

Squeezed Britain



The annual audit of low to middle income households



Income & Work

Household Finances

Housing

Future Prospects

Resolution Foundation

The Resolution Foundation is an independent think tank that aims to improve the lives of households on low to middle incomes (LMIs). This annual report sets out the economic position of the group using the latest large-scale survey data available and assesses their future prospects over the coming decade.

A longer version of this publication, with a wealth of additional and more detailed information, is available to download from our website: www.resolutionfoundation.org

A list of sources can be found at the end of this publication. Roman numerals accompanying the data and text identify the relevant sources.

Introduction

The last year has been one of the most difficult in living memory for Britain's households. The recovery has been faltering, few have enjoyed a pay rise, the cost of living has spiked and the government has introduced a major programme of cuts.

As a result, living standards have fallen for most groups in society. Here we focus on one group that has been particularly hit - those in work but below middle income. With an average household income of only £20,500 after tax, theirs is a daily struggle to keep up with the rising costs of essentials and to meet goals such as saving or buying a home.^{viii}

The roots of this story of squeezed Britain reach back before the recession. Wages have been flat for the typical worker since 2003.ⁱ Even before then, those in the bottom half of earnings did not share fully in the fruits of growth. The gap between them and higher earners has been growing for decades. Rising tax credits have helped boost living standards even in the face of stagnating wages. However, since April many families are feeling the squeeze more acutely as cuts start to bite.

The squeeze on living standards looks set to continue, leaving low to middle income Britain struggling to keep its head above water for some years to come.



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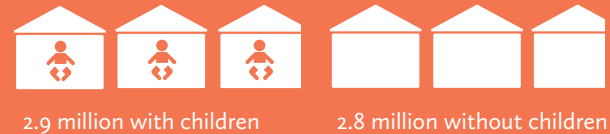


Who's in Squeezed Britain?

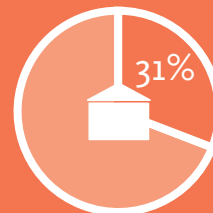
This report focuses on a group that makes up nearly one third of working-age households in Britain. Overwhelmingly in work, these households nevertheless manage on relatively modest incomes, leaving them susceptible to something as simple as an unexpectedly large fuel bill. While the most affluent households have seen a steady improvement in their incomes, low to middle income (LMI) households have seen only small gains since 2003. Many households move in and out of the LMI group from one year to the next but around a third remain 'stuck' over the longer term, finding themselves in the group over a 15 year period.

Households on low to middle incomes are defined by the Resolution Foundation as those of working age and living largely independent of the state but with incomes below the median (middle) in the UK. The definition excludes the poorest 10% of households and those who receive more than one fifth of their gross household income from means tested benefits, who we define as 'benefit reliant'. In practice, our definition of the LMI group includes a couple without children living on a gross annual household income of between £12,000 and £29,000, or a couple with two children on between £17,000 and £41,000. We define those above the middle as 'higher income'.^{viii}

Squeezed Britain at a glance



5.8 million households^{viii}



proportion of working-age households on a low to middle income^{viii}



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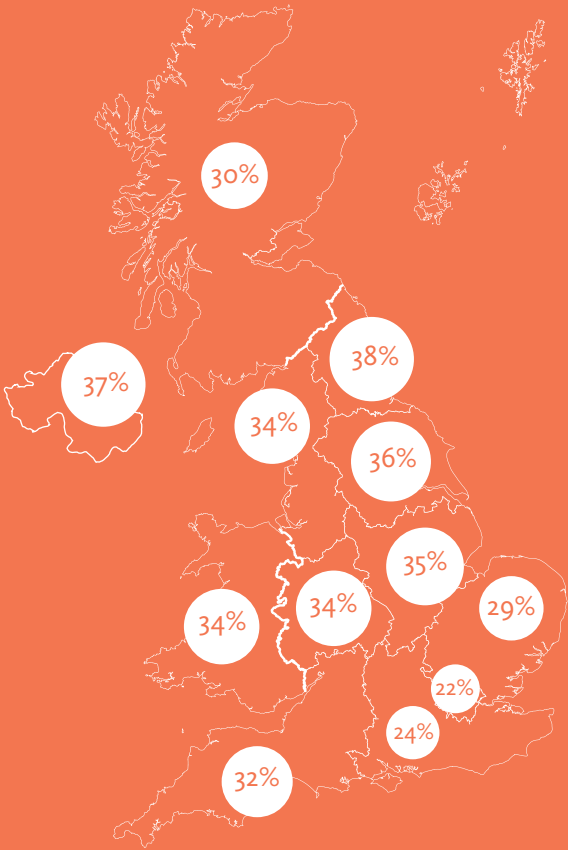


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Future Prospects

WHO LIVES WHERE? PROPORTION OF LMI
HOUSEHOLDS IN EACH REGION (UK 2009-10) ^{viii}



LMI in work ^{viii}



average net
income of an
LMI household ^{viii}



63%
own their
home ^{viii}



21%
rent
privately ^{viii}



16%
social
housing ^{viii}



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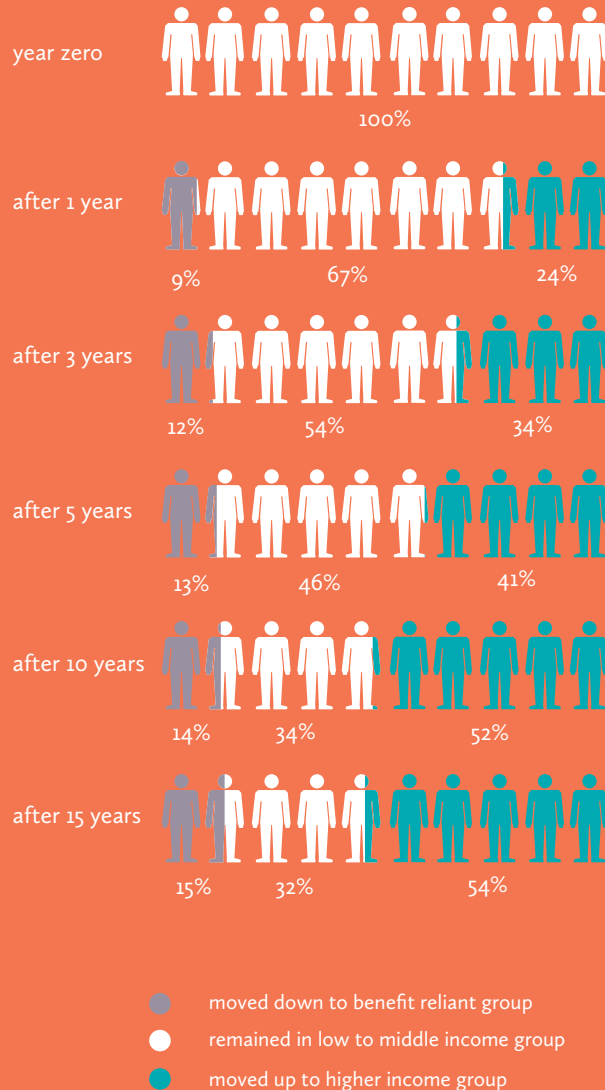


Housing



Future Prospects

WHO STAYS? HOW LONG DO HOUSEHOLDS STAY IN
THE LMI GROUP? (GB, AVERAGE 1991-2008) ¹¹



“I’m working 7 days a week to make ends meet because my wages haven’t gone up but everything else has. I don’t enjoy life anymore because I’m working all the time.”

