Cost of Living Bill – Economic Background

November 2022

Scottish Government
Riaghaltas na h-Alba

Cost of Living Bill – Economic Background

1. Energy prices

Despite the decision of the UK Government to introduce the Energy Price Guarantee from 1 October 2022, which will cap the typical household energy bill at £2,500 for the next two years,[1] compared to the previously announced Ofgem price cap of £3,549, this represents a further increase from the £1,971 cap in April 2022, and an even larger increase from the £1,277 cap in October 2021. Even taking into account the £400 Energy Bills Support Scheme payment, which is available in Winter 2022/23 (although not beyond), the increases in energy bills will be substantial, as set out in Table 1, which also sets out the changes relative to a cap of £2,500 since this will continue to apply in subsequent years.

Table 1. Change in cap on typical household energy bill

% change from	For cap of £2,500	For cap of £2,100 (i.e. including £400 support payment)
Apr-22	27%	7%
Oct-21	96%	64%
Oct-20	140%	102%

The following mitigations are being provided:

- A £400 Energy Bills Support Scheme payment for all energy consumers to be paid over the period October 2022 to March 2023, discussed above.
- A £650 Cost of Living payment for those on means-tested benefits
- A £300 Pensioner Cost of Living Payment for those pensioner households who receive the Winter Fuel Payment
- A £150 Disability Cost of Living Payment
- A £150 Council Tax rebate for households in council tax bands A-D or that receive council tax reduction

However, these mitigations will not be sufficient to offset the impact of higher energy costs. The change in the energy cap from £1,277 in October 2021 to £2,500 in October 2022 equates to an increase of £1,223, which for the 2.5 million households in Scotland implies an increase in total energy spending in the region of £3 billion. The mitigations set out above are estimated to be worth in the region of £1 billion in Scotland, leaving a substantial gap.

The above impacts are based on typical household consumption levels, which in many cases fall short of what is regarded as an appropriate level of heating as set out in the Scottish Government's Fuel Poverty definition. Table 2 illustrates the

[1] Government announces Energy Price Guarantee for families and businesses while urgently taking action to reform broken energy market - GOV.UK (www.gov.uk)

impact of these energy price changes, net of the mitigations set out above, on estimated fuel poverty rates.[2]

Table 2. Estimated fuel poverty rates based on energy price cap and taking into account mitigations in 2022-23

	Fuel poverty rate			Change in fuel poverty rate (% points)	
	2019	Oct 2021	Oct 2022	Oct 2022 on 2019	Oct 2022 on Oct 2021
Owned outright	21%	22%	28%	7%	6%
Mortgaged	12%	13%	19%	7%	6%
LA	36%	39%	52%	16%	13%
HA	39%	45%	57%	18%	12%
Private rented	36%	37%	48%	12%	11%
Scotland	**25%**	**27%**	**35%**	**10%**	**8%**

Source: Scottish Government analysis. See footnote 2 for more detail.

Note: Fuel poverty rates are normally calculated over the course of year, so the estimated rates for October 2021 and October 2022 show what fuel poverty rate would be if prices remained at these levels over the period of year.

Table 2 shows that there are significant increases in the fuel poverty rates, and that these increases are particular high in the private and social rented sectors, with around half of households in these sectors being in fuel poverty despite the Energy Price Guarantee. Table 3 shows a similar pattern for extreme fuel poverty rates.

[2] It should be noted that this modelling is based on the 2019 Scottish House Condition Survey data, since this is that latest available dataset which has all the variables required for fuel poverty modelling. The modelling uprates energy prices by the percentage increase in the price cap for each time period, and for the October 2022 estimate allocates the mitigation payments to households in the dataset based on eligibility for the different benefits. Every household benefits from the £400 Energy Bills Support Scheme payment. The National Statistics on fuel poverty rates for 2022, which will be published in late 2023/early 2024, could differ from these depending on changes other than fuel prices and benefit eligibility and also because they will use average energy prices across the year.

Table 3. Estimated extreme fuel poverty rates based on energy price cap and taking into account mitigations in 2022-23

	Fuel poverty rate			Change in fuel poverty rate (% points)	
	2019	Oct 2021	Oct 2022	Oct 2022 vs. 2019	Oct 2022 vs. Oct 2021
Owned outright	13%	15%	24%	11%	9%
Mortgaged	5%	6%	12%	7%	6%
LA	15%	18%	31%	16%	13%
HA	14%	18%	32%	18%	14%
Private rented	22%	24%	35%	13%	11%
Scotland	**12%**	**14%**	**24%**	**12%**	**10%**

Source: Scottish Government analysis. See footnote 2 for more detail.

Households on pre-payment meters will be particularly affected by the increase in energy prices, as around 80% of annual household gas consumption falls within the winter months,[3] and these households are unable to spread the costs over a longer period. Table 4 shows that the share of households on pre-payment meters is much higher in the private rented sector (22%) and social rented sector (43%) than in the owner occupier sector (6%).

Table 4. Presence of pre-payment meters by tenure

Prepayment meter present?	Owner Occupier		Private Rented		Social Sector		**Scotland**	
	Count	% of tenure	Count	% of tenure	Count	% of tenure	**Count**	**% of tenure**
No	1,470,000	94%	240,000	78%	360,000	57%	**2,070,000**	**83%**
Yes	80,000	6%	70,000	22%	270,000	43%	**430,000**	**17%**

Source: Scottish Government analysis of 2019 Scottish House Condition Survey data.

