million.

The difference in the cost estimates between the two scenarios reflects differences in the underlying assumptions. The average CPI inflation rate forecasted over the six-year period is 2.2%, which is significantly lower than the 3.2% forecasted average growth in London rents.

1. Data source: Bank of England  
2. Data source: Savills

Annual cost of LHA rate unfreeze



**Notes:** The costs refer to the additional public expenditure required to align the LHA rate to the 30th percentile; the alignment is assumed to be dynamic (for each year, the LHA rate equals the rent implied by the 30th percentile of the London rent distribution). Only London costs are within the scope of the analysis; indicative estimates of the total costs of LHA re-alignment across Great Britain are included in the Appendix.

# Savings estimates (London)

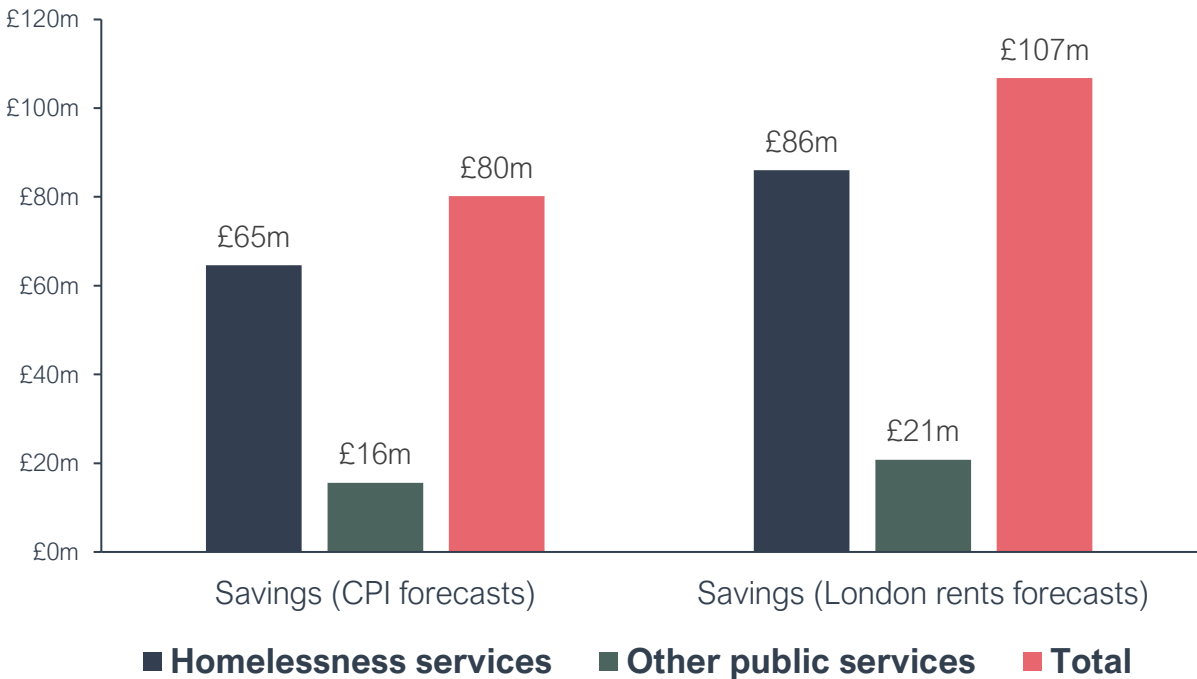
We estimate that unfreezing LHA rates will prevent between 16,500 and 22,000 London households from becoming homeless during the 2023/24 – 2030/31 period.<sup>1</sup>

The financial savings from reduced levels of homelessness are estimated between £80 and £107 million per year, on average, for the six-year period.

- Most of the savings are due to reduced expenses on homelessness services by local authorities.
- The remaining savings are due to reduced spending on wider public sector services.
- Note that these estimates do not include wider welfare gains from improved accommodation conditions, and reduction in poverty and homelessness.

1. These estimates are the additional number of households that will become homeless due to the rate freeze, keeping everything else constant. Future homelessness levels could increase or decrease due to many other factors; however, these factors are not analysed in these study.