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Household Finances



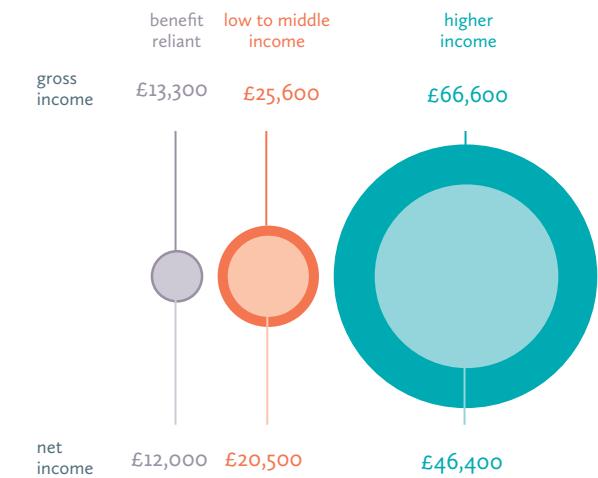
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Future Prospects

Wages are the single biggest component of household income for the LMI group. As such, stagnating wages for the bottom half of earners have put great pressure on household incomes in recent years. Meanwhile, wages in the top half, especially at the very top, have continued to grow, causing an ongoing rise in earnings inequality. Tax credits and rising women's employment helped prop up household incomes for the LMI group in the 2000s, at the same time as income from men's employment fell significantly. Recent and future cuts in tax credits will leave LMI families stretched, while high childcare costs continue to be a barrier to parents working longer hours to maintain their living standards.

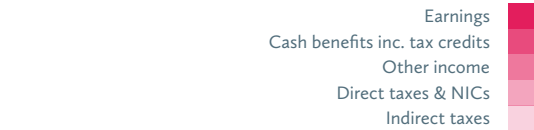
TYPICAL INCOMES: AVERAGE HOUSEHOLD INCOME BEFORE AND AFTER TAX (UK 2009-10) ^{viii}



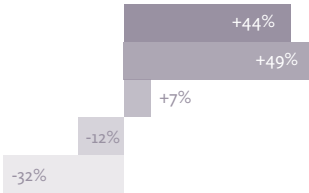
Real household incomes for the LMI group were broadly the same in 2010-11 as they were back in 2001-02.^{viii} This is in part because wages fell sharply during the downturn. A typical LMI worker saw a 4.2% real terms decline in earnings between 2010 and 2011.ⁱ But it also reflects a longer term trend. Men on below average earnings have seen their real wages decline since 2003.ⁱ With wages at the top continuing to grow, LMI workers have been falling further behind higher earners in relative terms. This has contributed to a 30 year decline in the share of national income going to workers in the bottom half. Prior to the 2008 recession, only £12 of every £100 of national income was paid as wages to the bottom 50% of workers compared to £16 in 1977. By contrast, the top 10% of earners took home £14 of every £100 of national income in 2008, more than the entire bottom half.^{i, xviii}

WHERE DOES THE MONEY COME FROM?

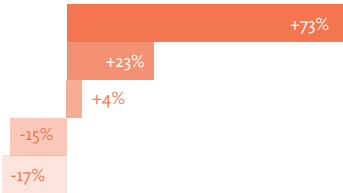
COMPONENTS OF GROSS HOUSEHOLD INCOME
(UK 2009-10) ^{xx}



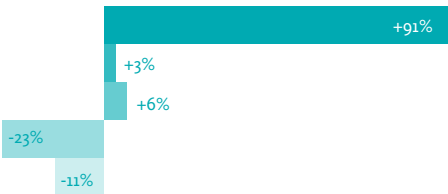
Benefit reliant



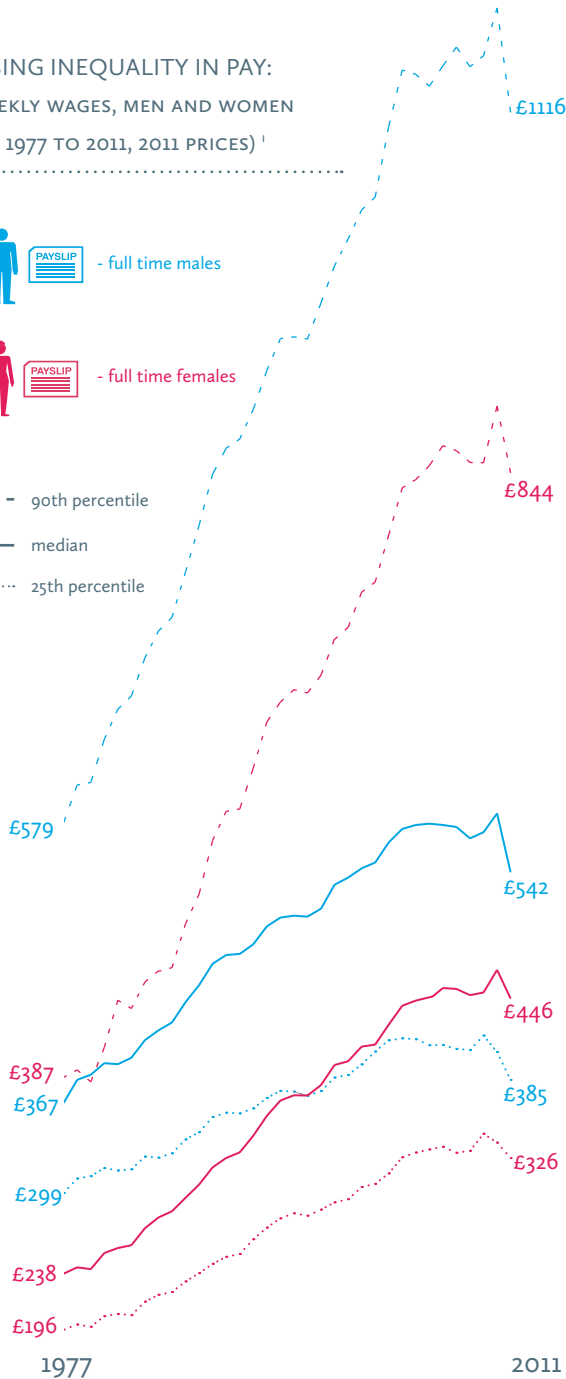
Low to middle income



Higher income



RIISING INEQUALITY IN PAY:
WEEKLY WAGES, MEN AND WOMEN
(GB 1977 TO 2011, 2011 PRICES) ¹



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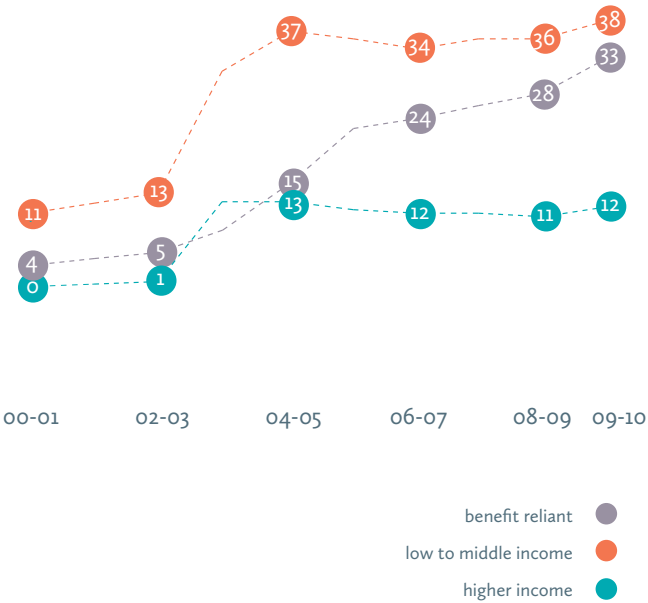
Housing