Table 5 shows that within each tenure, households on pre-payment meters are more likely to be in fuel poverty than those paying by other means, with around three-fifths of households who live in the rented sectors and who have a pre-payment meter being in fuel poverty.

[3] Pullinger, M.; Few, J.; McKenna, E.; Elam, S.; Webborn, E.; Oreszczyn, T. (2022): Smart Energy Research Lab: Energy use in GB domestic buildings 2021 (volume 1) - Data Tables (in Excel). University College London. Dataset. https://doi.org/10.5522/04/20039816.v1

Table 5. Estimated fuel poverty in October 2022 by tenure and pre-payment meter

	Prepayment meter present?	Total Households in fuel poverty	Fuel Poverty Rate
Owner Occupier	No	350,000	24%
	Yes	30,000	30%
Private Rented	No	110,000	44%
	Yes	40,000	60%
Social Sector	No	190,000	52%
	Yes	160,000	57%
Scotland	**No**	**640,000**	**31%**
	Yes	**220,000**	**52%**
	All	**860,000**	**35%**

Source: Scottish Government analysis. See footnote 2 for more detail.

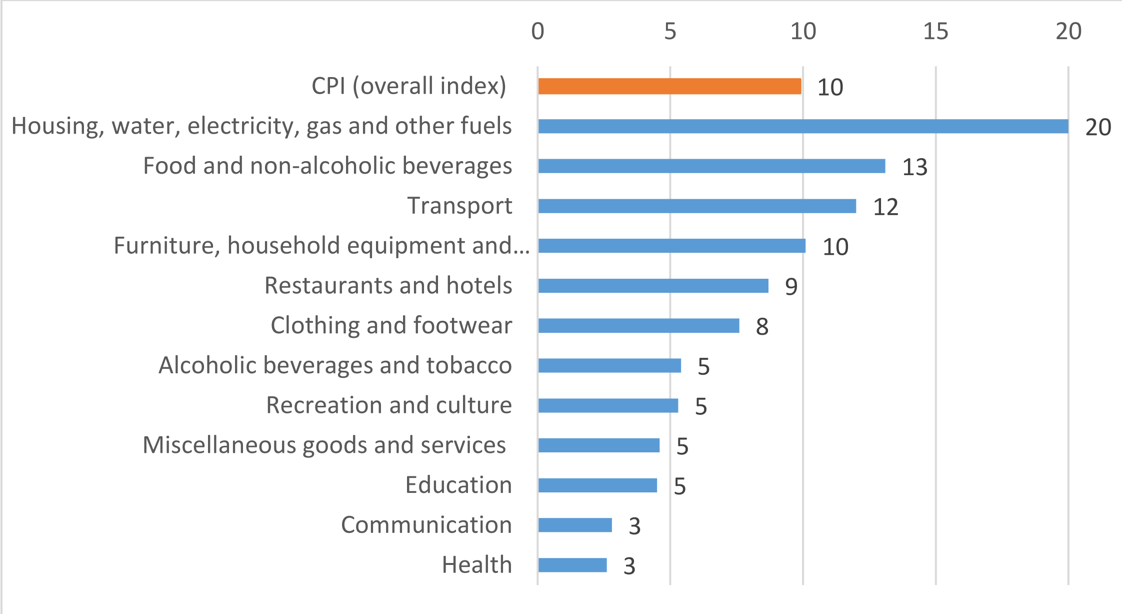
2. Wider inflationary pressures

As set out above, households are facing very large increases in fuel bills despite the mitigation payments, and will therefore need to use more of their household income to pay their energy bills. However, this impact is being felt at the same time as a large increase in other types of inflation. CPI inflation, which averaged 4% in 2021-22, has accelerated to 10% in August 2022. Although the Energy Price Guarantee has caused commentators to revise down their estimates for a peak of measured inflation of well over 10% in the short term, they still expect an extended period of high inflation, with, for example, the Resolution Foundation forecasting that inflation will remain around double digit levels throughout Winter 2022/23.[4]

As Figure 1 shows, although the increase in energy prices is a particularly important contributor to high levels of inflation, there are inflationary pressures across all goods and services, with very high levels of inflation affecting other types of necessities, such as food (13%), transport (12%) and clothing (8%). As a result, even excluding energy, CPI inflation was 7% in August 2022.

[4] Figure 12 on P22 of Resolution Foundation (2022), A blank cheque.

