# No growth in household incomes last year – for only the fourth time in the last 30 years

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# In 2017–18, average household income growth stalled for first time since 2012–13

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# Introduction

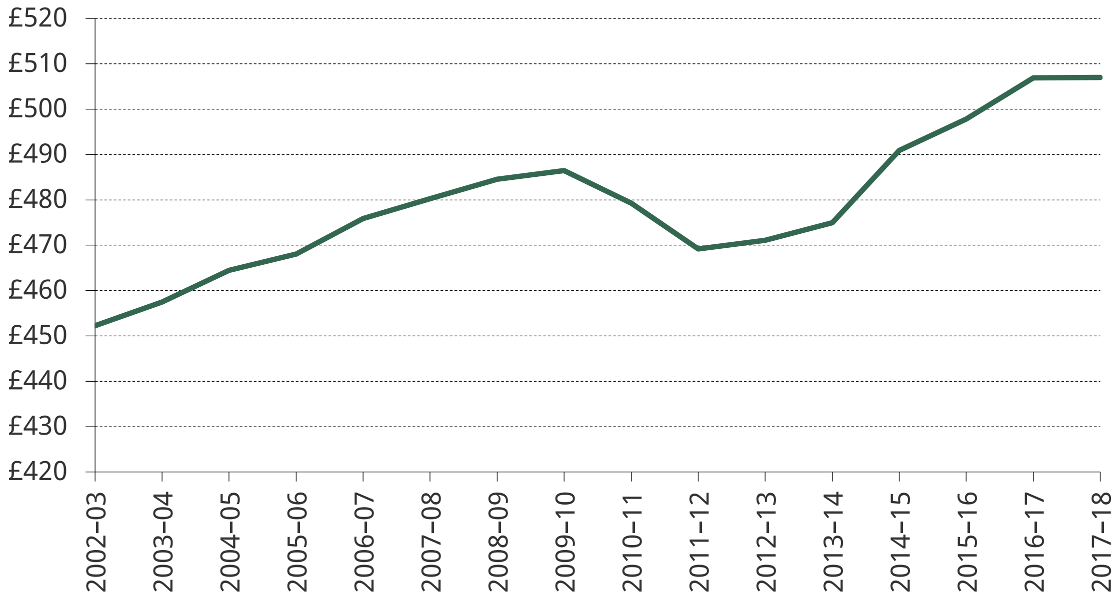
Following the falls in average living standards in the years after the Great Recession, average (median) household incomes grew by 8% between 2011–12 and 2016–17 after adjusting for inflation. But in 2017–18, that recovery in average household incomes stopped, with 0% real growth between 2016–17 and 2017–18.

That is the most striking result in today's (Thursday 28th March 2019) release of the government official statistics on incomes and poverty in the UK in 2017–18, published by the Department for Work and Pensions. This short briefing note summarises what the newly released data tell us about how living standards changed in 2017–18, and what the implications are for income inequality and poverty. A more in-depth study into the recent trends, funded by the Joseph Rowntree Foundation, will be published in early Summer.

The new data show that income growth was close to zero right across the income distribution in 2017–18, and overall absolute (and relative) poverty rate was therefore unchanged.