Future Prospects

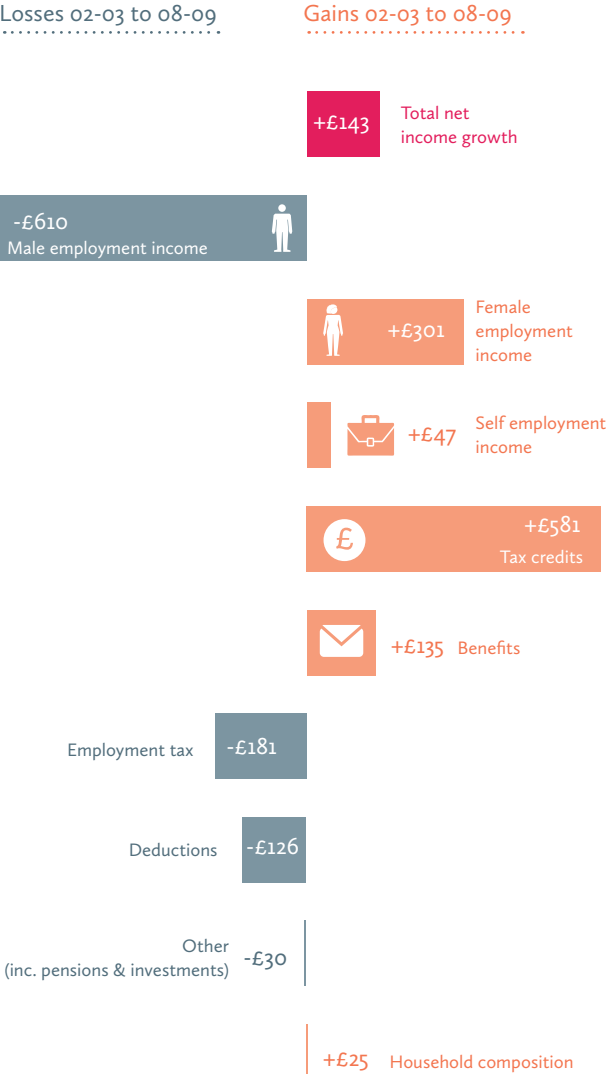
The LMI group is the largest recipient of tax credits, reflecting their position in work but on relatively low incomes. Tax credits have played an increasingly important role over the 2000s in propping up the incomes of LMI households in the face of stagnating wages. Analysis by the Institute for Fiscal Studies shows that tax credits contributed an additional £581 to the income of the average LMI household between 2002-03 and 2008-09.^{xiv}

KEY SUPPORT: PROPORTION OF FAMILIES RECEIVING TAX CREDITS (% , UK 2000-01 TO 2009-10)^{viii}



WHERE DID INCOME GROWTH COME FROM?

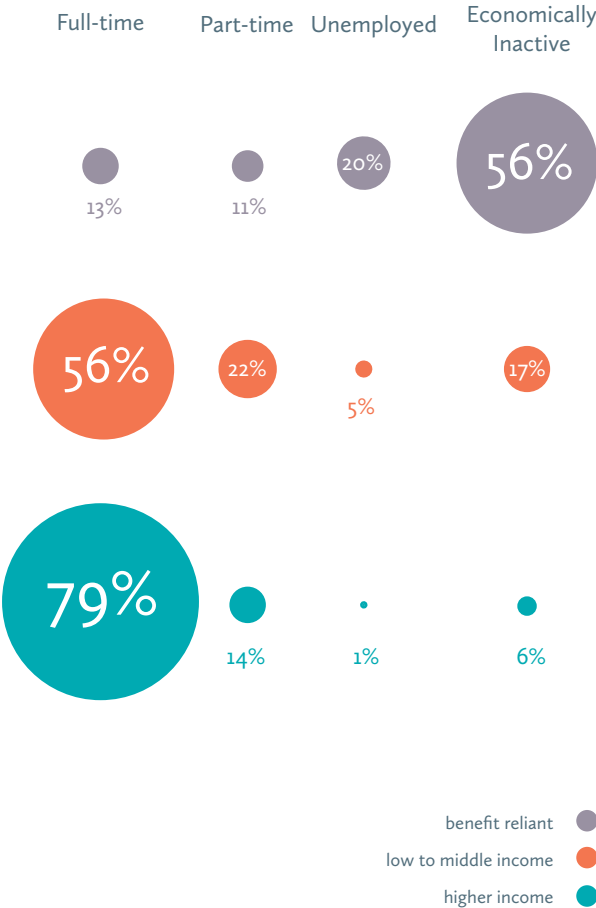
CHANGES IN THE COMPONENTS OF AVERAGE LMI HOUSEHOLD INCOME (UK 2002-03 TO 2008-09, 2008-09 PRICES)^{xiv}



The vast majority of LMIs are in work of some form, although a higher proportion work part-time than in the higher income group.

In recent decades there has been a shift in employment from men to women. Among LMIs the proportion of women employed is now higher than the proportion of men. This is partly because men are more likely to be self employed but also because the unemployment rate for men in the group has jumped from just above 3% before the recession to nearly 7% now.^{viii} As a result from 2002-03 to 2008-09 the average LMI household lost £610 of income from male employment and gained £301 from female employment.^{xiv}

PATTERNS OF WORK: ECONOMIC ACTIVITY AMONG ADULTS (UK 2009-10) ^{viii}



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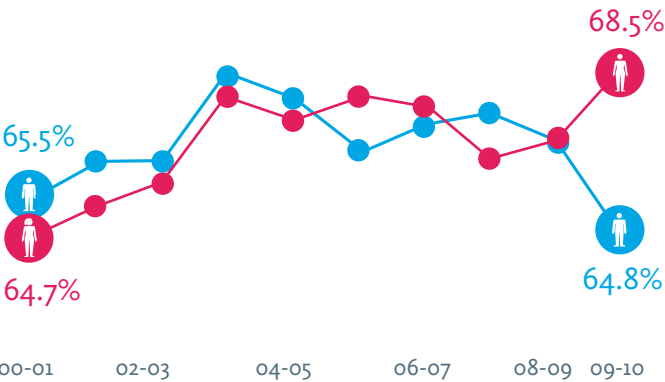
Housing



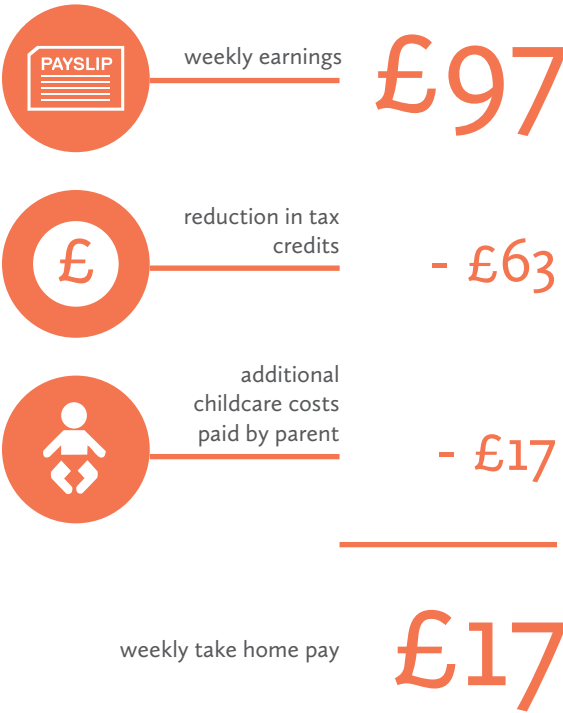
Future Prospects

One third of women in the LMI group work part-time compared to one quarter in the higher income group. This is, in part, because childcare in the UK continues to be very expensive by international standards, even more so since the 2011 cut in support for childcare costs. This means that second earners on low wages with children take home a smaller proportion of their pay than in almost all other OECD countries. The introduction of Universal Credit in 2013 will for the first time provide support for childcare to those working fewer than 16 hours a week. However, it will create even greater disincentives for second earners with children seeking to work more than part-time who will lose more in tax credits as well as having to pay for childcare.