Figure 1. August CPI annual inflation, by category



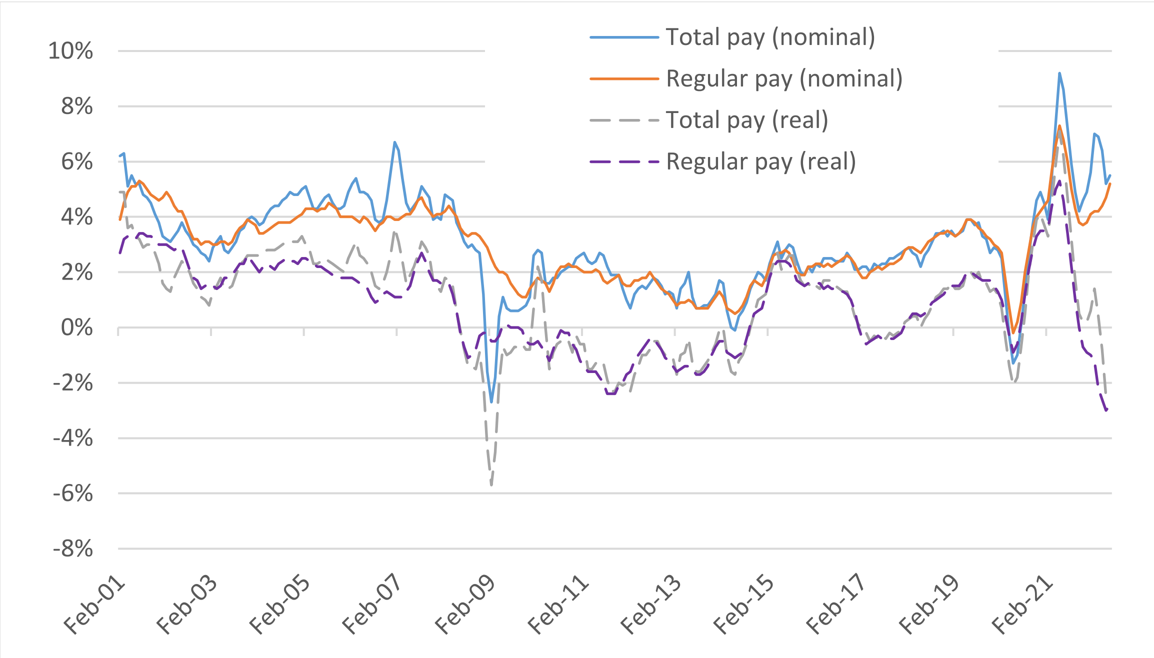
Source: ONS, Consumer price inflation, August 2022.

3. Trends in earnings

Increases in wages and benefits are not keeping pace with the higher inflation rate, meaning that in real terms households are worse off. The latest Scottish Fiscal Commission forecast (May 2022) was that real average earnings would fall by 2.7% in Scotland over the course of 2022-23.[5] More up-to-date data shows the extent of the squeeze on real earnings. The most recent data on average weekly earnings published by the ONS (May-July 2022) shows that across Great Britain, while total pay (5.5%) and regular pay (5.2%) were rising in nominal terms, these increases are insufficient to offset the increase in inflation, such that in real terms total pay fell by 2.6% and regular pay by 2.8% (Figure 2).

[5] Figure 3.2 on P39 of Scottish Fiscal Commission (2022), Scotland's Economic and Fiscal Forecasts – May 2022.

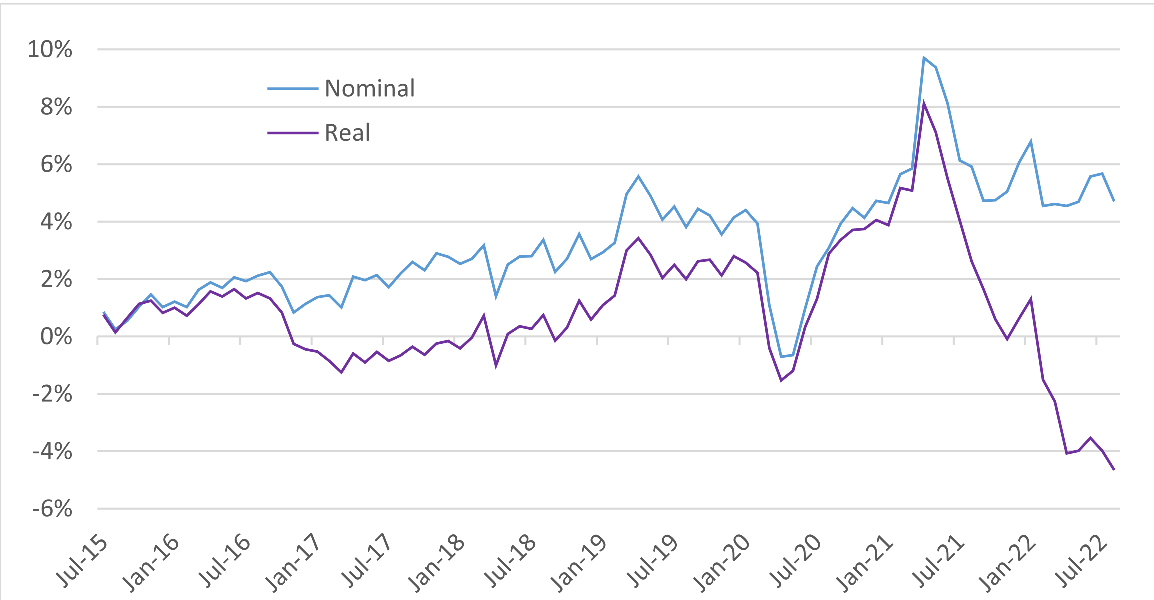
Figure 2. Average weekly earnings annual growth rates in Great Britain, seasonally adjusted, January to March 2001 to May to July 2022



Source: ONS, [Average weekly earnings in Great Britain]

Figure 3, which uses pay data for Scotland taken from HMRC PAYE records, tells a similar story