## Average living standards: median household income growth stalls for first time since 2012–13

**Figure 1. Median net household income (before housing costs) since 2002–03**

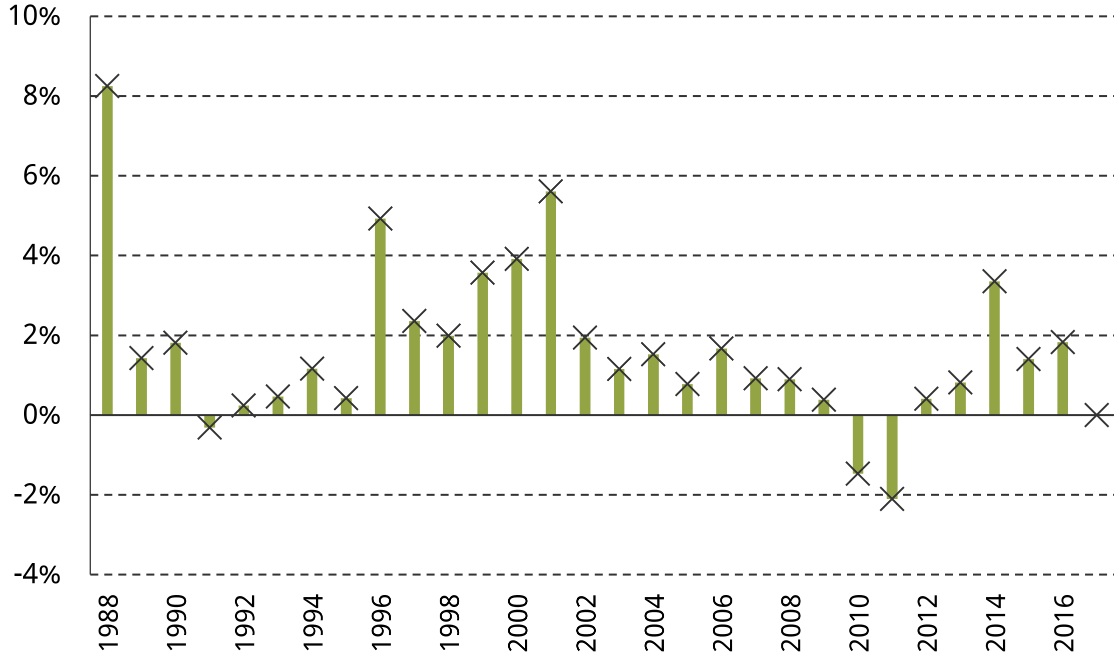



Note: Incomes have been measured net of taxes and benefits but before housing costs have been deducted and are expressed in 2017–18 prices. All incomes have been equivalised using the modified OECD equivalence scale and are expressed in terms of equivalent amounts for a childless couple. Source: Department for Work and Pensions (2019) "Households below average income: 1994/95 to 2017/18.

The average (median) household in the UK in 2017–18 was £507 per week, 6% above its pre-recession (2007–08) level, and 8% above its post-recession low in 2011–12.

However, as Figure 2 shows, there was no average income growth at all in 2017–18. This means that income growth stalled for the first year since 2012–13. In fact, 2017–18 was only the fourth year in the last 30 years where median income did not grow in real terms.

