Technical briefing: What will the latest poverty data tell us?

Date: 30 June 2014

Introduction

On 1st July the latest data on poverty will be published by DWP; it is the only government endorsed measure of household income. This paper outlines what NPI expect the forthcoming data to show and the factors affecting the poverty level, along with an explanation of the methodology. It accompanies a shorter press briefing.

Data note: The data in this report refers to income before housing costs (BHC). NPI prefer the after housing costs (AHC) measure, but we use BHC here for two reasons. First it is the headline measure used by the government in its child poverty targets. Second an AHC estimate requires assumptions on housing costs and housing benefit that would reduce the reliability of our estimates. More information on the methodology is contained at the end of this paper.

Background

Income is made up a number of elements (earnings, benefits, investments etc) and a fall in one could be countered by a rise in another. The Family Resources Survey provides the only comprehensive picture of how changes in all income sources affect how much the typical UK household has to spend. The findings from this survey will be published on Tuesday 1st July.

The data published last year was for 2011/12. It showed that 2011/12 was the second year in a row that household income fell in real terms (prices grew faster than income). The drop meant that real incomes had fallen back to the level they were at a decade earlier.

It also showed that 16% of people in the UK were in poverty (measured before housing costs). A household is defined as in poverty if their net income is below 60% of the average (median) in that year. As the average income fell in 2011/12 the poverty threshold also fell. In 2011/12 incomes at the bottom of the distribution fell by about the same amount as those in the middle, so the poverty rate was unchanged.

Factors that influence income and poverty

The tables below summarises the main economic and policy changes that that affected household incomes in 2012/13 and 2013/14. The forthcoming data will reflect 2012/13, a year when inflation was at 2.7%, earnings increased by 1.3% and benefits by 5.2%.

The under-occupation penalty, cuts to council tax benefit, the overall benefit cap and the 1% benefit uprating were introduced in April 2013. This was also the year that the Personal Tax Allowance increased by £1,335 (double the increase in the previous year), inflation fell to 2.2% and the employment rate continued to increase. The data for this period (2013/14) will not be released until after the general election.

![npi logo]

*Changes in the economy and policy affecting household income*

Factor	Change in 2012/13 in forthcoming data	Change in 2013/14 not in forthcoming data
Prices (CPI inflation)	+2.7%	+2.2%
Employment rate (age 16-64)	+1.2 ppts	+0.7 ppts
Earnings (average pay)	+1.3%	+1.1%
Tax (personal tax allowance)	+£630pa	+£1,335pa
State Pension	+5.2%	+2.5%
Tax credits and child benefit	no change	no change
Means-tested benefits	+5.2%	+1%
Council Tax Benefit	No change	-£2.70pw (2.3M families)
Housing benefit (social rented sector)	No change	-£14.32pw (0.5M families)
Overall benefit cap (workless families)	No change	-£50pw (28k families)

NB: Figures are the annual change to the mid-point of 2012/13 and 2013/14.

Estimates for 2012/13

NPI have modelled these changes to estimate how in combination they have impacted household incomes and poverty. More detail on the methodology and reliability of these figures can be found at the end of this paper.

We expect the 2012/13 data to show that after accounting for changes in prices, the median household income in the UK did not change. This would mean the typical income for a couple household was £440 per week (net of tax, but including earnings and benefits).

Median household income in the UK (before housing costs)
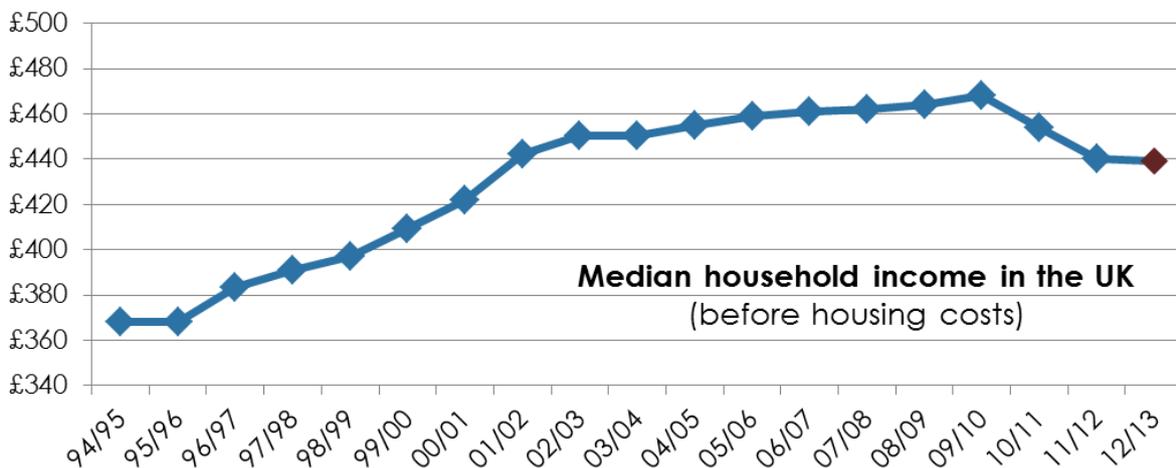
Income at the bottom of the distribution was also unchanged and we expect the **poverty rate to have remained at 16%**. The number of people in poverty in the UK however would be slightly higher (by about 100,000) as the overall population grew.

The table below shows NPI's modelled estimates of the number of people in working and non-working families in poverty in 2012/13; and how it has changed over the year.

- The number of people in poverty in *pensioner* families was just under 2 million (or 15%) around 80,000 lower than the previous year.

- The number of people in *full-working* families[1] was half the number in pensioner families at 1 million (or 4%), unchanged since the previous year.

- The largest group in poverty are the 3.7 million in *part-working* families[2], 280,000 higher than the previous year. More than 1 in 5 people in part-working families were in poverty in 2012/13.