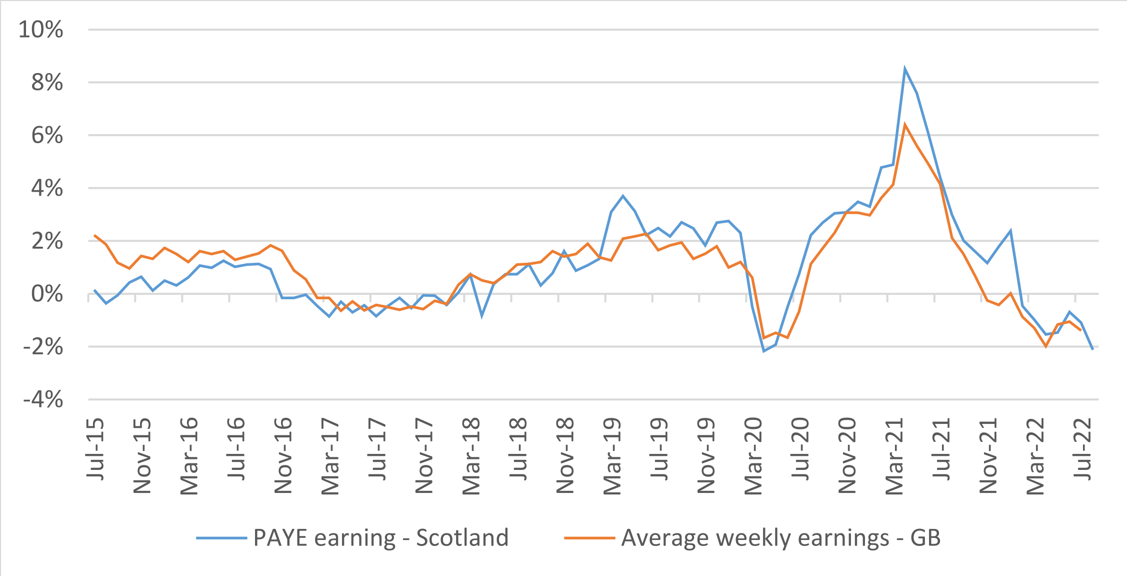
Figure 3. Growth in median pay in Scotland (from PAYE Real Time Information)



Sources: ONS, Earnings and employment from Pay As You Earn Real Time Information, seasonally adjusted. Real pay calculated using all-items CPI from ONS, Consumer price inflation, August 2022.

The fact that the squeeze on household budgets is not just related to energy costs is illustrated by Figure 4 which deflates average weekly earnings for Great Britain and median pay in Scotland from PAYE records by the CPI excluding energy costs. This shows that both measures of earnings have moved into negative territory in recent months. As a result, households will struggle to cover non-energy related inflation, even before attempting to pay for energy bills, meaning they will either need to reduce savings or cut back on consumption, particularly poorer households who have low or no savings.

Figure 4 Real earnings growth, deflated by the CPI excluding energy costs



Sources: ONS, Earnings and employment from Pay As You Earn Real Time Information, seasonally adjusted and Average weekly earnings in Great Britain. The regular pay timeseries is used for average weekly earnings as it is less volatile than total pay, which includes bonus payments, but the trend for total pay is similar. Earnings data is deflated by the CPI excluding energy (time series DKC5 from ONS, Consumer price inflation time series).

4. Trends in benefits

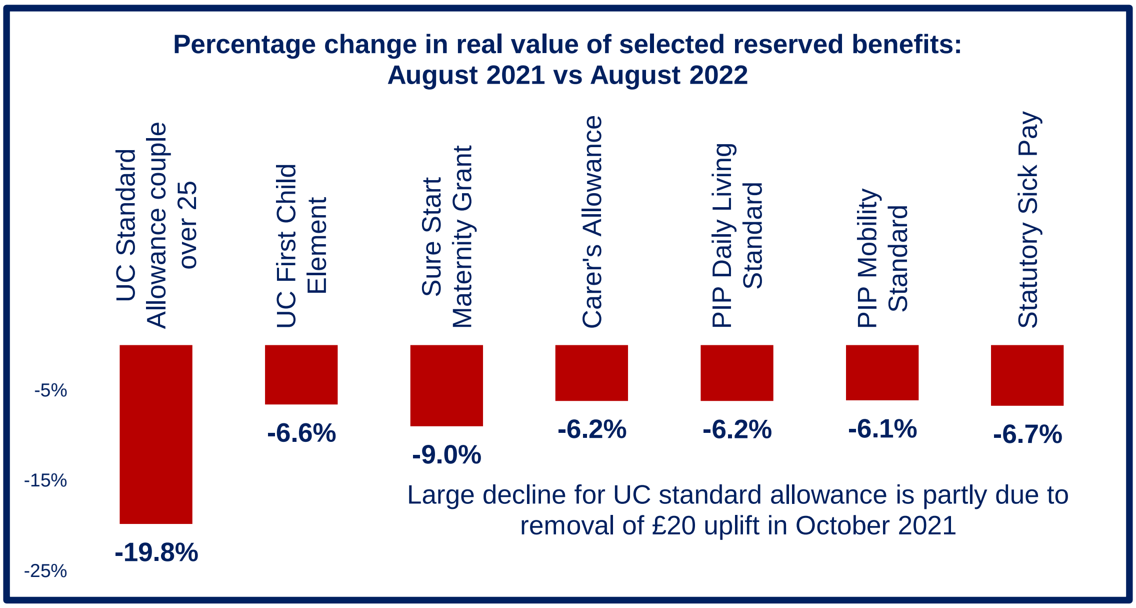
For those households who depend partly or fully on benefit income, the situation is even more challenging. The UK Government uprated allowances on reserved benefits in April 2022 using the September 2021 inflation rate, which at 3.1% is significantly below the 10% inflation rate currently being experienced. Table 6 and Figure 5 show the change in the real value of the maximum value of universal credit awards. These show substantial reductions, both due to the level of uprating, and also due to the decision to reverse the uplift to Universal Credit that was introduced during the initial stages of the Covid-19 pandemic.