**Figure 2. Growth in median household income (before housing costs) in the last 30 years**



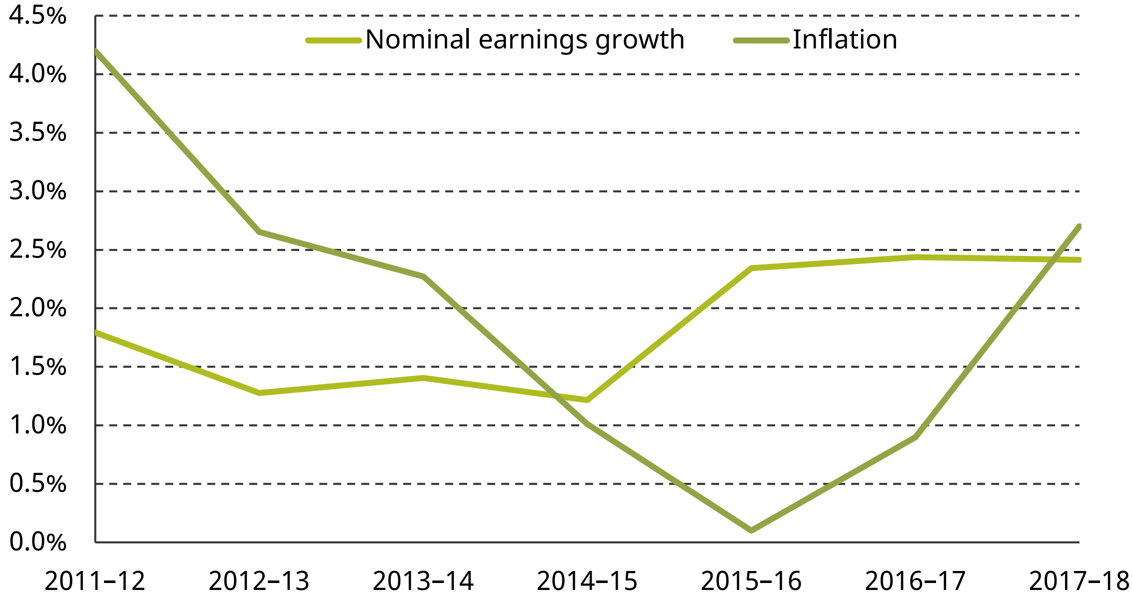

Note: Incomes have been measured net of taxes and benefits but before housing costs have been deducted and are expressed in 2017–18 prices. Years refer to calendar years up to and including 1992 and to financial years from 1993–94 onwards. Data are representative of households in Great Britain between 1990 and 2001–02 and of households in Great Britain and Northern Ireland from 2002–03 onwards. Source: Department for Work and Pensions (2019) "Households below average income: 1994/95 to 2017/18", and authors' calculations using the Family Expenditure Survey.

The stalling of median income growth is not necessarily surprising. The largest source of households' incomes – employee earnings fell in real terms on average in 2017–18. This is shown in Figure 3 below. In 2017–18, cash-terms weekly earnings growth was 2.4%, similar to the two preceding years (and higher than the 2011–12 to 2014–15 period). However, inflation rose from 0.9% in 2016–17 to 2.7% in 2017–18, meaning real earnings growth was –0.3%.

In addition, most working age benefits were frozen in cash terms in 2017–18, meaning they fell by 2.7% in real-terms, and in addition there were other discretionary cuts to tax credits began to come into force that year too. Although the "benefit freeze" was also in place the previous year in 2016–17, it was much less significant in that year because inflation was much lower.

On the positive side, there was another large increase in the employment rate (of 16-64 year olds) of 0.7 percentage points, this was not enough to push income growth into positive territory in 2017–18.

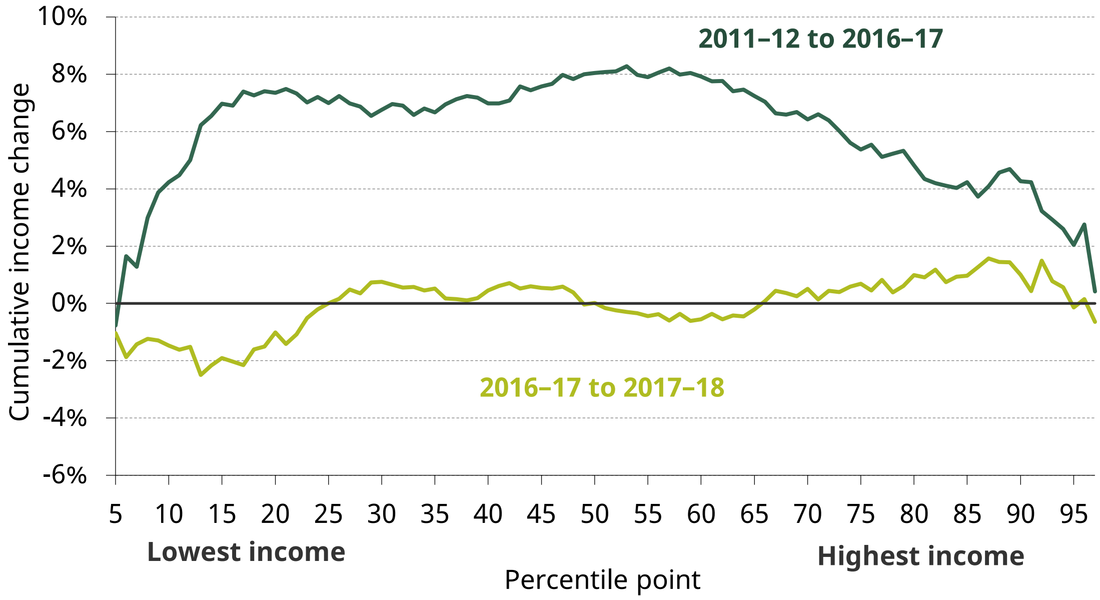
**Figure 3. Nominal (cash terms) weekly earnings growth and inflation, 2011–12 to 2017–18**




Source: IFS calculation using ONS Average weekly earnings series and CPI plus mortgage interest payments. (https://www.ons.gov.uk/economy/inflationandpriceindices/adhocs/008572consumerpriceindicesseriesexcludingrentsmaintenancerepairsandwaterchargesfortheperiodjanuary1996toapril2018 ).

