JRF JOSEPH ROWNTREE FOUNDATION

INSPIRING SOCIAL CHANGE

LIVING STANDARDS, POVERTY AND INEQUALITY IN THE UK: 2017–18 TO 2021–22

Debates over living standards, poverty and inequality in the UK are often hampered by the fact that official data on household incomes are available only with a significant lag, with the latest statistics available covering 2015–16.

The authors attempt to fill this gap by estimating what has happened since 2015–16 to household incomes. They also estimate how they might evolve up to 2021–22 if current tax and benefit policy plans are kept to, and if the latest macroeconomic forecasts from the Office for Budget Responsibility (OBR) – for things such as earnings and employment – were correct. There is of course significant uncertainty around any macroeconomic forecasts, and hence around any projection of future trends in household incomes based on those forecasts. To the extent that future macroeconomic trends differ from the OBR's forecasts, these projections – particularly for median income and inequality, and to some extent poverty – will also differ. As well as projecting median income, inequality and poverty in the UK, the authors also provide projections at a regional level.

Key points

- Real median income is projected to grow by around 5.1% between 2015–16 and 2021–22 – slow by historical standards. However, this projection is highly sensitive to the path of real earnings, and might well turn out to be optimistic given that the OBR have indicated they are likely to revise down their forecast for future earnings growth.
- Inequality is projected to rise between 2015–16 and 2021–22, as working age benefits are cut and real earnings growth boosts the income of higher income households.
- At the UK level, absolute poverty – defined using a fixed real poverty line, and after deducting housing costs – is projected to remain roughly unchanged between 2015–16 and 2021–22. Absolute child poverty is projected to rise by 4.1 percentage points (ppts), primarily due to the impact of planned changes to working-age benefits.
- Absolute poverty is projected to fall in the South, the East, Yorkshire and Scotland, but rise in the North East, North West, Wales, Northern Ireland and the Midlands.
- Different trends in poverty are partly driven by share of income that low income families get from earnings. Those regions where low-income families are less reliant upon earnings (and therefore more reliant upon benefits) are projected to see a larger increase in absolute poverty.

The research

By Andrew Hood and Tom Waters, Institute for Fiscal Studies

NOVEMBER 2017

BACKGROUND

(All years from this point are financial, referred to by their first calendar year). Since 2007 median income has grown by 0.5% per year, considerably below the historical average of 2% per year. This was driven by the fall and limited recovery in real earnings. This period was also characterised by meagre productivity growth, with the latter no doubt being a key cause of the former.

Over the same period inequality fell, especially if measured before deducting housing costs. Between 2007 and 2015, real incomes at the 10th percentile grew by 7.7%, while incomes at the 90th fell. This is explained by the weakness in real earnings affecting high income households more than low-income ones, since earnings make up a larger share of their income.

With incomes among low-income households increasing, overall absolute poverty fell, driven by declines in child and pensioner poverty of 3.9 ppts and 3.5 ppts respectively.

Median income and inequality

Looking forward, the authors project real median income to increase, but only slowly. Between 2015 and 2021, real median income is projected to grow by just 5.1%, or 0.8% per year. This would leave median income about 19% below where it would have been had growth since 2007 continued in line with the long-run trend.

This projection is highly dependent upon the path of real earnings. In their latest forecast the OBR expected earnings to grow fairly slowly over the next few years. However, they have since indicated that even that forecast may have been too optimistic: should earnings turn out to be weaker than they previously expected, these projections for median income growth would be weaker too.