Table 6. Change in real value of UC award by family type vs August 2021

Family type	**% change**	**Loss in real value in month**
Single parent < 25, 2 children	-15.7%	-£136
Couple < 25, 1 child	-16.9%	-£130
Single > 25, no children	-25.9%	-£107
Couple > 25, 3 children	-13.6%	-£151

Sources: Scottish Government analysis of Universal Credit rates, deflated using the ONS Consumer price inflation.

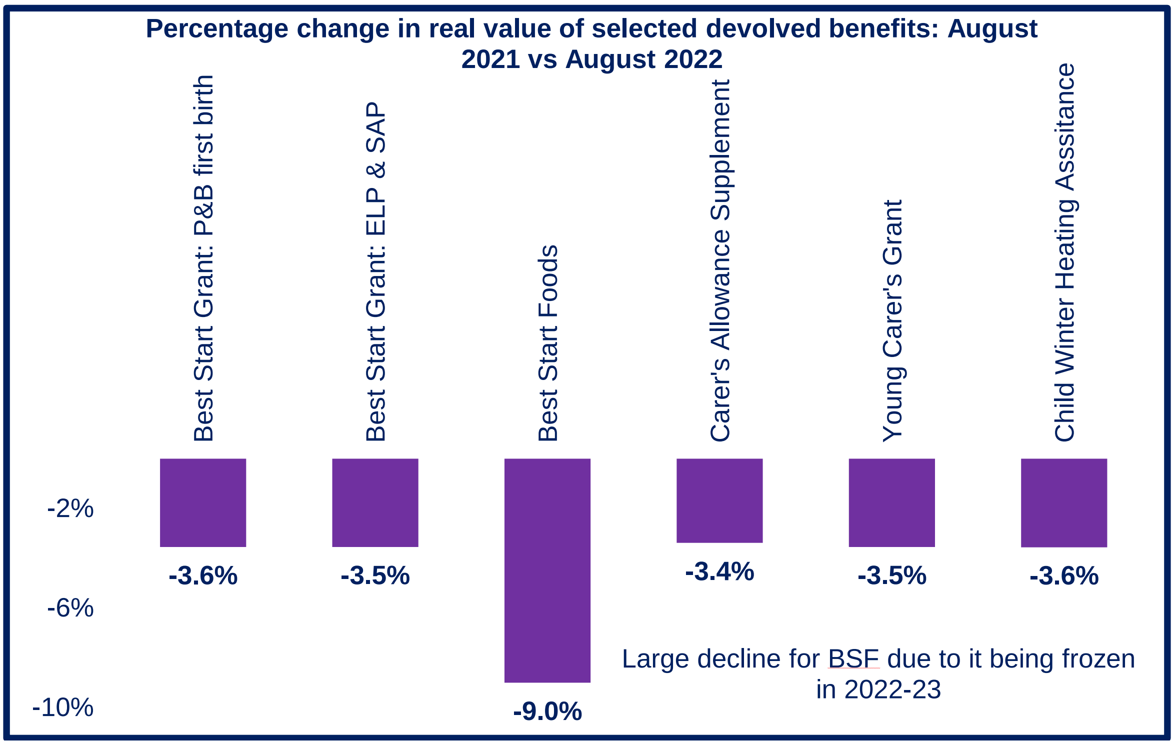
Figure 5.



Source: Internal SG analysis.

The Scottish Government uprated most devolved benefits by 6% in contrast to the UK Government's 3.1%, but despite this additional protection, the spike in inflation means that the value of these benefits has also fallen in real terms, albeit by less than reserved benefits (Figure 6).

Figure 6.



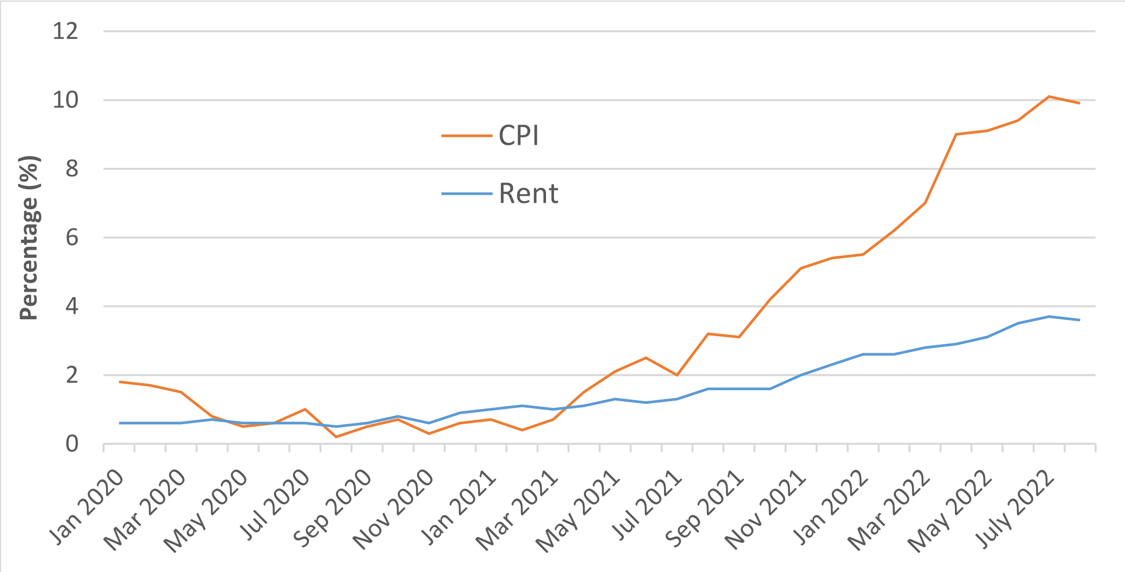
Source: Internal SG analysis.