THE GENDER SHIFT IN WORK: PROPORTION OF LMI MEN AND WOMEN WHO ARE EMPLOYEES (UK 2000-01 TO 2009-10) ^{viii}



MAKING WORK PAY? WEEKLY TAKE HOME PAY UNDER UNIVERSAL CREDIT FOR A SECOND EARNER WORKING 16 HOURS AT THE MINIMUM WAGE (UK 2011-12 PRICES) ^{iv}



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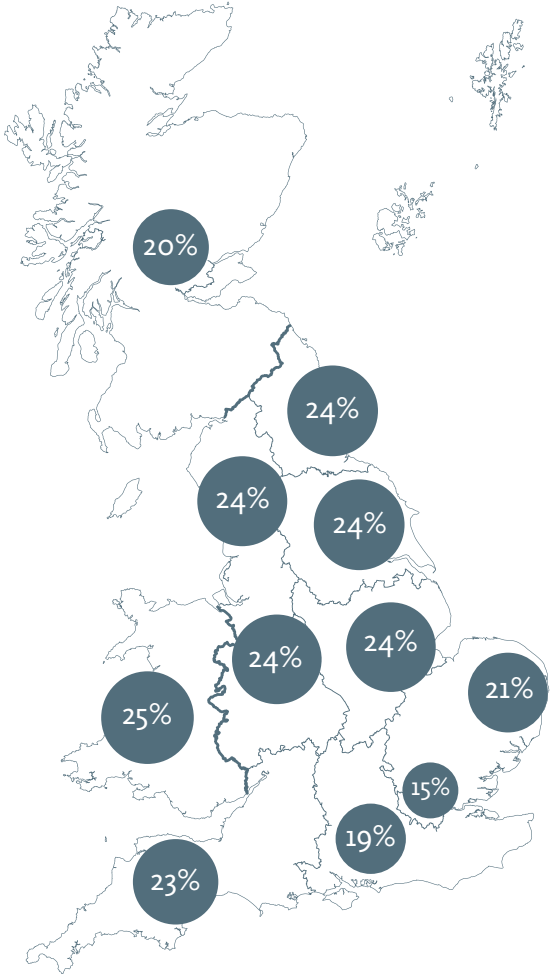
Future Prospects

Job insecurity and low pay are a pervasive feature of squeezed Britain. Low pay varies significantly by region: the South East, the North West and London all have more than half a million people earning less than the living wage (currently £8.30 an hour in London and £7.20 in the rest of the country).

Workers in the LMI group are concentrated in the retail, health and social care, manufacturing and construction sectors, while the higher income group is more evenly spread across industries. Retail has the third biggest gap between top and bottom pay of all UK industries and is also the sector with the largest number of workers paid below the living wage.¹



LOW PAY IN BRITAIN: PROPORTION OF WORKERS EARNING LESS THAN THE LIVING WAGE BY REGION (GB 2010)¹



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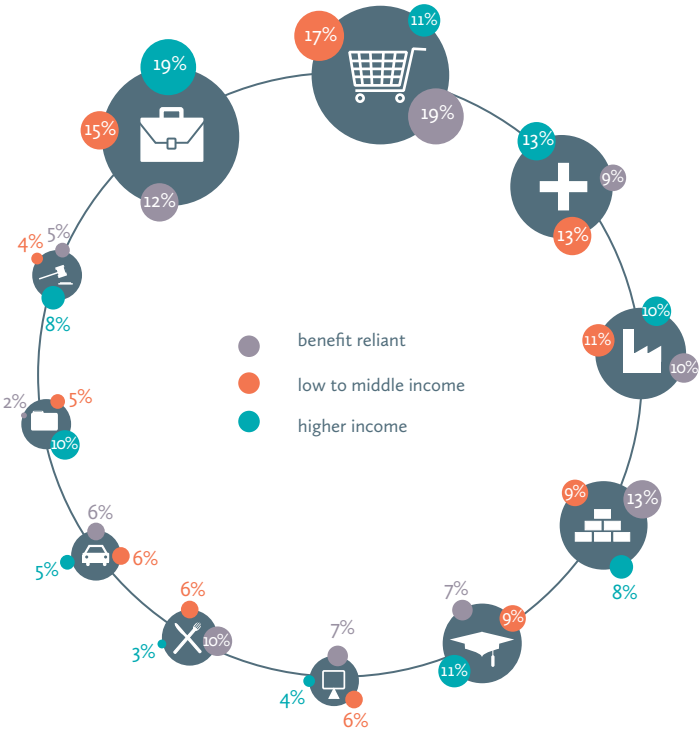


Housing



Future Prospects

WHO WORKS WHERE? PROPORTION OF JOBS IN EACH INDUSTRIAL SECTOR BY INCOME GROUP (UK 2009-10)^{viii}



Despite rapid growth in degree level education, LMIs remain much less likely to have a degree than those in the higher income group.^{viii} This matters because a greater supply of graduates has not dampened the positive effect of holding a degree on social mobility – indeed, the penalty for not holding a degree has increased over time. In both the 1990s and 2000s, those without a degree were much less likely to move up the earnings ladder during their thirties and more likely to move down than degree holders, all other things being equal.^{xii} This is compounded by the fact that those with higher levels of qualifications continue to be more likely to be offered education or training in work.^{xi}



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Household Finances

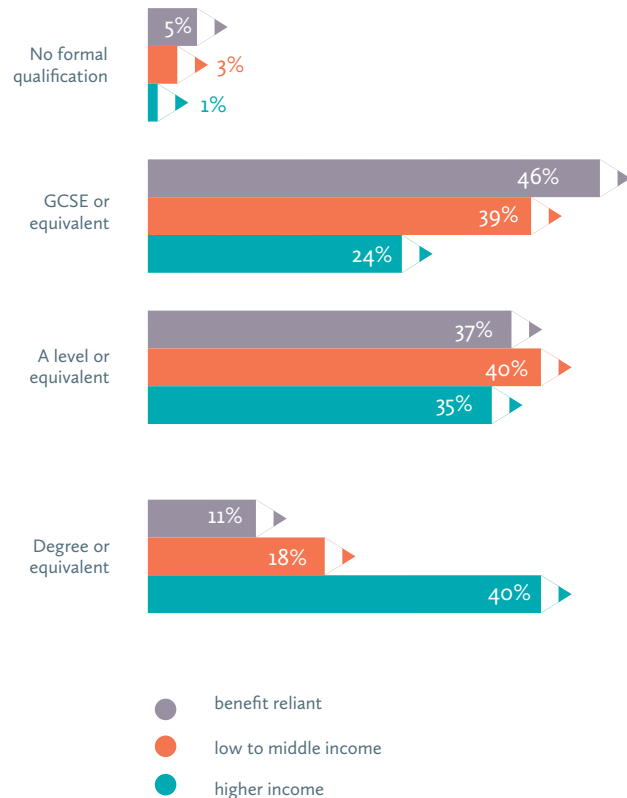


Housing



Future Prospects

KEY SKILLS: HIGHEST LEVEL OF EDUCATIONAL
QUALIFICATION AMONG ADULTS (UK 2009-10) ^{VIII}



“This year we’ve struggled more than ever. We’ve had less money so we haven’t been able to save. We just don’t feel prepared for any shocks that life might throw at us.”

Household Finances



Household Finances

Housing

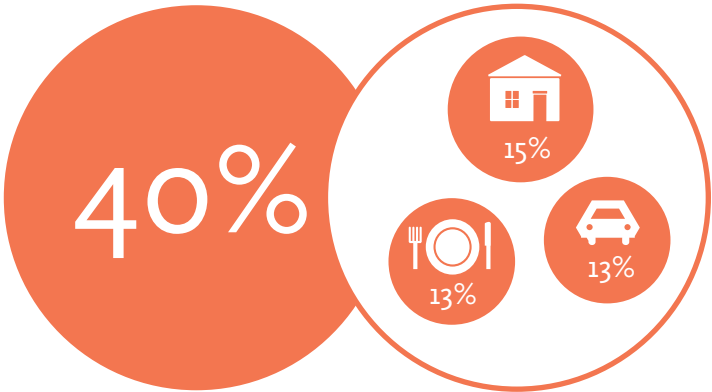
Future Prospects

Prices have risen significantly more quickly than earnings since the start of 2010. Despite an anticipated slowdown in inflation in the coming months, real wages are expected to fall until 2013, putting even more pressure on household finances. LMIs have faced a particularly tough time as the cost of their weekly shopping basket has risen faster than overall inflation. With limited savings to fall back on and a lack of credit availability, a growing number of LMIs have found themselves struggling to keep up with payments. Many have been forced to put off household repairs and holidays and are not managing to save.