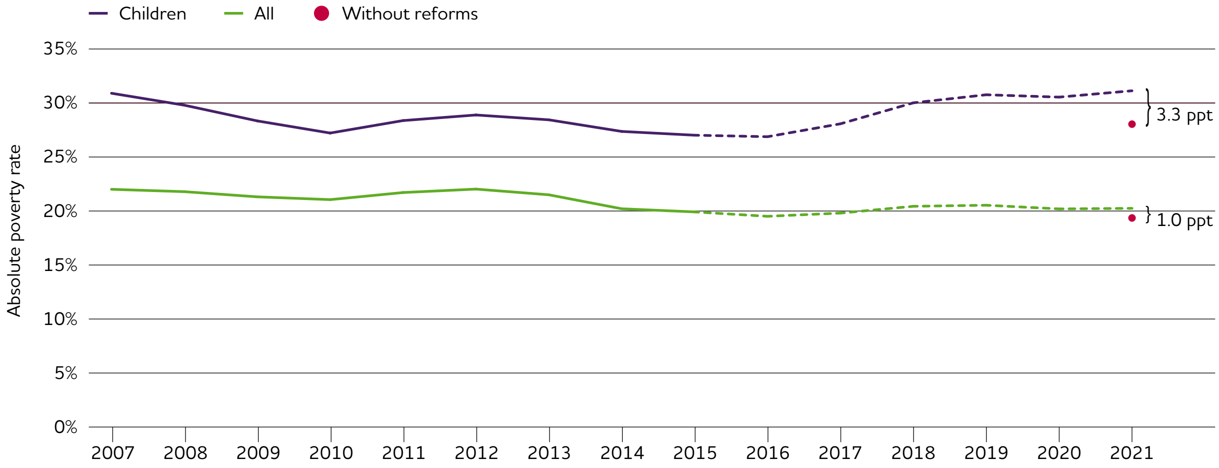
Inequality is projected to rise over the same period, reversing the falls seen since the recession. Two factors combine to explain this. First, the OBR expect real earnings to rise – albeit slowly – which increases inequality as earnings make up a larger share of incomes for high income households. Second, the government plans to cut working-age benefits in real terms over the period.

However, the path inequality will take is highly dependent upon the distribution of growth in workers' earnings, which is itself highly uncertain. In these projections the authors assume that all workers earning above the National Living Wage see an equal proportional rise in earnings. If instead, future earnings growth is concentrated among high or low income households, the picture for inequality could differ substantially.

UK poverty

Figure 1 shows projected absolute After Housing Costs (AHC) poverty rates, with and without planned tax and benefit reforms. The most significant of these reforms are the freezing of most working-age benefits in cash terms until March 2020, the transition to Universal Credit, and the policy to limit tax credits and universal credit to the first two children (henceforth 'the two child limit'). As the figure makes clear, overall poverty is projected to remain roughly unchanged between 2015 and 2021: it would be projected to fall in the absence of planned reforms, which are projected to increase poverty by 1ppt. Absolute child poverty is projected to rise by 4.1 ppts, with almost all of that rise being explained by reforms. Relative child poverty is also projected to rise, from 30% to 37%.

Figure 1: Absolute AHC poverty rates, with and without planned direct tax and benefit reforms



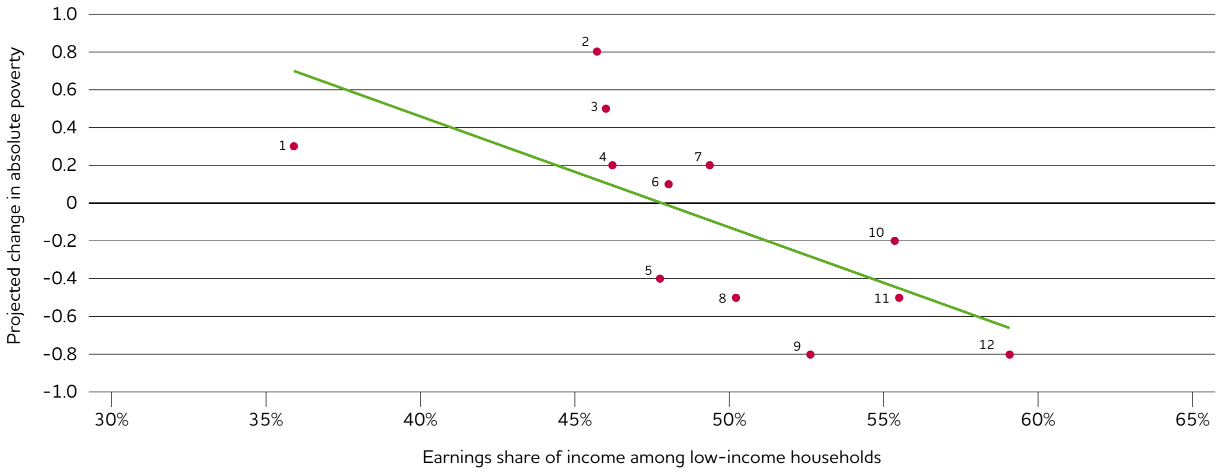
Source: Authors' calculations using Family Resources Survey, various years, and projections for 2016 to 2021 given assumptions specified in the text.