- Around 3.2 million people in *workless families* were in poverty in 2012/13, 120,000 fewer than the previous year. At a level of 40% it is almost double the poverty rate for all other groups.

Family work status	People in poverty	Annual change	Poverty rate	Annual change
Pensioners	1.98M	-80,000	15%	-0.6pt
Full working	1.03M	15,000	4%	0.0pt
Part working	3.69M	280,000	22%	1.1pt
Not working	3.21M	-120,000	41%	-0.2pt
Total	9.91M	100,000	16%	0.0pt

One of the long-standing trends in poverty data is the growing share of people in poverty that belong to a working family. We expect this trend to have continued in 2012/13. Excluding those in pensioner families, in 2012/13 60% of people in poverty lived in a working family, 2 percentage points higher than the previous year.

How can changes in the economy and policy explain these expected changes in poverty?

Poverty among **pensioner families** fell slightly so the income of poorer pensioners grew at a faster rate than the median. This is likely to be due to the uprating of state pension of 5% (above the 3.1% increase in prices and 2.9% increase in median income).

The number of workless families in poverty fell but the poverty rate among **workless families** hardly changed. The number fell because the increase in employment meant that there were fewer unemployed families. But the poverty rate was flat because the incomes of workless families (largely made up of benefits which increased by 5%) rose in line with the median income.

For **full-working families** there was very little change in the number in poverty or the poverty rate. As people in full-working families account for 40% of the population, their income heavily influences the median (and also the poverty line). The main factors affecting the income of this group were the changes in earnings and the personal tax allowance. The unchanged poverty rate suggests that full-working families at the bottom of the income distribution benefited as much from these changes as those in the middle.

ONS data on workless households shows that much of the increased employment in 2012/13 caused a shift in people from workless families towards **part-working families** (rather than full-working families). With a poverty rate of 22% this also meant the number of people in part-working families in poverty rose.

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[1] Families where all adults are in work and at least some of this work is full-time (excludes all families containing someone that is self-employed)
[2] Families where not all adults are in work or the only work done is part-time (includes all families containing someone that is self-employed)

But some of the rise in the number of people in part-working families in poverty is linked to the increased poverty rate. This is likely to be the result of a combination of factors. Tax credits which were frozen make up a larger share of the income of part-working families than full-working ones. Plus their earnings and the tax liability will be lower so they benefit comparatively less from increased earnings and the personal tax allowance.

What about 2013/14?

April 2013 was when the main benefit cuts took place (the 1% up-rating, cuts to council tax benefit, the under-occupation penalty and the overall benefit cap). It is also when the personal tax allowance went up by more than £1,325 and when the economic indicators started to look promising. Unlike 2012/13 when we expect the poverty rate did not change, in 2013/14 the numbers are likely to have shifted.

Given the increase in the personal tax allowance, it's likely that median incomes started to increase in 2013/14 (but not at the same rate in which they fell). But the poverty rate could have increased also. The cuts to benefits have a greater impact on those at the bottom of the income distribution. Likewise an increase in earnings and the tax allowance impact on low-earner families. It's plausible that as incomes in the middle start to increase, those at the bottom continue to fall.

The data for 2012/13 is the last to be published before the general election. But it will only show how the first half of the Government's term affected household income, not the second and these two halves are very different. Unfortunately, the data that shows us how the main benefit cuts and the return to growth have affected households will not be published until after polling day.

Data note

Our expectations of the poverty figures are based on a model developed by NPI. It estimates income and poverty levels for 2012/13 based on the 2011/12 poverty data. This data has been adjusted to account for changes in a range of factors that affect household income. It has been tested on previous years of data produced an accurate estimate of median income and the poverty rate for different family types (the figures presented in this paper).

However, certain additional assumptions apply for 2012/13 which we're not required for earlier years. Here we list the main assumptions that have been made to apply the model to 2012/13 and their possible impact on the figures.

Inflation: the level of inflation used by DWP to calculate *real* median incomes is bespoke – it is based on RPI with a slight variation. This inflation level is published with the income data. For the model NPI assumed that DWP will use the inflation rate of 3.1%. The level of inflation impacts how household incomes have changed in real terms. NPI expect that the median income was unchanged in 2012/13. A higher level of inflation than our estimate would result in a real terms decrease in median income and a lower level of inflation would result in an increase.

Personal Tax Allowance: the increase in the personal tax allowance meant the model required an additional component to account for its impact on households incomes. As 2012/13 was the first year that it occurred we have been unable to "road test" this aspect of the model on data from earlier years. The change in the personal tax allowance will have influenced the median income level.

Grossing: the model adjusts the 2011/12 data to account for the annual growth in the number of households in the UK (based on DCLG household estimates). However, DWP

have altered their grossing methodology for 2012/13 to align it to Census estimates. NPI's model is based on the pre-census household estimates. Whilst grossing affects the overall number of people in poverty and the rate, we do not expect it to affect the year-on-year change.

The remainder of this section outlines the other adjustments made to the 2011/12 data to produce the expected numbers for 2012/13. These have been applied in the same way to earlier years of data and found to produce accurate results.

Employment: Adjustments to the level of employment were based on the *Working and Workless Households*, ONS publication derived from the Labour Force Survey household datasets.

Benefit income: Adjustments to the level of benefit income was based on changes in entitlement to different benefits from April 2012.

Earnings: Adjustments to the level of earnings were based on the ONS *Annual Survey of Hours and Earnings*.

Housing costs: the model does not currently consider income after housing costs. This would require further assumptions on changes to housing costs and the value of housing benefit. To calculate before housing costs income it was assumed that housing benefit increased at the same rate as other benefit income. Tests on earlier years of data suggest that this is a sufficient proxy.