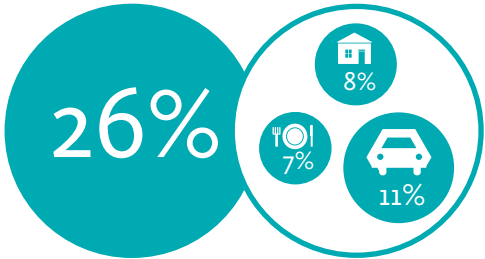




BURDEN OF ESSENTIALS: PROPORTION OF DISPOSABLE HOUSEHOLD INCOME SPENT ON ESSENTIALS (UK 2009) ^{xiii}

Low to middle income



Higher income



-  Housing and fuel
-  Food and drink
-  Transport



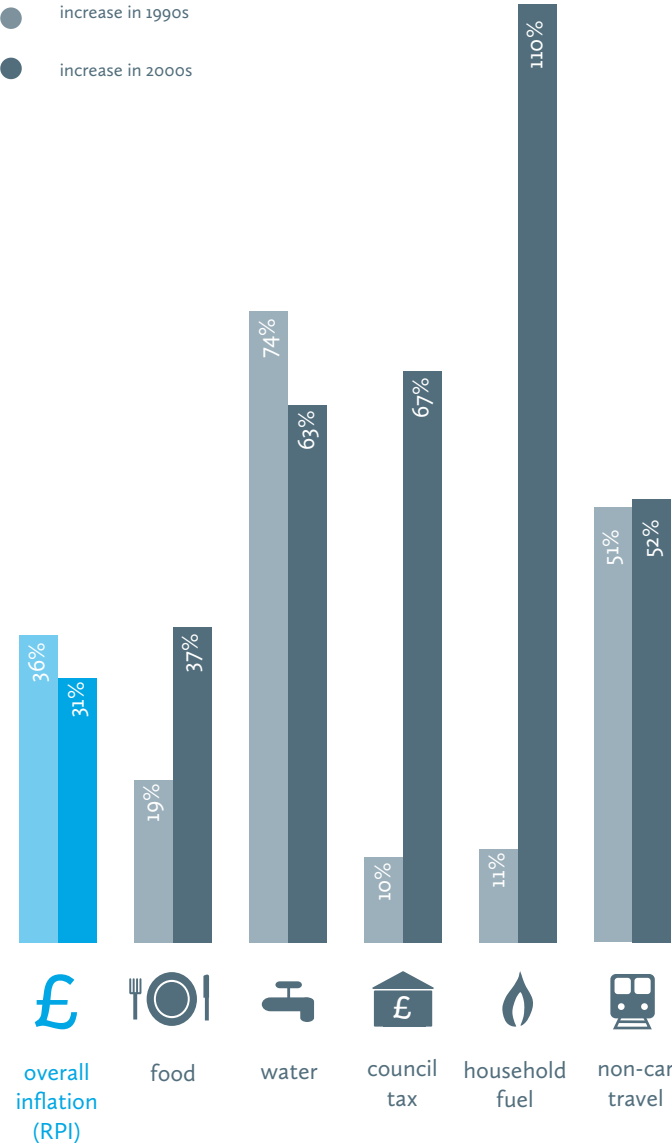
Household Finances

Housing

Future Prospects

LMI households spend a larger proportion of their household income on essentials such as food, fuel and transport than higher income households. The costs of these goods have risen much faster than inflation in the overall economy. The price of fuel, for example, went up by 110% in the 2000s compared to only 31% for overall inflation.^v Such patterns mean that LMI households have faced higher rates of inflation than those on higher incomes over the past decade, increasing the relative cost of their annual shopping basket by £427 in 2011.^{xiii} These cost pressures are taking their toll with 11% of the LMI group being behind with at least one household bill compared to 3% for the higher income group.^{viii}

