Fiscal Policy, Monetary Policy and Intergenerational Inequality in the UK

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Output per head only just above 2008Q1 level

GDP per person aged 16+

2% per year growth

15% gap

Source: Office for Budget Responsibility
And forecast growth also weak ...

2% per year growth

18% gap

GDP per person aged 16+

Source: Office for Budget Responsibility
Income and earnings inequality down recently

90:10 ratio for UK Net Equivalised Household income and Gross Weekly Earnings

Source: Family Expenditure Survey; Family Resources Survey; Annual Survey of Hours and Earnings
Income and earnings inequality down recently

90:10 ratio for UK Net Equivalised Household income and Gross Weekly Earnings

Source: Family Expenditure Survey; Family Resources Survey; Annual Survey of Hours and Earnings
Having grown sharply over 1980s

Source: Figures 3.6 and 3.7 of Living Standards, Poverty and Inequality: 2016
Top 1% share continuing to rise until 2008

Source: Figure 3.7 of *Living Standards, Poverty and Inequality: 2016*
Median incomes stagnant

Source: Figure 2.6 of *Living Standards, Poverty and Inequality: 2016*
Much worse for the young

Source: Figure 2.6 of Living Standards, Poverty and Inequality: 2016
Much better for the old

Source: Figure 2.6 of Living Standards, Poverty and Inequality: 2016
The distribution of wealth
And concentrated at older ages

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Of course the old hold the cash

25th percentile
Median
75th percentile

Cash/near cash holdings vs. Age-group
But it’s the young who can’t build up savings

If you work until 67, die at 90, and have earnings that grow 2% p.a.

With 4% real interest rate you need to save 10% of income to replace 50% in retirement

With 0% real interest rate saving rate needs to be 30%
The old also hold the housing wealth

Home-ownership rates by age-group

Percentage of individuals who own their own home

- 16-24
- 25-34
- 35-44
- 45-64
- 65-74
- 75+

Source: English Housing Survey

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Much more so than just 15 years ago

**Home-ownership rates by age-group**

<table>
<thead>
<tr>
<th>Age Group</th>
<th>2001/02</th>
<th>2013/14</th>
</tr>
</thead>
<tbody>
<tr>
<td>16-24</td>
<td>15%</td>
<td>10%</td>
</tr>
<tr>
<td>25-34</td>
<td>55%</td>
<td>60%</td>
</tr>
<tr>
<td>35-44</td>
<td>75%</td>
<td>80%</td>
</tr>
<tr>
<td>45-64</td>
<td>85%</td>
<td>90%</td>
</tr>
<tr>
<td>65-74</td>
<td>90%</td>
<td>95%</td>
</tr>
<tr>
<td>75+</td>
<td>80%</td>
<td>85%</td>
</tr>
</tbody>
</table>

Source: English Housing Survey

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Younger cohorts much less likely to be owner occupiers

Homeownership rate

Age

20%
30%
40%
50%
60%
70%
80%
90%

1930s
1940s
1950s
1960s
1970s
Early 1980s

Early 1980s
And DB pensions have collapsed

Percentage of employee jobs in a defined benefit pension scheme

Source: ONS
Proportion of private sector employees in DB scheme 1997 and 2015

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But there is an increasing aggregate deficit of DB schemes

Assets and liabilities of DB schemes in the Pensions Protection Fund

Source: PPF/ The Pensions Regulator
Overall younger cohorts accumulating less wealth
Loose monetary policy supporting tight fiscal policy

Latest outturn and forecast for total Government spending and receipts

Source: OBR
Crucial point: after 8 years of “austerity” the size of the state is just back at pre crisis levels
Increases in spending on pensions and health offset cuts elsewhere

<table>
<thead>
<tr>
<th>Category</th>
<th>2007-08</th>
<th>2016-17</th>
</tr>
</thead>
<tbody>
<tr>
<td>Pensioner benefits</td>
<td>+0.8</td>
<td></td>
</tr>
<tr>
<td>Health</td>
<td>+0.7</td>
<td>+0.3</td>
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<tr>
<td>Overseas aid</td>
<td>0.2</td>
<td>-0.2</td>
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<tr>
<td>Working-age benefits</td>
<td>-0.3</td>
<td>-0.3</td>
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<tr>
<td>Debt interest</td>
<td>-0.3</td>
<td>0.2</td>
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<tr>
<td>Schools</td>
<td>-0.4</td>
<td>-0.5</td>
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<tr>
<td>Defence</td>
<td>-0.5</td>
<td></td>
</tr>
<tr>
<td>Other</td>
<td></td>
<td>0.0</td>
</tr>
<tr>
<td>Public order &amp; safety</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Spending in 2016-17</td>
<td>39.0</td>
<td>39.3</td>
</tr>
</tbody>
</table>
Tax and benefit changes have hit the bottom half and the very top

Percentage change in net household income as a result of tax and benefit policies implemented under the coalition government

- 5%
- 4%
- 3%
- 2%
- 1%
- 0%
- 1%
- 2%

Source: IFS
Pensioners protected, those with children hit hardest

Impact of coalition government tax and benefit policies by group

Percentage change in net household income

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Source: IFS
Fiscal policy has worked with monetary policy and underlying trends to protect the old and hit the young

1. **Triple lock** means basic state pension has grown 9%pts more than average earnings since 2010-11.
The triple lock

Growth rate of basic state pension compared to average earnings
(2010-11 level = 100)

Source: OBR and author’s calculations
Policy changes have exacerbated existing trends

1. **Triple lock** means basic state pension has grown 9%pts more than average earnings since 2010-11.

2. **The state pension age** for men has not kept up with increasing longevity
Dramatic increase in numbers living longer in recent decades

Proportion of male 65-year-olds surviving to given age

- 65 in 1987
- 65 in 2017

Source: ONS Life Tables
Policy changes have exacerbated existing trends

1. **Triple lock** means basic state pension has grown 9%pts more than average earnings since 2010-11.

2. **The state pension** age for men has not kept up with increasing longevity

   - Without further rises in the state pension age, pension spending will rise rapidly as a share of GDP, and require other spending cuts or tax rises.
Even without triple lock, state pension spending will rise as a share of GDP
Policy changes have exacerbated existing trends

1. **Triple lock** means basic state pension has grown 9%pts more than average earnings since 2010-11.

2. **The state pension** age for men has not kept up with increasing longevity

3. Reductions in pensions lifetime allowance have not hurt current pensioners but those who are currently of working age.

4. Cuts to public service pensions mostly impact those of working age

5. Taxation of housing continues to favour those who already own...
Fiscal attempts to offset have been minimal, counter-productive or ineffective

1. Ending requirement to annuitise pensions
   response to low interest rates
2. “Help-to-buy” intended to help first time buyers
   has likely raised prices
3. Attempts to increase housebuilding ineffective
4. Taxes on buy-to-let as a ‘third best’ response
Fiscal and monetary policies together

Distributional effects of fiscal policy regularly analysed:
- Increasing focus on impact by age, not just income

Impacts of monetary policy less easy to define:
- What is the counterfactual?
- Would need to know impact of monetary policy on asset markets

Attitudes matter
- Changes to asset values seen as “act of God”
  - Impacts via e.g. DB schemes may not be visible
- Those who already have money notice changes to interest rates
  - But bigger impact on those looking to build savings
- Fiscal policies reducing entitlements of old seen as “retrospective”
- Tax increases/benefit cuts for working age deemed acceptable