With respect to housing benefit, or the housing element of universal credit, it should also be noted that Local Housing Allowance rates, which set the maximum amount of rent that can be covered by benefit payments, have been frozen by the UK Government for two years, after having been reset to the 30th percentile during the initial stages of the Covid-19 pandemic.

5. Trends in rents

Figures from the ONS Private Rental Index show that the annual increase in private rents across all tenants in Scotland has been accelerating over recent months. The increase of 3.7% in July 2022 was the highest since the series started in 2012, and the index remained at an elevated level of 3.6% in August 2022.

Figure 7. Annual increase in private rents in Scotland (ONS Private Rental Index, Experimental Statistics) compared with UK CPI inflation



Sources: ONS Index of Private Housing Rental Prices and Consumer price inflation.

Note that the ONS figures are experimental statistics incorporating an assumption relating to average tenancy length to account for rents to sitting tenants, and therefore will differ from separate recent lettings-agency figures that cover advertised rents only. The ONS series also only reports on national level increases, and beneath this increases in rents in some areas of the country are likely to vary.

Therefore, looking at latest data from letting agents (noting that they will not have compete market coverage) for the latest quarter Apr-Jun 2022 compared with Apr-Jun 2021, Citylets have reported that advertised rents have increased by 15.1% in Edinburgh, 13.0% in Glasgow, and 4.4% in Aberdeen.[6] Rightmove have reported that advertised rents in Scotland have increased by 12.5% over the same time period.[7]

With respect to the issue of how often rents are increased, a variety of anecdotal and survey evidence suggests that a significant share of sitting tenants do not experience a rent increase each year. A survey of tenants undertaken for the Nationwide RentBetter Project found that over half of tenants responding to the survey had not

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6 Citylets Quarterly Reports

7 Rightmove Rental Price Tracker

experienced a rent increase during their current tenancy.[8] This is due to a combination of high levels of turnover in the private rented sector (Scottish Household Survey data shows that around a third of tenants have been in their property for less than a year)[9] and landlord rent setting approaches. A survey of landlords and letting agents undertaken for the RentBetter project reported that of those responding to the survey, around half reported never increasing rents or only on change of tenancy.[10] Of the remainder, only around a third reported that they increased rents each year, and for landlords who increase rents less frequently than each year, only a portion of their tenants will experience a rent increase in any given year.

Taken together, the evidence suggests that of those tenants who have been in their property for at least a year, significantly less than half would expect to have a rent increase during the course of a year. Assuming that the starting dates of tenancies are approximately equally distributed over the course of a year, this would suggest that significantly less than a quarter of sitting tenants who have been in their property for at least a year would experience a rent increase over a 6-month period.

Data from the Scottish Household Survey (Figure 8) which shows that average rents to tenants who have been in their property for more than a year are consistently below average rents for those who have been in their property for less than a year is consistent with this analysis.

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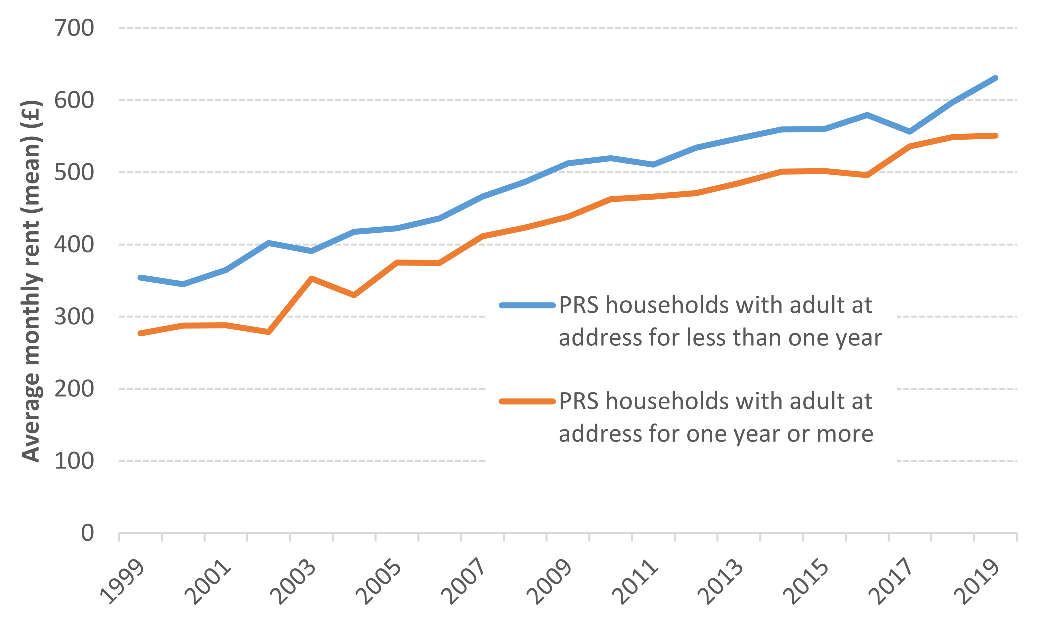
[8] 59% of tenants reported not having experienced an increase, and this increases to 63% if those not answering this question are excluded.