## Income inequality: slight falls in income for lower income households but no large changes

**Figure 4. Real income growth by percentile point, 2011–12 to 2017–18 (UK)**




Note: Incomes have been measured net of taxes and benefits but before housing costs have been deducted and have been equivalised using the modified OECD equivalence scale. Percentiles 1–4 and 98-99 are excluded because of large statistical uncertainty.

Source: Department for Work and Pensions (2019) and IFS calculations using the Family Resources Survey.

Income growth in 2017–18 was close to zero across most of the income distribution. There is some evidence that incomes fell slightly for poorer households in the bottom quarter of the income distribution, although this was not statistically significantly different from zero. This is likely to be in part due to the cuts to working age benefit and tax credit entitlements that occurred in 2017–18.

As discussed above, most working-age entitlements fell by 2.7% in real terms in 2017–18. Our analysis of previous HBAI data from 2016–17 suggests that for the poorest fifth of working age households, benefits and tax credits make up around half their income, meaning that the reductions to benefit entitlements significantly affect the incomes of poorer households.

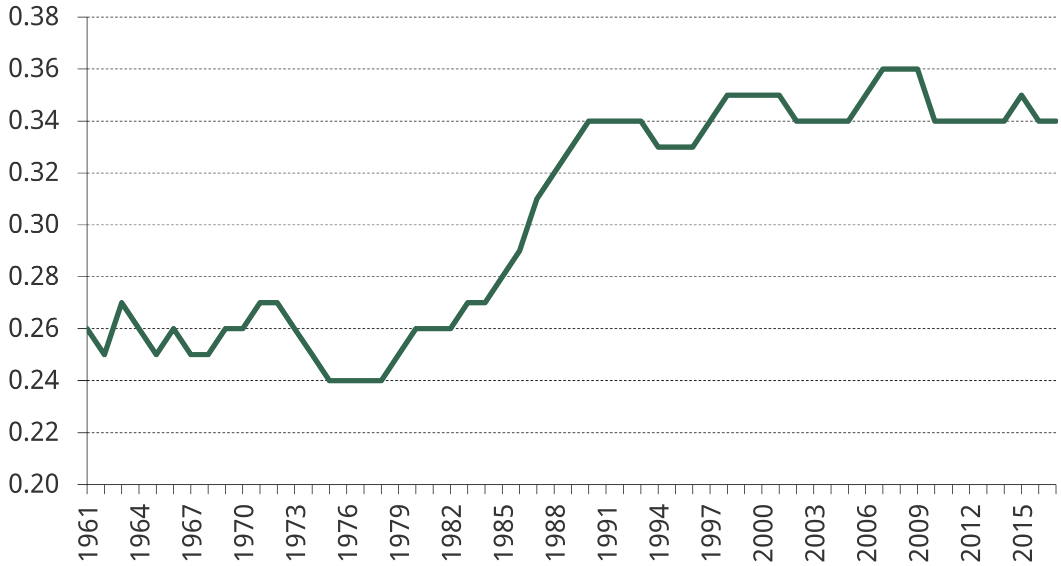
Figure 4 shows this pattern differs somewhat from that seen during the recovery from the recession (2011–12 to 2016–17), where income growth was substantially stronger for middle income households than for high or low income households.

The Gini coefficient is often used as a summary measure of income inequality across the whole income distribution. Figure 5 shows that on this measure of inequality, there was no change in overall income inequality in 2017–18. The Gini was at 0.34 (rounded to 2 significant figures, as the official statistics are), the same level as in 2016–17. This is consistent with the relatively small differences in income growth between richer and poorer households in the latest year of data.

Although overall inequality did not change in these official statistics, there is some other evidence that that the very higher earners have recently seen somewhat higher pay growth. The Office for Budget Responsibility's most recent report finds that that in April-September 2018, annual cash-terms pay growth was 5.9% for the top 0.1% of earners, compared to 3.7% on average. This provides some evidence of increases in inequality at the very top of the income distribution more recently.