COST OF LIVING PRESSURES: PRICE RISES BY CATEGORY OF SPEND (UK 1990 TO 2009)^v

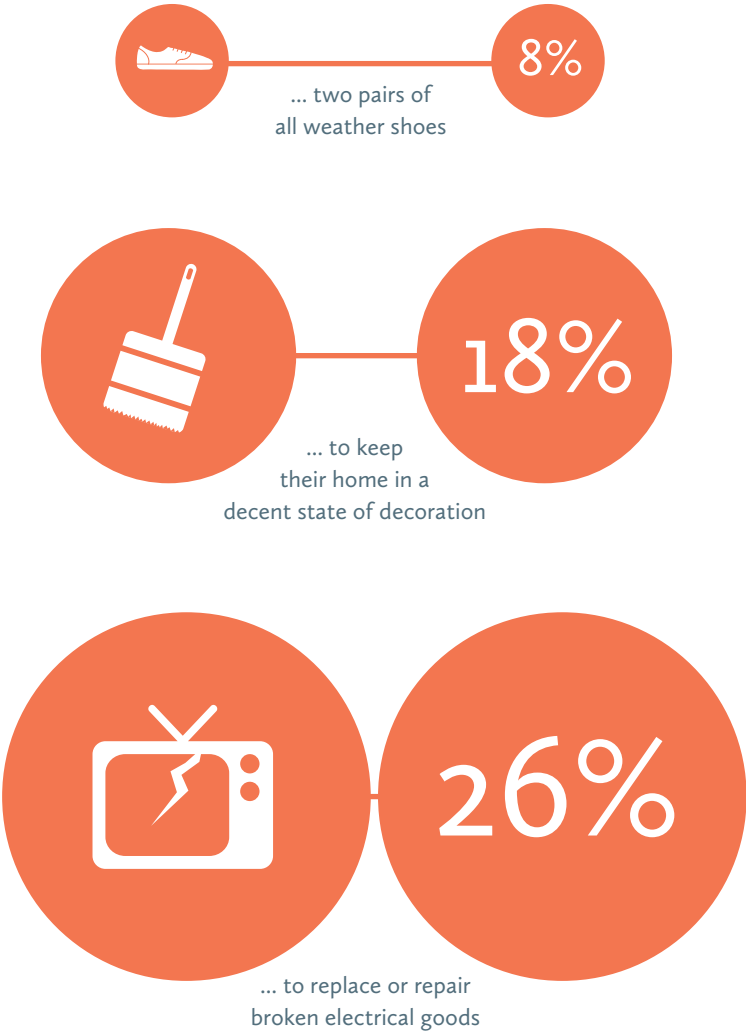


Household Finances

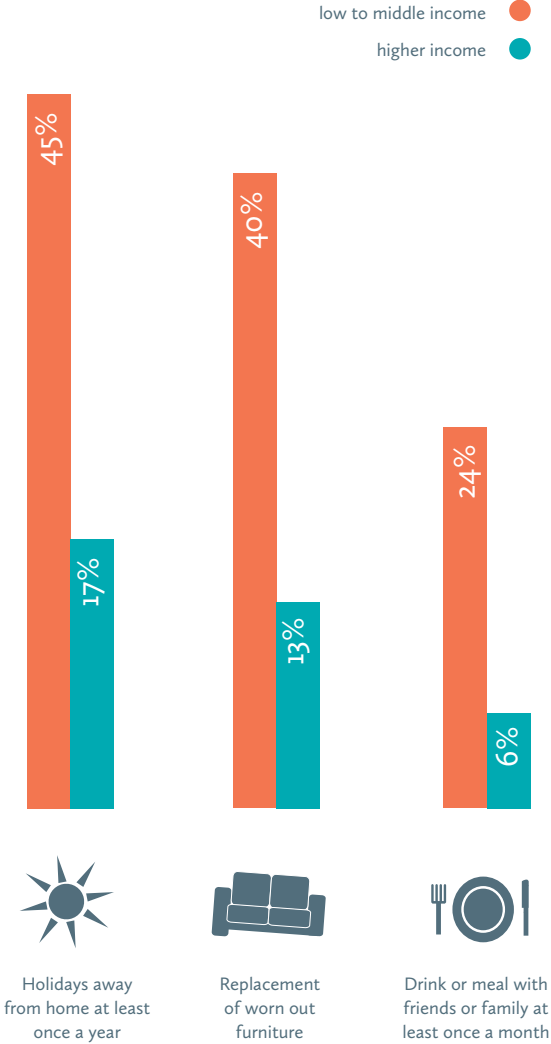
Housing

Future Prospects

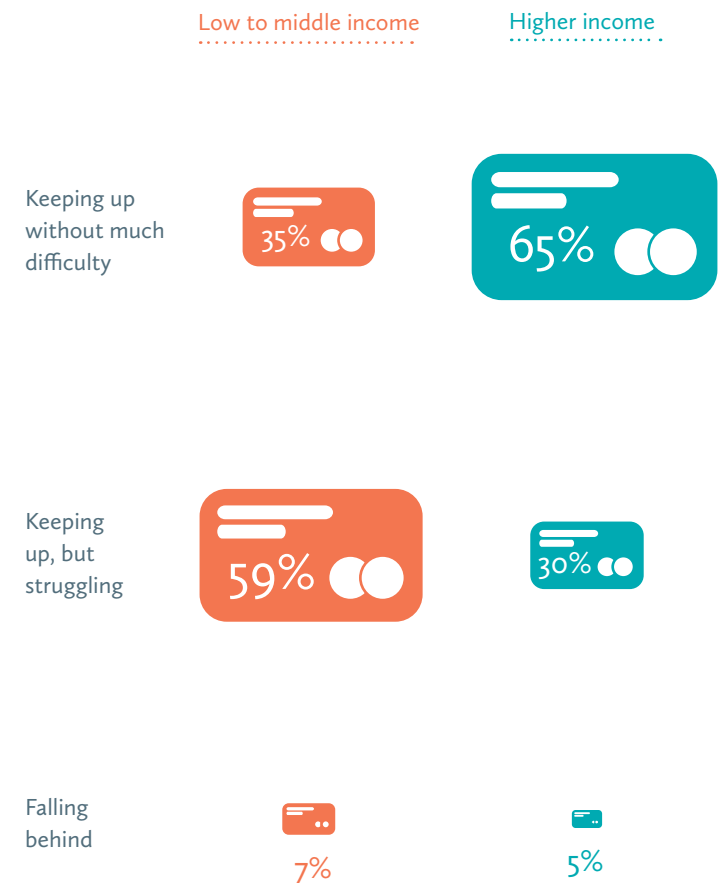
OUT OF REACH: PROPORTION OF LMIs WHO WOULD LIKE,
BUT CANNOT AFFORD... (UK 2009-10) ^{viii}



UNMET ASPIRATIONS: PROPORTION OF FAMILIES WHO WOULD LIKE, BUT CANNOT AFFORD... (UK 2009-10) ^{viii}



JUGGLING BILLS: HOUSEHOLDS' SELF-REPORTED ABILITY TO PAY BILLS & CREDIT COMMITMENTS (GB 2011) ^{xvi}



Credit and savings provide a vital economic cushion against unexpected household spending and major shocks such as illness or unemployment. LMIs are still finding it difficult to access credit - almost 50% say that it was harder to borrow in 2011 than it was in the previous year, and many are still suffering from the burden of debt.^{xvi} Two thirds of LMI households have limited savings on which to draw in an emergency and two thirds of adults in the group are not contributing to a private pension, putting them at risk of poverty in retirement and adding to Britain's growing wealth gap.^{viii}



Household Finances

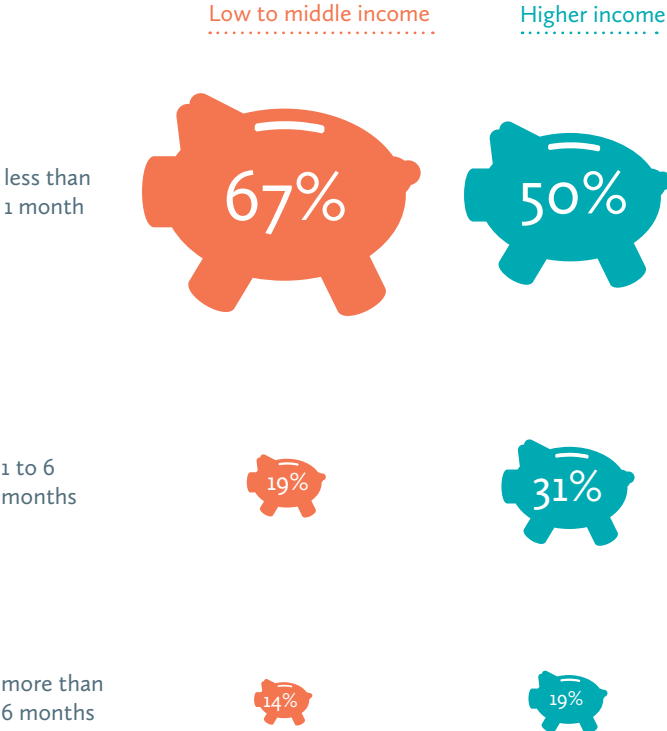


Housing

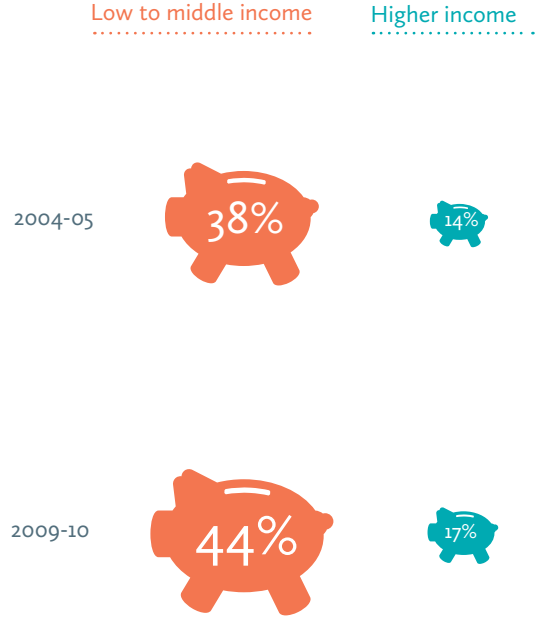


Future Prospects

SAFETY NET: NUMBER OF MONTHS' NET INCOME
HELD IN SAVINGS BY FAMILIES (UK 2009-10) ^{viii}



THE SAVINGS SQUEEZE: PROPORTION OF FAMILIES
WHO WOULD LIKE TO SAVE £10 A MONTH BUT
CANNOT AFFORD IT (UK 2004-05 & 2009-10) ^{viii}



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Future Prospects

SECURE RETIREMENT? PROPORTION OF ADULTS WITH
NO / FROZEN PERSONAL OR OCCUPATIONAL PENSION
(UK 2009-10) ^{VIII}

Low to middle income



Higher income



“Saving for a mortgage is just impossible. I try and work extra hours but the deposit you need these days is so big it feels like I’ll never own my own home.”

Housing



Housing



Future Prospects

Housing is a critical component of household living standards. It is the single largest household expense and is an important route to asset ownership. While the aspiration for home ownership remains strong, a radical shift is taking place in the housing market with LMI's under 35 finding it increasingly difficult to get on the housing ladder. With limited mortgage availability for first-time buyers, historically high house prices and stagnant wages, many in this group are finding themselves stuck in private rented accommodation. Meanwhile, those in the group who are already home owners face a precarious future as they contemplate the prospect of higher mortgage payments when interest rates eventually rise.



