

## London and West Midlands suffer highest rates of poverty in the UK

London and the West Midlands displace North-East England and Northern Ireland as the regions of the UK with the highest rates of poverty when we take account of differences in the cost of living around the country, according to *Poverty and Inequality in the UK 2008*, the annual analysis by IFS researchers of yesterday's *Households Below Average Incomes* data from the Department for Work and Pensions.<sup>1</sup>

The annual *Households Below Average Income* report from the Department for Work and Pensions describes the pattern of household incomes after deducting direct taxes and adding tax credit and benefit payments, and adjusted for family size. It compares incomes both before housing costs (BHC) and after housing costs (AHC). A separate press release from the IFS dated 10 June 2008 detailed the main developments in the latest year, including low income growth and rises in poverty and inequality.

Today's report provides a more detailed analysis of key trends in living standards, poverty and inequality, based on the data that underlie yesterday's DWP publication. The main findings are as follows:

### Living Standards and Inequality

- Mean household income has grown by an average of 2.1% a year in real terms under the current Government. But this masks two distinct periods – five years of fast growth averaging 3.4% a year to 2001-02, followed by five years of slow growth averaging less than 1% per year.
  - This slowdown can also be seen in National Accounts data. These show slowing growth in household disposable income per head since 2001-02, despite comparatively robust growth in national income per head over the same period. This suggests that households have seen their share of national income fall since 2001-02.
  - Real income growth was close to zero across most of the income distribution between 2005–06 and 2006–07. Only incomes towards the top saw growth much above zero. Real income growth in the top 1% of the distribution is estimated to have been more than 5% between 2005-06 and 2006-07, compared with median real income growth of just 0.4%. (The 5% figure is not statistically significantly different from zero, but relatively rapid growth at the top is in line with recent trends.)
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- Income inequality has now risen back to its highest-ever level – last seen in 2000-01 – as measured by the Gini coefficient (at least since comparable records began in 1961).
- Middle incomes have kept pace with incomes towards the top of the income distribution (the ratio of incomes at the 90th percentile to incomes at the 50<sup>th</sup> percentile is unchanged since 1996–97). However, there is some evidence that incomes at the very top of the distribution (the 99th percentile) have been ‘racing away’ from incomes further down the distribution.

## Poverty

- Poverty among the whole population increased for a second successive year in 2006-07, to a level statistically significantly higher than in 2004-05. The risk of poverty has increased for children, parents, pensioners and working-aged childless adults over the last two years.
- The rise in pensioner poverty is large and statistically significant: 300,000 using incomes measured BHC, and 200,000, AHC. The increase in poverty is due to an increased risk of poverty for all age-groups of pensioners, but particularly older ones. There are three main explanations:
  - First, the abolition of age-related payments (an additional £50 or £200 *on top* of the winter fuel payments paid during winter 2005) can likely explain 100,000 of the rise.
  - Second, as detailed in the press release of June 10<sup>th</sup>, increasing inflation led to a fall in the real value of some benefits, including the state pension.
  - Third, like all surveys, the Family Resources Survey (from which HBAI statistics are constructed) suffers from sampling error and mistakes or omissions by respondents. It seems that in 2006-07, these problems may have been somewhat more noticeable than usual, with, in particular, more severe underreporting of the Pension Credit.
- Poverty amongst working aged adults without dependent children was broadly stable in 2006-07, in contrast to the significant rise in the previous year. Nevertheless it remains close to an historic high, reflecting the fact that Labour’s redistributive policies have largely passed this group by.

## Material deprivation

- The Government has a new definition of poverty to supplement the usual measure of relative low income. This says a family is poor if it has a relatively low income *and* is unable to afford certain items/necessities. On this measure, child poverty has fallen slightly since 2004-05. This is consistent with the living standards of the poorest families with children having improved since 2004-05, but not having improved as quickly as those in the middle of the income distribution.

- Families with a low income are not always materially deprived. Indeed, children in households with less than 40% of median income – those in so-called ‘severe’ poverty – are, on average, less deprived than those in households with between 40% and 60% of median income.
- A material deprivation indicator suggests that child poverty is more of a problem in London, and less of a concern in Scotland, Wales and Northern Ireland, than a relative low-income measure of child poverty.
- Children in a working lone-parent family are less likely to be in income poverty than those in a one-earner couple family, but more likely to be in poverty using a material deprivation indicator. If the material deprivation indicator is a good measure of living standards, then this weakens the case for paying higher working tax credit to couples on the basis that their costs are higher.