Savings due to LHA rate unfreeze (per annum)



**Notes:** Savings reflect the average annual decrease in public sector expenses from reduced levels of homelessness in London over the six-year period (2023/24 – 2030/31). Homelessness services include services related to prevention, relief and main duties. Other services include health care and mental health services as well as contacts with the criminal justice system.

# Appendix

## Methodology: Savings associated with homelessness

The public sector savings from reduced homelessness are set out below. Additional details on inputs and assumptions are provided in the next two slides.

1. The reduction in households' net income from the rate freeze is translated into an increase in homelessness. The increase in homelessness is estimated based on the income – homelessness elasticity obtained from Bramley et al. (2010). This elasticity suggests that a 1% decrease in household net income leads to 0.48% increase in homelessness.<sup>1</sup>
2. Each household that becomes homeless utilises one or more of the prevention, relief and main duty related services. The share of households using these services is estimated using historical data from the Department for Levelling Up, Housing & Communities.
3. The increase in the utilisation of homelessness services is monetised using estimates on average unit costs.
4. Previous research<sup>2</sup> suggests that households that become homeless are more likely to use drug and alcohol treatment services, health care and mental health services, and interact with the criminal justice system. These wider public service cost savings associated with homelessness reduction are estimated assuming an average cost per household avoiding homelessness. The average cost is informed by data provided by Crisis.

1. Unfreezing LHA rates will reduce or eliminate shortfalls between private rents and housing support, increasing disposable income for most households claiming LHA. This increase in income reduces the number of households that would have ended up in homelessness in a “do nothing” scenario and widens access to Private Rented Sector properties to households currently in temporary accommodation, enabling their homelessness to be relieved.