WHAT KIND OF HOME? HOUSING TENURE AMONG HOUSEHOLDS
(UK 2009-10) ^{viii}

Benefit reliant



Low to middle income



Higher income

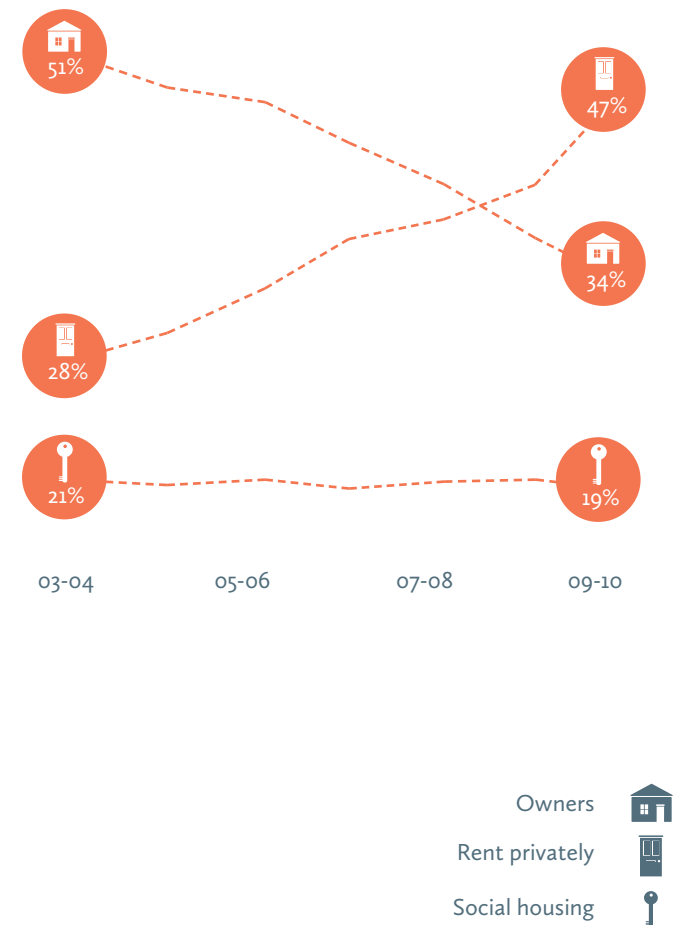


-  Owners
-  Rent privately
-  Social housing

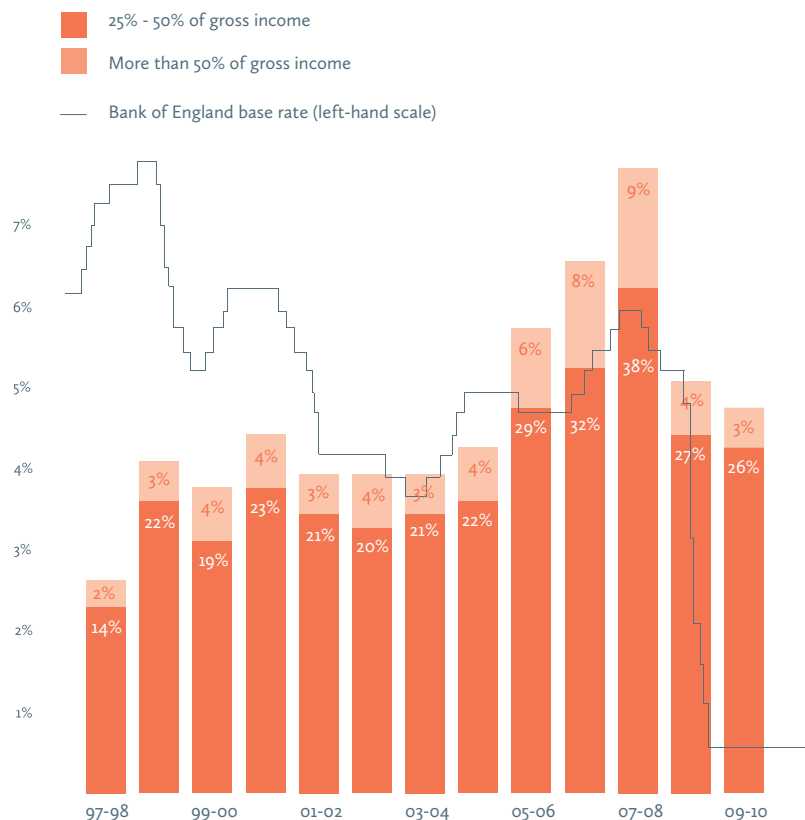


Overall, 63% of LMI households now own their home on a mortgage or outright, compared to over 70% 10 years ago, and 83% of higher income households now. However, among under 35s, the picture looks very different. The proportion of LMI households aged under 35 renting privately has more than tripled from 14% in the late 1980s to 47% now. In just the last six years the number of LMIs under 35 and owning a home has nose dived from 51% to 34%. Meanwhile, numbers in social housing have decreased slightly.^{vi, viii}

GENERATION RENT: CHANGE IN HOUSING TENURE FOR LMIs AGED UNDER 35 (UK 2003-04 TO 2009-10)^{viii}

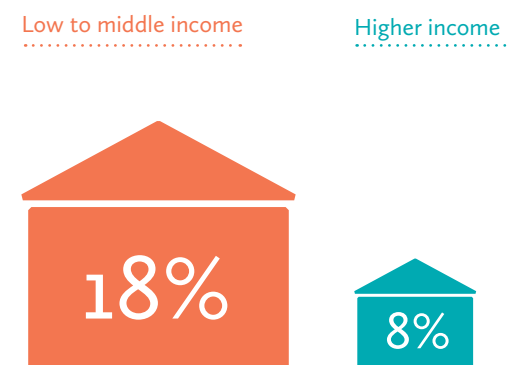


AN INCREASED BURDEN: PROPORTION OF GROSS INCOME ACCOUNTED FOR BY MORTGAGE PAYMENTS AMONG LMI OWNERS (ENGLAND 1997-98 TO 2009-10)^{vii}

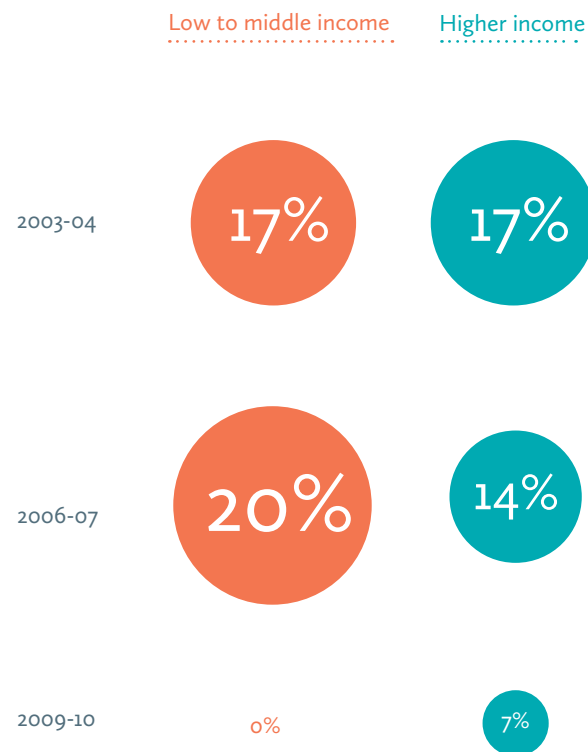


Mortgage payments make up a significant proportion of outgoings for LMI households - equivalent to more than 25% of income for over a quarter of those LMI households with a mortgage, and equivalent to over 50% of income for a further 3%.^{vii} Housing costs also became a greater burden for tenants over the 2000s. Private sector rents increased by a third in real terms between 1999-00 and 2009-10.^{viii} As a result, around one fifth of LMI households are struggling to keep up with the costs of a mortgage or rent.^{xvi}