Over a longer horizon, Figure 5 shows that income inequality as measured by the Gini coefficient has remained essentially unchanged since the early 1990s, but is  much higher than it was before the large rise in inequality that occurred during the 1980s. Previous IFS research1 has shown that this lack of change in overall income inequality since the early 1990s reflects two countervailing trends: a fall in income inequality across most of the distribution, and a rise in income inequality at the very top (for example measured by the share of income going to the top 1%).

**Figure 5. The Gini coefficient of income inequality, 1961 to 2017–18**

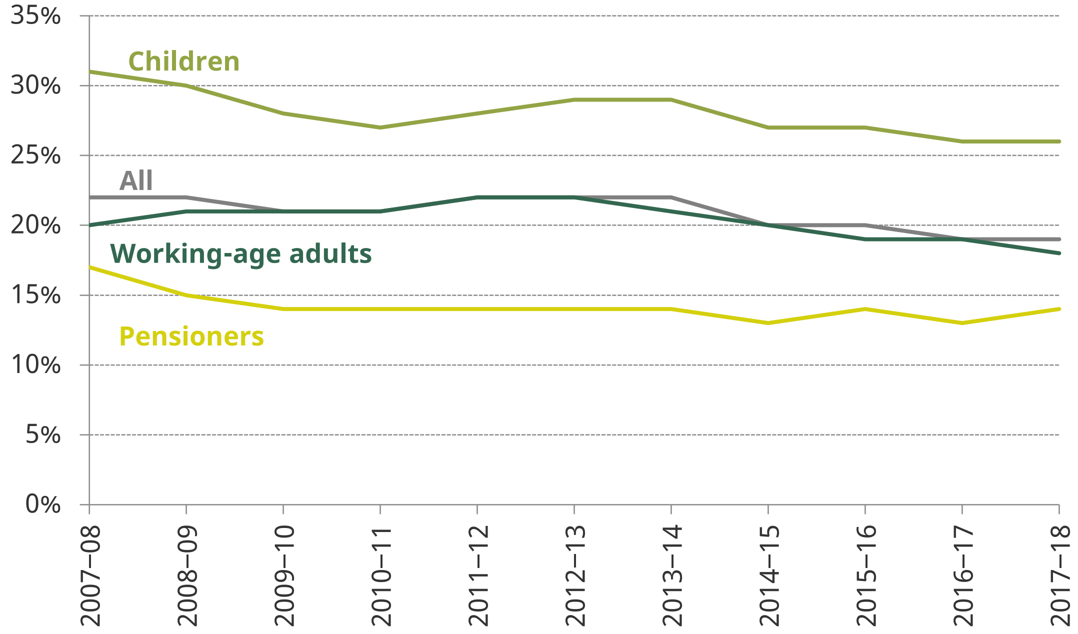



Note: Incomes have been measured net of taxes and benefits but before housing costs have been deducted and have been equivalised using the modified OECD equivalence scale. Years refer to calendar years up to and including 1992 and to financial years from 1993–94 onwards. Figures relate to UK households from 2002–03 onwards and to GB households for earlier years. Source: Department for Work and Pensions (2019) and IFS calculations using the Family Resources Survey and the Family Expenditure Survey.

[1] See Belfield et al (2017) "Two Decades of Income Inequality in Britain: the roles of wages, household earnings and redistribution", *Economica,* 84(334), pp. 157-179

## Poverty: Overall income poverty unchanged in 2017–18

**Figure 6. Absolute poverty rate (AHC) by demographic group**




Note: Incomes have been measured net of taxes and benefits and after housing costs have been deducted and have been equivalised using the modified OECD equivalence scale. The absolute poverty line is defined as 60% of median AHC income in 2010–11.

Source: Department for Work and Pensions (2019)

When assessing trends in poverty there are good reasons to focus on measures of income after deducting housing costs, which we do in this section.

The overall rate of absolute income poverty (measured AHC) was 19% in 2017–18, unchanged from 2016–17. Although there were slight falls in before-housing-cost incomes for low income households (as documented in the previous section), this was not the case for incomes measured AHC. This means that housing costs of low-income households fell in 2017–18 compared to middle income households. One potential reason for this is that there were mandated cuts in rents for tenants in the social rented sector in 2017–18.

