What does yesterday’s news mean for living standards?

Robert Joyce
Real Household Disposable Income

- OBR forecasts total RHDI

- OBR’s implied forecasts for growth in per-capita RHDI, given ONS population projections:

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<td>0.9%</td>
<td>1.2%</td>
<td>1.4%</td>
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<td>Yesterday</td>
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If the OBR is correct...

- 4.7% fall in per-capita RHDI between 2009 and 2012
  
  - Easily the largest fall over a three-year period on record (since 1955)
  
  - Previous largest fall was 1.9% between 1974–77

- Per-capita RHDI still lower in 2016 than it was in 2006
  
  - Combination of slow growth pre-recession, sharp fall during recession, and slow recovery afterwards

- Worst previous decade on record for changes in per-capita RHDI was 1973-83, when it grew by 14.4%
Another measure of income

- Much of OBR’s increased pessimism about RHDI due to increased pessimism about non-labour, non-benefit income
  - Gloomier expectations about company profits and stock market in near term – implications for investment income
  - Likely to affect those close to top of income distribution most
  - Would expectations about (e.g.) median income look different?

- RHDI is a national accounts measure – just an aggregate

- But we have model which attempts to forecast distribution of income

- Uses same net household income definition as in government statistics on income distribution (HBAI), and Child Poverty Act (2010)
  - Similar to, but not strictly comparable with, measure of real income in RHDI series
Important assumptions and caveats

• We use model to link changes in employment and earnings, as well as taxes and benefits, to net household income
  – Use OBR’s macroeconomic forecasts, over which there is much uncertainty, as ‘inputs’ to this model

• OBR forecasts average (mean) earnings, but not the distribution of earnings around that average
  – Assume all earned income grows at the rate of the mean

• OBR forecasts total employment, but not employment among subgroups
  – Model changes in size of the employed population, but not changes in its composition
**Things we learnt yesterday which are relevant for net household incomes (1)**

**New macroeconomic forecasts from the OBR (March 2011 forecasts in red)**

<table>
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<tr>
<th>Employment (millions)</th>
<th>2011</th>
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<tr>
<td>29.0</td>
<td>29.2</td>
<td>29.5</td>
<td>29.7</td>
<td>30.0</td>
<td></td>
</tr>
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<td>29.2</td>
<td>29.4</td>
<td>29.7</td>
</tr>
<tr>
<td>Real mean earnings growth (%)</td>
<td>-3.1</td>
<td>-1.4</td>
<td>0.3</td>
<td>0.7</td>
<td>0.7</td>
</tr>
<tr>
<td></td>
<td>-4.3</td>
<td>-1.3</td>
<td>0.2</td>
<td>1.2</td>
<td>0.9</td>
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Things we learnt yesterday which are relevant for net household incomes (2)

- Changes to tax and benefit policy
  - Council tax freeze in England in 2012–13; costs £675 million in 2012-13
  - Above-inflation increase in child element of Child Tax Credit will not go ahead; saves £975 million in 2012–13
  - More elements of Working Tax Credit will be frozen; saves £265 million in 2012–13
  - Revenue-neutral changes to Pension Credit
  - Fuel duty increase originally planned for April 2011 delayed further to August 2012, increase originally planned for April 2012 cancelled; costs £975 million in 2012-13
Distributional impact of changes taking effect in 2012–13 by income decile group

Change in net income

Income Decile Group

© Institute for Fiscal Studies
Distributional impact of changes taking effect in 2012–13 by household type

Change in net income

-2.0% -1.5% -1.0% -0.5% 0.0% 0.5% 1.0%

Families with children  Pensioners  Working-age without children  All

-1.5% -1.0% -0.5% 0.0% 0.5% 1.0%

Autumn Statement  Pre-announced  Total % gain
Real median net household income: projections

- Before yesterday's news
- With revised OBR forecasts
- With revised OBR forecasts and policy announcements

Sources: Department for Work and Pensions’ HBAI series; IFS calculations and projections using Family Resources Survey.
Forecasted real growth in median net household income: summary

• Between 2009-10 and 2012-13, we are forecasting 7.4% fall in real median net household income
  
  – Essentially the same as between 1974-77 (fall of 7.5%), which is largest 3-year fall since records began (starting 1961)

• Real median net household income in 2015-16 forecast to be lower than in 2002-03
  
  – Again, combination of slow growth pre-recession, sharp fall during, and slow recovery after
  
  – Easily longest period of no growth at median since records began
And Government’s child income poverty targets?

- We estimate little overall change in outlook for path of child poverty in coming years
  - Remains inconceivable that Government will get close to its 2020 child poverty targets under current policies

- Government previously said its reforms would not increase relative income child poverty through to 2012-13

- We disagreed slightly
  - We model Local Housing Allowance (LHA) reforms; HMT were not

- Government now thinks its reforms will increase relative child poverty by about 100,000 in 2012-13

- Why the change?
  - Tax credit cuts announced yesterday
  - HMT is now modelling LHA reforms
Conclusions

• OBR and IFS modelling both suggest we are living through the worst period for changes in measures of average living standards since consistent records began in mid 50s/early 60s

• OBR’s revisions yesterday to previous macroeconomic forecasts have worsened the outlook for living standards

• New tax and benefit measures are, on average, a takeaway from lower-income families with children, and giveaway to middle and top of income distribution
  – But very small compared to changes already announced

• Of course, huge uncertainties remain