[9] In 2019, 35% of survey respondents living in the private rented sector had been at their current address for less than one year (Table 3.8 of Scottish House Condition Survey 2019 annual report), and in 2020 the corresponding figure was 31% (Table 1_26 of Scottish Household Survey 2020 Results Housing Tables). Note that the results in 2020 could have been affected by the change in survey methodology due to the impact of the Covid-19 pandemic.

[10] Around 17% reported never increasing rents and around 32% reported increasing rents on when the tenancy changes. See Section 3.3 of RentBetter (2020), Wave 1 Landlord and Letting Agent Survey Findings.

Figure 8. Average 2-bedroom private rented sector rents by length of tenure



Source: Scottish Government analysis of Scottish Household Survey data

It should be noted that the RentBetter research also found that landlords were much more likely to raise rents regularly in Edinburgh, where rents have been rising faster than in Scotland as whole.[11] This suggests that while, when market rents are not growing too fast, landlords may prefer to wait to the end of what are often relatively short tenancies before they reset rents, since the gap between the rent paid by their sitting tenant and the market rent will not be too large, and they may be reluctant to disturb their relationship with their tenant,[12] landlords do adapt their behaviour when market rents are rising more significantly. This would suggest that the share of tenants who would experience a rent rise over the next six months in the absence of legislation may be higher than would usually be the case, given the acceleration in average Scottish rents reported by the ONS Private Rental Index.

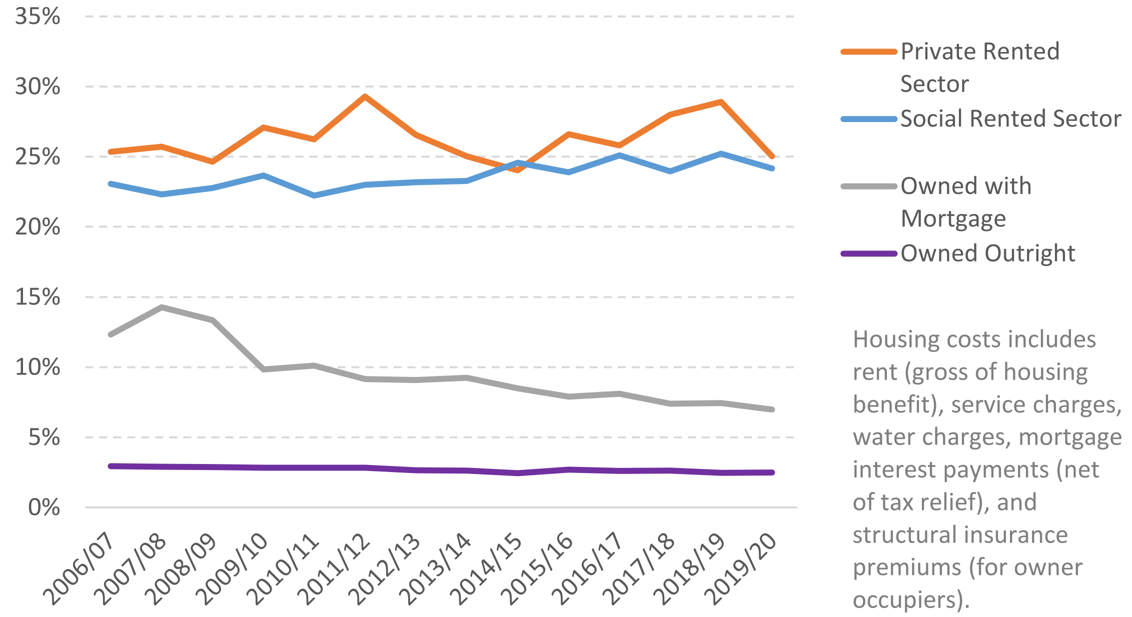
6. Level of vulnerability of households in rental sector

In general households living in the rental sectors have less flexibility than owner occupiers, because their housing costs, relative to their incomes, tend to be higher. This is illustrated by Figure 9, which shows that the housing cost to income ratio is higher on average in the rented sectors, and Figure 10 which shows that households towards the lower end of the Scottish income distribution who live in the rented sectors tend to spend a substantial portion of their income on housing costs.

[11] For example, 30% of respondents in Edinburgh reported increasing rents annual, compared with 15% of all survey respondents.