The unchanged overall absolute poverty rate comes after falls in poverty over the preceding three years (from 22% to 19% between 2013–14 and 2016–17). Just as the recovery in average incomes came to a halt in 2017–18, so did progress in reducing absolute poverty.

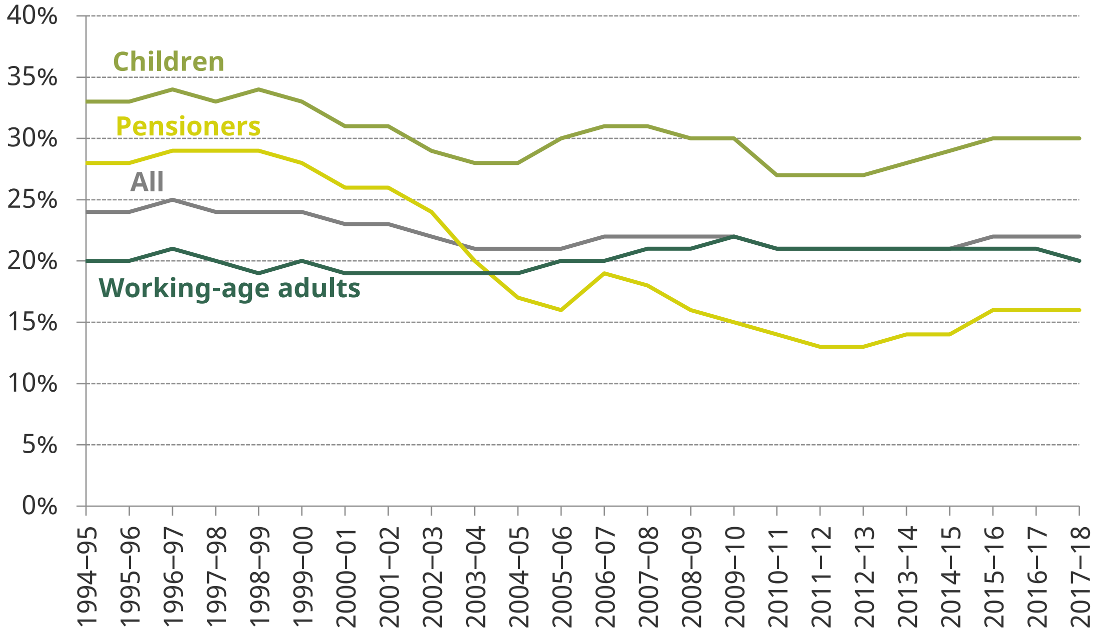
While the *absolute* poverty line is unchanged in real terms from year to year, the *relative* poverty line changes in line with average income. Hence, because there was essentially no average income growth in 2017–18, the relative and absolute poverty rates changed in a very similar way.

Figure 7 puts the changes in relative poverty in a longer run perspective. It shows that over the last 15 years there has been little change in overall relative poverty: in every year since 2002–03, overall relative poverty has been either 21% or 22%.

But this stability in overall relative poverty masks changes for different groups in recent years. Pensioners saw enormous falls in poverty from the late 1990s to 2012–13, but since then pensioner poverty has risen by 3 percentage points. Relative child poverty has also risen by 3 percentage points since 2012–13, reversing the falls between 2007–08 and 2010–11. The relative child poverty rate is still below its recent peak in the late 1990s.

In contrast, working age adults – who have benefitted most from the labour market recovery – have seen slight falls in relative poverty over the same period, though their relative poverty rate is unchanged compared to the mid 1990s.

**Figure 7. Relative poverty rate (AHC) by demographic group**




Note: Incomes have been measured net of taxes and benefits and after housing costs have been deducted and have been equivalised using the modified OECD equivalence scale. The relative poverty line is defined as 60% of median AHC income in each year. Figures relate to UK households from 2002–03 onwards and to GB households for earlier years.