### **Regional living standards and poverty rates (*see tables at end for more detail*)**

- We detail how median income, real income growth since 1996-97, poverty rates and changes in poverty since 1996-97 vary across the country. When we use **national prices** we find:
  - Median income before housing costs (BHC) is highest in the South East and London and lowest in the North East, West Midlands and Northern Ireland.
  - Income growth (BHC) since 1996-97 has been fastest in London (28%) and the North East of England (26%) and slowest in the West Midlands (14%) and East Midlands (17%).
  - The rate of poverty is highest in the West Midlands (20.9%) using incomes measured BHC and in London (27.5%) using incomes measured AHC. It is lowest in the South East under both measures (13.7% and 18.3% respectively).
  - The rate of poverty has fallen most in the North East of England using both incomes measured BHC (-4.4%) and AHC (-6.2%), with Scotland seeing sizeable falls under both measures, and Wales and the South West under AHC poverty only. On the other hand, poverty is either unchanged (AHC) or risen very slightly (BHC) in the West Midlands, with the East Midlands and South East also performing relatively poorly.
- However, the cost of living varies considerably across the country – even after accounting for housing costs. In 2004-05 (the most recent year for which we have information about regional price variation), when accounting for price differences:
  - Living standards in London, and the South East are lower than when using national prices, whilst those in Wales, Scotland and northern regions of England are higher. Accounting for differences in the cost of living means that London falls from having the 2<sup>nd</sup> highest median

income (BHC) to the 4<sup>th</sup> highest, whilst Scotland moves from 5<sup>th</sup> highest to 2<sup>nd</sup> highest. Wales moves up from 11<sup>th</sup> position to 7<sup>th</sup> position, with the West Midlands taking its place.

- London goes from mid-table (18.2%) to having the highest rate of poverty (BHC) in the country by some margin (22.6%) when its high cost of living is taken into account. The South East, East and South West also see rises in their rate of poverty. The rate of poverty in Scotland, Wales and northern regions of England falls when their lower prices are taken into account, with Wales and the North East seeing particular improvements.

### **Lone parents receiving tax credits**

- Two years ago, IFS researchers said that the Government was paying child-related support to 200,000 more lone parent families than were thought to live in the UK. By 2006-07, this number has fallen to 100,000. This matches very well with new estimates from the Government that in 2004-05, whether through fraud or error, it wrongly paid tax credits to 80,000 families who claimed to be lone parents. That some couples are receiving tax credits as lone parents is supported by detailed analysis of the Family Resources Survey, which suggests that more low-income couples families – and fewer low-income lone parent families – are receiving tax credits than HMRC think it is paying out. Although we cannot know how much this is due to fraudulent behaviour, the financial incentive to pretend to be a one-adult family with children continues to be substantial, reflecting the generosity of tax credits which are based on a family means-test.

Ali Muriel, Research Economist, says “The Government is sure to be disappointed by a fifth consecutive year of slow average income growth. Though the economy as a whole has grown robustly in recent years, the money doesn’t seem to be finding its way into average take-home incomes. Meanwhile, incomes at the very top of the distribution continue to grow strongly, ‘racing away’ from the rest, and pushing income inequality back to its highest level in recent history.”

Luke Sibieta, Research Economist, says “The Government’s new material deprivation indicator paints a different picture of the poor than income. We should be wary of describing children in households with less than 40% of median income as living in ‘severe’ poverty; in reality, they seem to be less materially deprived on average than those in households with between 40% and 60% of median income.”

Mike Brewer, Senior Research Economist, says “This report shows that comparing the income levels of households in different regions can give a misleading picture of differences in the standard of living. Whether we account for differences in the cost of living between regions directly, or whether we ask what

essentials families with children can afford, we find that living standards are lower in London, and higher in Wales, Scotland and Northern Ireland than if we simply compare income levels”.

David Phillips, Research Economist, says “When we take differences in regional price levels into account, the poverty map of Britain is a not a simple ‘North-South divide’. The West Midlands has the second highest poverty rate and the second lowest standard of living in the country. The region has seen the smallest decline in poverty and the weakest growth in household incomes of any UK region over the past 10 years. By contrast, Wales, Scotland and North-east England all have significantly lower rates of poverty than the headline figures suggest when the low cost of living in these regions is taken into account.”