2. PWC (2018). Assessing the costs and benefits from Crisis' plan to end homelessness. Available [here](#).



# Inputs & assumptions

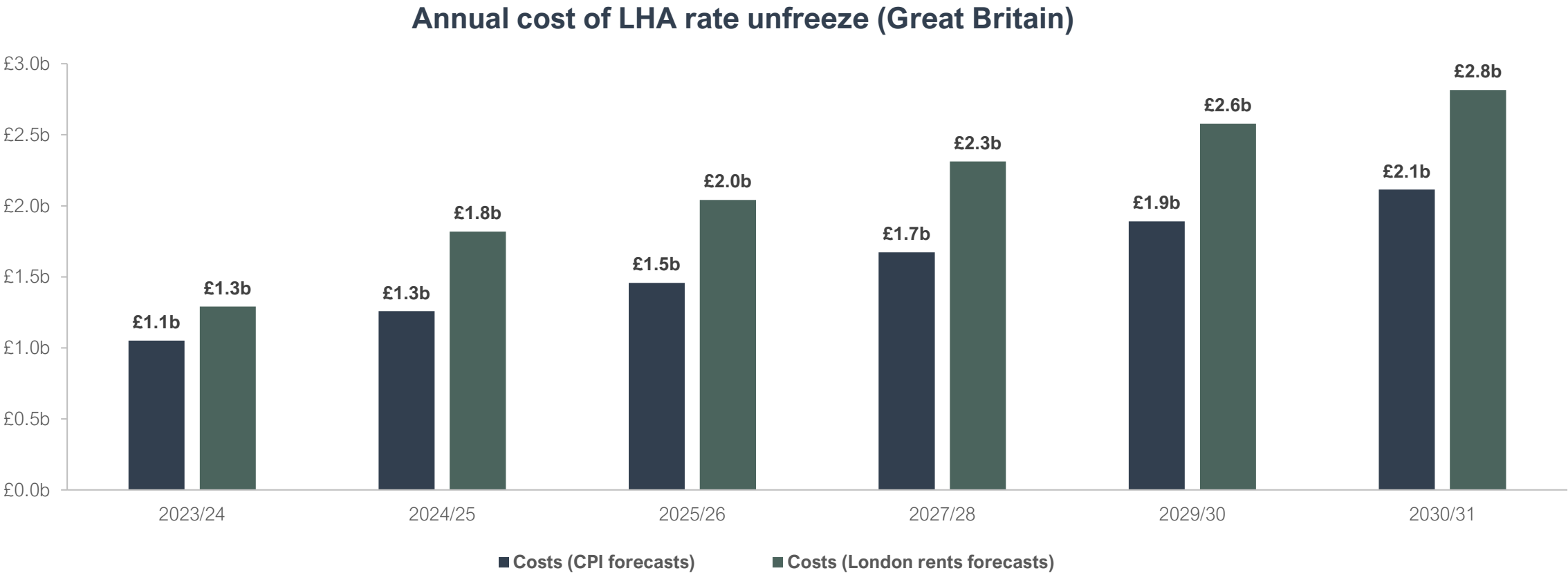
Cost/savings	Input / Assumption	Description	Value	Source
<b>Cost estimation</b>	Baseline LHA expenditure	The 2021/22 total Great Britain expenditure on LHA	£9.8 billion	Department for Work & Pensions, Spring Budget 2023, Expenditure and Caseload forecasts.
<b>Cost estimation</b>	Share of London LHA expenditure	The 2021/22 share of London LHA expenditure relative to Great Britain total LHA expenditure	40%	Department for Work & Pensions Stat Xplore; Alma assumption.
<b>Cost estimation</b>	LHA rates	Historical 30th percentile LHA rates	Various	<a href="https://www.gov.uk/government/publications/local-housing-allowance-lha-rates-applicable-from-april-2023-to-march-2024">https://www.gov.uk/government/publications/local-housing-allowance-lha-rates-applicable-from-april-2023-to-march-2024</a>
<b>Cost estimation</b>	Property type distribution	Percentage of shared accommodation, 1-bed, 2-bed, 3-bed and 4-bed properties within the scope of LHA	Various	Understanding Society; Alma calculations.
<b>Cost estimation</b>	Benefit cap	Percentage of households that will not benefit from the LHA re-alignment due to the benefit cap	5.5%	Department for Work & Pensions, Benefit cap: number of households capped to February 2023, Official Statistics; Alma assumption.
<b>Savings estimation</b>	Income - homelessness elasticity	Elasticity used to estimate the impact of net income increase due to LHA re-alignment on homelessness reduction.	0.48	Bramley, G., Pawson, H., White, M., Watkins, D., Pleace, N. (2010). Estimating housing needs. Department for Communities and Local Government.
<b>Savings estimation</b>	Prevention duty cost	Average cost per household that is eligible for prevention duty.	£500	Assumption used in the <a href="#">Local Housing Allowance report</a> adjusted for inflation and London uplift.

# Inputs & assumptions

Cost/savings	Input / Assumption	Description	Value	Source
Savings estimation	Relief duty cost	Average cost per household that is eligible for relief duty.	£10,863	Formula using the percentage of households that get private accommodation, a monthly rent estimate together with an average rent inflation, and average duration of the relief duty. The monthly rent is the median of the London rent taken from the ONS; the average duration is six months.
Savings estimation	Main duty cost	Average cost per household that is eligible for temporary accommodation duty.	£115,560	Formula using the percentage of households that get private accommodation, a monthly rent estimate together with an average rent inflation, and average duration of the main duty. The monthly rent is the average of the London rent taken from the ONS. This assumption is validated by data provided by the IBBA report (2022/23Q4) considering the recent increase in nightly shared accommodation placements and costs. The average length of stay is assumed to be five years and is informed by data provided by a sample of London boroughs.
Savings estimation	Percentage of households eligible for homelessness support	Percentage of households eligible for prevention duty, relief duty, and main duty.	45% (prevention); 63% (relief); 14% (TA)	Statutory Homelessness Annual Report 2021-22, England. Department for Levelling Up, Housing & Communities.
Savings estimation	Other services cost - Households	Additional costs per household that becomes homeless (e.g., health care and mental health care services costs).	£5,186	Assumption used in the <a href="#">Local Housing Allowance report</a> adjusted for inflation and London uplift.
Savings estimation	Other services cost - Children	Additional costs per children that becomes homeless (e.g., health care and mental health care services costs).	£976	Assumption used in the <a href="#">Local Housing Allowance report</a> adjusted for inflation and London uplift.
Savings estimation	Average number of children per household	Average number of children in a household that becomes homeless	0.49	<a href="#">Shelter</a>