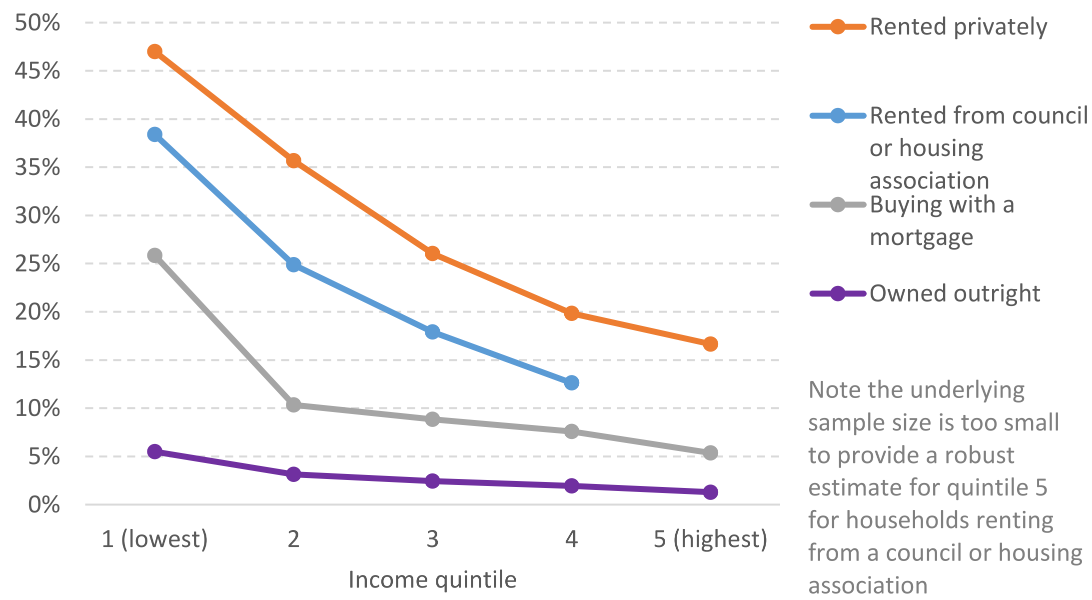
[12] If landlords are happy with their current tenant, they may be concerned that a rent increase might increase the probability that the tenant will move, with the associated void costs to the landlords and the possibility that the new tenant may not be as satisfactory in terms of rent payments and other aspects.

Figure 9. Average monthly housing costs as a proportion of net household income are higher for the rented sectors compared to owner occupiers



Source: Family Resources Survey, as reported on in [New Deal for Tenants draft strategy consultation.]

Figure 10. Ratio of housing costs to income, Scotland 2017-2020 - by tenure and income quintile



Source: Family Resources Survey, as reported on in [New Deal for Tenants draft strategy consultation.]

The rented sectors have a higher proportion of people who are in relative poverty (39% of social rented households and 34% of private rented households, compared to 7% of households buying with a mortgage and 14% of households who own outright), as well as children in relative poverty (47% of social rented households and

40% of private rented households, compared to 10% of households buying with a mortgage and 18% of households who own outright.)[13]

Households in the rented sector are also more likely to be financially vulnerable[14] (63% of social rented households and 40% of private rented households in Scotland categorised as financially vulnerable, compared with 24% of households buying with a mortgage and 9% of households owning outright), which reduces their ability to cope with rental increases and other inflationary shocks.

7. Evidence related to security of tenure and wellbeing

Findings from evidence reviews and research studies undertaken in the UK (including Scotland) suggest that feelings of insecurity related to tenure have impacts on tenants' health and wellbeing.[15] Research notes that negative psychosocial effects of living in insecure and precarious (as well as unaffordable housing) impact on tenant wellbeing and mental health. These studies conclude that the negative impacts of housing insecurity are complex and affect tenants in several different ways, including by causing financial distress (including distress related to potential expenses related to moving); causing concerns over finding a new property; making it difficult for tenants to feel at home and connected to place when insecure; and by causing stress over the potential of being separated from local support networks; among other mechanisms.

While much of this research is qualitative and based on the lived experience of tenants (particularly those on a low income), a larger study that linked data from the UK Household Longitudinal Study to measurable health outcomes found that desire to remain in current home was one element that led to significantly increased levels of biomarkers associated with infection and stress.[16]

In their interviews with tenants, McKee et al[17] (2019) conclude that feelings of insecurity were commonly reported amongst those on low incomes, and it is reasonable to suppose low-income tenants are also most likely to be additionally impacted by the current cost of living crisis. Additionally, a 2018 report by the Joseph Rowntree Foundation on forced evictions in England and Wales concluded that "the experience of forced moves and evictions was extremely stressful for low-income households as they struggled to find alternative properties because they are often seen as undesirable by private landlords and are often unable to access social housing."[18]

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[13] The latest available data covers the period 2017 to 2020 and is sourced from Poverty and Income Inequality in Scotland Tables

[14] Financial vulnerability is defined as households with savings which would cover less than one month of income at the poverty line. Data covers the period 2018 to 2020 and is sourced from Scottish Government Statistical publication on Wealth in Scotland 2006-2020

[15] HW-in-PRS-Part-2-final.pdf (housingevidence.ac.uk) ; Health and wellbeing in the private rented sector Part 1 | Literature review : CaCHE (housingevidence.ac.uk) ; McKee-etal-HousingStudies-2020.pdf (stir.ac.uk) ; cache03192.pdf (thinkhouse.org.uk)

[16] Housing and health: new evidence using biomarker data | Journal of Epidemiology & Community Health (bmj.com)

[17] McKee-etal-HousingStudies-2020.pdf (stir.ac.uk)

[18] poverty-evictions-and-forced-moves-2018-jrf.pdf (yhphnetwork.co.uk) p4

Recent survey research carried out in 2021/2022 with predominantly low-income tenants in the PRS in Scotland undertaken by researchers on behalf of the Joseph Rowntree Foundation and the Scottish Government found that 78% of surveyed tenants identified "feeling secure in my property" as one of the most important things to them when it came to their rented housing.[19]

[19] NB this work is now published and available at Living in Scotland's private rented sector: A bespoke survey of renter's experiences : CaCHE (housingevidence.ac.uk)

This publication is available at **www.gov.scot**

Any enquiries regarding this publication should be sent to us at

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