Notes to editors:

1. Further analysis of the data underlying the official statistics will available in *Poverty and Inequality in Britain: 2008* by Mike Brewer, Alastair Muriel, David Phillips and Luke Sibieta. This report was launched at IFS on 11 June 2008. It is available at <http://www.ifs.org.uk/comms/comm105.pdf>. The official HBAI document is available at <http://www.dwp.gov.uk/asd/hbai.asp>. The other IFS PR is available at [http://www.ifs.org.uk/press.php?publication\\_id=4253](http://www.ifs.org.uk/press.php?publication_id=4253).

**Table 1: Regional Relative Median Income and Relative Poverty (2005-06 and 2006-07)**

**UK = 100 (Income) UK = 22% (Poverty)**

| Region           | Relative Income | Relative Poverty (AHC) |
|------------------|-----------------|------------------------|
| South East       | 116.6           | 18.3%                  |
| London           | 112.7           | 27.5%                  |
| East of England  | 107.5           | 18.7%                  |
| South West       | 100.8           | 19.6%                  |
| Scotland         | 98.6            | 19.3%                  |
| East Midlands    | 95.0            | 22.5%                  |
| Yorkshire        | 93.7            | 22.2%                  |
| Wales            | 93.1            | 22.5%                  |
| North West       | 92.9            | 24.0%                  |
| North East       | 90.9            | 23.4%                  |
| Northern Ireland | 90.9            | 19.9%                  |
| West Midlands    | 90.8            | 24.4%                  |

**Table 2: Percentage Growth in Real Incomes Across the Country and Percentage Point Change in Relative Poverty rate (AHC) (1996-97 to 2006-07)**

**UK percentage growth = 20%**

| Region          | Percentage Growth | Change in Poverty (ppt) |
|-----------------|-------------------|-------------------------|
| London          | 28%               | -2.8%                   |
| North East      | 26%               | -6.3%                   |
| South West      | 24%               | -4.0%                   |
| Yorkshire       | 23%               | -3.5%                   |
| Wales           | 22%               | -4.9%                   |
| Scotland        | 21%               | -4.6%                   |
| East of England | 20%               | -2.6%                   |
| North West      | 18%               | -2.0%                   |
| East Midlands   | 18%               | -1.4%                   |
| South East      | 18%               | -1.7%                   |
| West Midlands   | 14%               | -0.0%                   |

**Table 3: Using Regional Prices – Median Income and Poverty Rates (BHC) (2004-05, in 2006-07 prices)**

| Region           | National prices | Regional prices | National Prices | Regional Prices |
|------------------|-----------------|-----------------|-----------------|-----------------|
| South East       | £429 (1)        | £407 (1)        | 12.2% (12)      | 14.9% (11)      |
| London           | £415 (2)        | £378 (4)        | 18.2% (7)       | 22.6% (1)       |
| East Anglia      | £396 (3)        | £392 (3)        | 13.8% (11)      | 14.6% (12)      |
| South West       | £377 (4)        | £372 (5)        | 14.1% (10)      | 15.5% (7)       |
| Scotland         | £371 (5)        | £393 (2)        | 17.2% (9)       | 14.9% (10)      |
| East Midlands    | £355 (6)        | £364 (6)        | 18.9% (5)       | 18.2% (4)       |
| North West       | £352 (7)        | £363 (9)        | 18.4% (6)       | 16.9% (6)       |
| West Midlands    | £347 (8)        | £355 (11)       | 19.7% (3)       | 19.0% (2)       |
| Yorkshire        | £342 (9)        | £363 (8)        | 18.0% (8)       | 15.1% (9)       |
| Northern Ireland | £341 (10)       | £356 (10)       | 20.6% (2)       | 18.4% (3)       |
| Wales            | £339 (11)       | £364 (7)        | 19.3% (4)       | 15.3% (8)       |
| North East       | £330 (12)       | £350 (12)       | 21.6% (1)       | 18.0% (5)       |
| UK               | £372            | £374            | 17.0%           | 17.0%           |

Note that the poverty rates reported in table 3 are for BHC prices and are therefore not comparable with those in table 1 and 2. The latest available regional price indices are for 2004-05 and it for this table 3 presents results. Relative ranking in brackets.