Source: Department for Work and Pensions (2019)

## The future: Conditional on a smooth Brexit, the OBR expects modest growth in average earnings in the coming years

**Figure 8. OBR forecasts for growth in earnings, the national living wage and the employment rate between 2017–18 and 2022–23**


Note: Average earnings and National Living Wage (NLW) deflated by the Consumer Price Index (CPI). Real average earnings and real NLW growth are proportional, employment growth is percentage point change in the rate. Employment rate refers to all aged 16 or over.

Source: Office for Budget Responsibility (2018) *Economic and Fiscal Outlook*, March 2019.

The Office for Budget Responsibility's (OBR) latest macroeconomic forecasts were published two weeks ago (13th March 2019), and were predicated on the UK avoiding a disorderly exit from the European Union.

If the forecasts prove to be correct, there will be modest but steady earnings growth of 1% per year in coming years, resulting in a 5% rise in real average earnings between 2017–18 and 2022–23, which would boost average incomes. The earnings of low paid employees are likely to rise more quickly as the growth in the National Living Wage continues to outpace average earnings. The employment rate is forecast to remain unchanged, with employment growth being subdued by an ageing population.

Most working age benefits have remained frozen in cash terms in 2018–19, a policy that will continue into 2019–20. In combination with other cuts to tax credits and universal credit, this means that benefit entitlements are shrinking in real terms, pushing down the incomes of poorer households.

All together, the forecast increases in earnings and planned reductions in benefits and tax credits suggest that incomes are likely to rise more for middle and high income households than low income households in the coming years, leading to higher levels of income inequality and relative poverty.

Having said that, since the recession, real earnings growth has been consistently lower than forecast by the OBR and employment has grown substantially more quickly than expected. If this pattern of lower-than-expected earnings and higher-than-expected employment were to continue, this would boost lower incomes more and supress higher incomes, potentially helping to hold down or prevent rises in income inequality and relative poverty.

## Appendix: Measuring incomes and poverty in the UK

The "Households Below Average Income" Statistics that the government have released, and that are used in this briefing note, are based on a survey called the Family Resources Survey of around 19,000 households per year. Using these data, Department for Work and Pensions measure household incomes in the following way:

- Incomes are measured after all direct taxes have been paid and state benefits have been received;
- Incomes are measured at the *household* level, meaning the incomes of all household members are added together;
- Incomes are adjusted for the household size and composition (and expressed as the equivalent income for a childless couple);
- Incomes are adjusted for inflation using a variant of the Consumer Prices Index and are expressed in 2017–18 prices.

Using these data, it is possible to measure how many people are in income poverty. There are two main measures of income poverty measured by the government:

- Absolute income poverty: This measures how many people have household incomes below a level that is fixed in real terms (i.e. the level increases in line with inflation over time).
- Relative income poverty: This measures how many people have an income below 60% of contemporaneous median income. Therefore, as median income has grown during the recovery, the amount of income needed to move out of relative poverty has risen too.

In this briefing note, we exclusively look at measures of poverty that use incomes measured after housing costs are deducted ("AHC"). The government also releases poverty statistics using incomes measured before housing costs are deducted ("BHC"). We use AHC measures for low income people, measuring poverty AHC is likely to provides a better reflection of their material living standards. This is discussed in more detail on page 97 of Cribb et al (2018)[2].

Table 1 shows the levels of weekly net household income after housing costs that different sized households require to avoid being classified as in absolute or relative poverty. These threshold income levels vary across household types because income is adjusted to account for household size and composition.

[2] Cribb, Norris Keiller and Waters (2018) 'Living Standards, Poverty and Inequality in the UK: 2018', IFS Report R129

**Table 1. Cash values of poverty lines for example families in 2017–18 (£ per week)**

| | Childless couple | Single adult | Lone parent, one child | Couple, one child | Couple, two children |
|---|---|---|---|---|---|
| **AHC** | | | | | |
| Absolute poverty line | 247 | 143 | 193 | 296 | 346 |
| Relative poverty line | 262 | 152 | 204 | 314 | 367 |

Note: Incomes have been measured net of taxes and benefits and after housing costs have been deducted. The children in these example families are assumed to be aged 13 or younger. For families with older children, the poverty lines are slightly higher. The absolute poverty line is defined as 60% of median income in 2010–11 and the relative poverty line as 60% of median income in 2017–18.

Source: Department for Work and Pensions (2019)