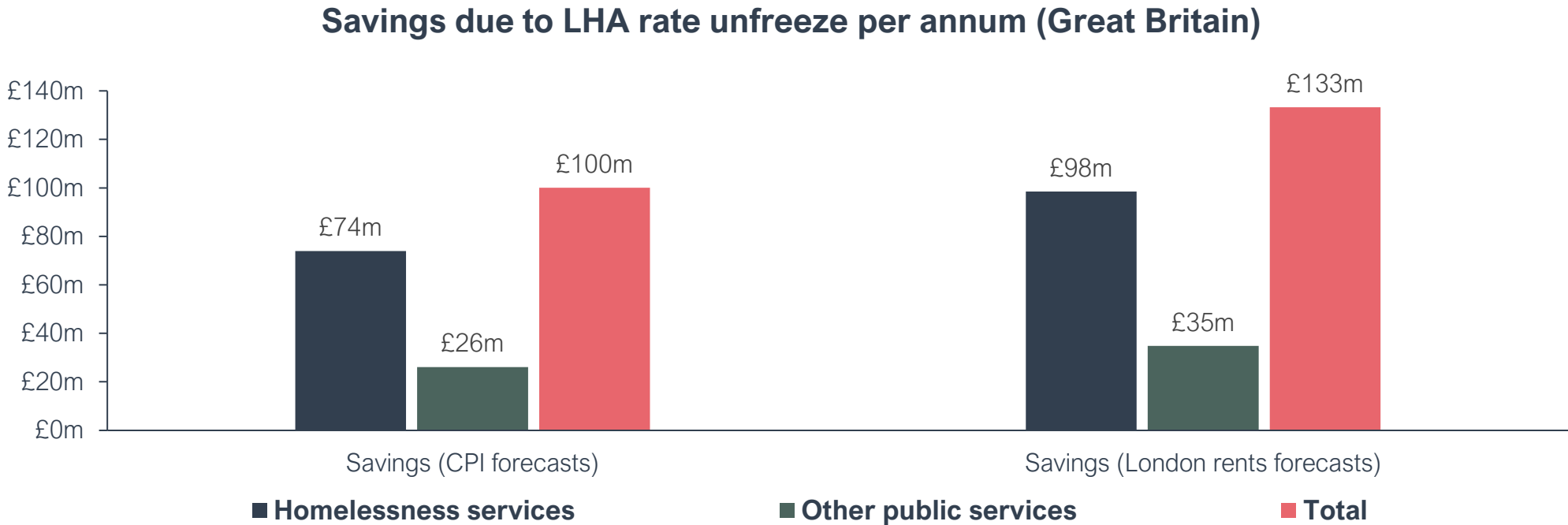
# Cost estimates (Great Britain)

The estimates of the Great Britain costs are based on the same assumptions used to derive the London estimates and should be interpreted with care. The aim is to provide a **broad estimate** of the total Great Britain costs of the LHA unfreeze.



# Savings estimates (Great Britain)

The estimates of the Great Britain savings are based on the same assumptions used to derive the London estimates and should be interpreted with care.<sup>1</sup> The aim is to provide a **broad estimate** of the total Great Britain savings of the LHA unfreeze. It is estimated that the ending of the LHA rate freeze will prevent between 28,000 and 37,000 households from becoming homeless during the period between 2023/24 and 2030/31. The associated public sector cost savings are estimated between £100 and 133 million per year.



1. The only Great Britain specific assumption is the average cost of temporary accommodation which is based on the average monthly rent in England provided by the ONS.



RESEARCH TECHNOLOGY COMMUNICATION

[www.almaeconomics.com](http://www.almaeconomics.com)