Notes: Poverty line is 60% of median income in 2010, adjusted by CPI excluding rent.

Regional poverty

Figure 2 shows the projected change in overall absolute poverty in each region between 2013–15 and 2019–21, against the share of income coming from earnings for low-income working-age households in that region. There are two things to note from this figure. First, there is considerable variation in the projected change in poverty: while Northern Ireland and Wales are projected to see rises in absolute poverty of 0.5 and 0.8 ppts respectively, London and the South East are projected to see falls of 0.8 ppts. Second, much of that variation is explained by the extent to which low-income working-age households in those regions are reliant on earnings for their income. Those less reliant on earnings will get only a small boost in incomes when real earnings rise, and will be more exposed to planned cuts to working-age benefits. Relative poverty is expected to rise in all parts of the UK, but the largest rises are likely to be in the North East, Wales and Northern Ireland. Much smaller increases are expected in London and the South East.

Figure 2: Projected change in absolute poverty against earnings share of income among low-income working-age households



1	North East	4	North West	7	East Midlands	10	South West
2	Wales	5	Yorkshire and Humberside	8	Scotland	11	East of England
3	Northern Ireland	6	West Midlands	9	London	12	South East

Source: Authors' calculations using Family Resources Survey, various years, and projections for 2016–21 given assumptions specified in the text.

Notes: 'Low-income households' are those with real income below 70% of median income in 2010, adjusted by CPI excluding rent. Working-age households are those where all members are under 65.

Another key driver of trends in poverty across regions is the two child limit. The share of people living in low income households with at least three children varies considerably between regions, with the share in the West Midlands and Northern Ireland being almost twice as high as in Scotland, the South West, and South East. The two child limit will have a bigger effect on incomes in those regions with more low-income large households, and so they are projected to see a bigger rise in poverty as a result.

These regional projections assume that earnings and rent growth in each region will follow the OBR's national forecast. The relative fortunes of different regions could be different to these projections if there is significant geographical variation in future growth in rent or pay.

Conclusions

Since the recession, median income growth has been weak. This trend is projected to continue for the next few years, as earnings falter and inflation rises. Cuts to working-age benefits together with growth in real earnings are likely to push inequality up over the period, particularly when measured on an AHC basis.

Overall absolute poverty is projected to be little changed, but absolute child poverty is projected to rise, mainly thanks to policy reforms. These trends differ between regions, with their labour market and demographic characteristics driving the differences: those regions with more large low-income families, and greater dependence upon benefits, face less favourable prospects for poverty.

About the project

The authors take the latest data used to produce official income and poverty statistics (Family Resource Survey 2013 to 2015) and adjust these data for relevant known and forecast changes – for example demographic and labour market trends, and changes to tax and benefit policy – to create a projected distribution of household incomes in each year up to 2021.

FOR FURTHER INFORMATION

The full report, **Living Standards, Poverty and Inequality in the UK: 2017–18 to 2021–22** by Andrew Hood and Tom Waters, is published by the Institute for Fiscal Studies. It is available at www.ifs.org.uk

Read more publications at www.jrf.org.uk
Other formats available
ISBN: 978-1-911581-19-2

Joseph Rowntree Foundation
The Homestead
40 Water End
York YO30 6WP
Tel: 01904 615905

email: info@jrf.org.uk
www.jrf.org.uk
Ref: 3274

JRF JOSEPH ROWNTREE FOUNDATION

INSPIRING SOCIAL CHANGE