THE HOUSING SQUEEZE: PROPORTION OF HOUSEHOLDS STRUGGLING TO PAY FOR ACCOMMODATION (GB 2011)^{xvi}



AN END TO EASY CREDIT: PROPORTION OF FIRST TIME
BUYERS USING A 100% MORTGAGE (ENGLAND 2003-04
TO 2009-10)^{vii}

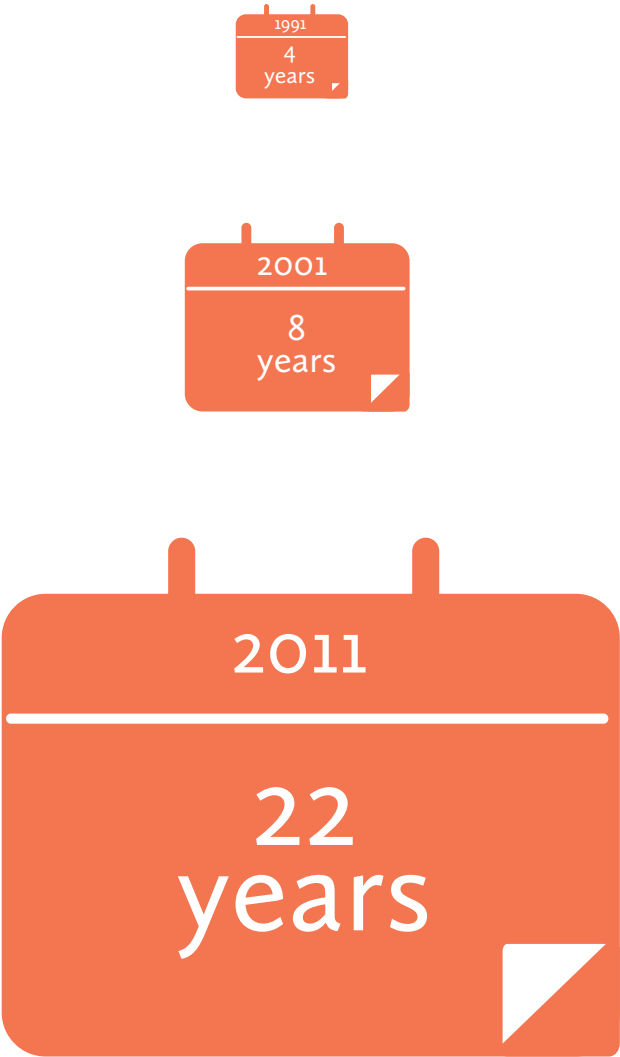


Part of the reason for this heavy burden of mortgage payments is the number of first-time buyers in the LMI group who bought with a high loan to value mortgage prior to the credit crunch. 20% bought with a 100% mortgage in 2006-07.^{vii} The availability of high loan to value mortgages has since tailed off, with no LMIs being able to access 100% mortgages in 2009-10. An LMI household would now have to save for 22 years to accumulate a deposit for the average first home, compared to just 3 years in 1997. It would take even longer for those who live in London.^{iii, ixvi, xx}

The number living in the private rented sector for longer periods of time is climbing as many resign themselves to never becoming a home owner. For those who do rent privately, the picture is one of increasingly short supply, rising prices and frequent dissatisfaction with issues from security of tenure to contract charges. 8% of LMI tenants are now behind with their rent. 10% say they are dissatisfied with their current private rented accommodation and over a quarter disagree that the private rented sector is a 'good tenure'.^{vii}



THE DISAPPEARING LADDER: TIME TAKEN FOR THE
AVERAGE LMI HOUSEHOLD TO SAVE FOR A TYPICAL FIRST TIME
BUYER DEPOSIT (UK 1991 TO 2011) ^{III, IXVI, XX}



SHUT OUT: PROPORTION OF NON-HOMEOWNER HOUSEHOLDS THAT
NEVER EXPECT TO BUY (ENGLAND 2009-10) ^{VII}

Benefit reliant



Low to middle income



Higher income

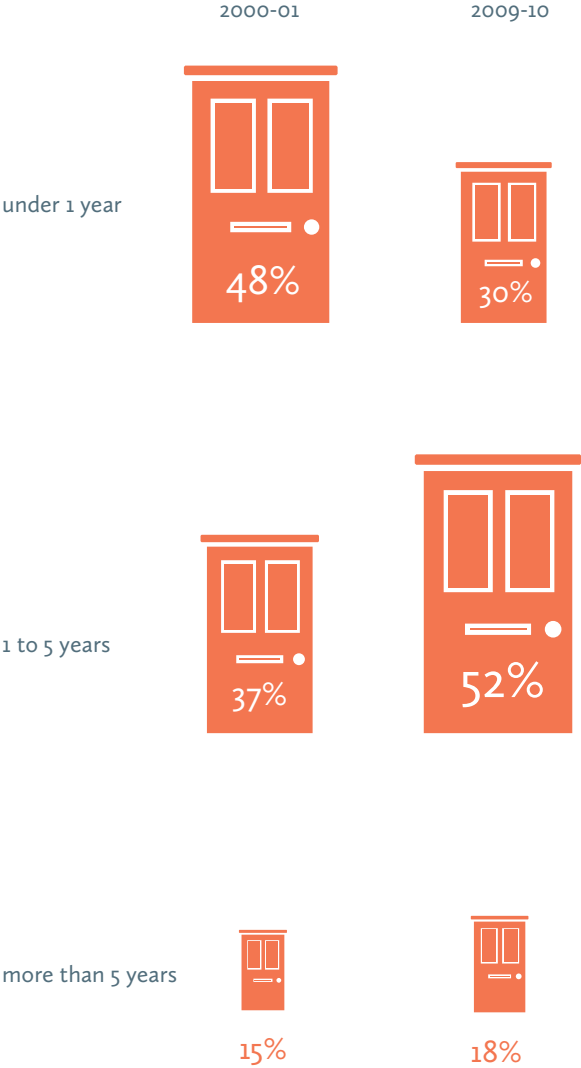


Housing



Future Prospects

MORE THAN JUST A STOP-GAP: LENGTH OF RESIDENCE
IN CURRENT PRIVATE RENTED ACCOMMODATION AMONG LMI
TENANTS (ENGLAND 2000-01 & 2009-10) ^{vii}



“My electric, my
gas, my food are all
steadily going up and
unfortunately my wages
aren’t going up to
meet that.”

Future Prospects

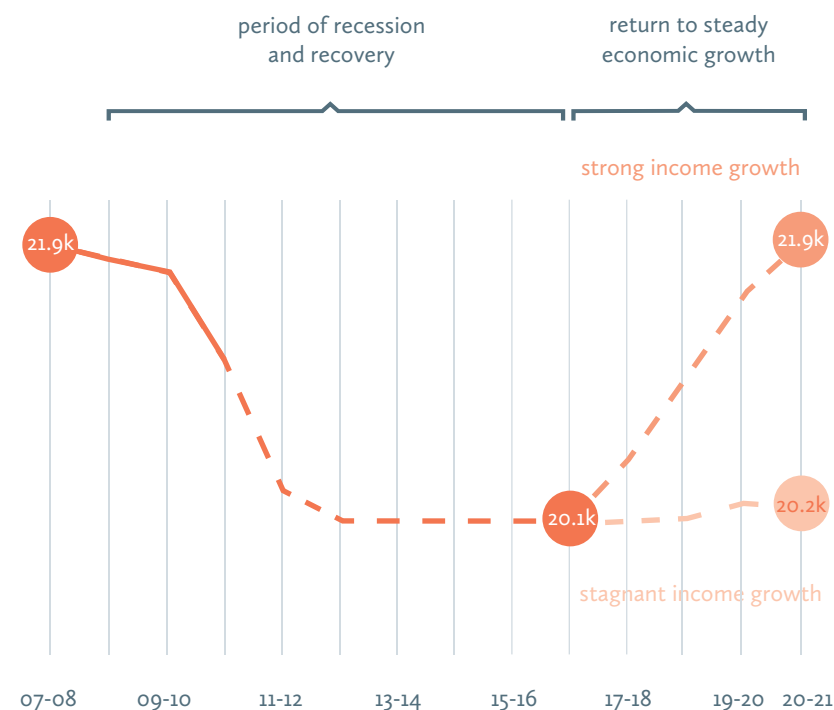


We have come through a deep recession but the nature of any future recovery remains highly uncertain. Moreover, projections of future growth in earnings and income indicate that a return to economic growth alone does not guarantee a bright future for Britain's 5.8 million low to middle income households.

In the immediate term, LMI households are experiencing a real terms decline in earnings of 4.2% in 2011-12, followed by an expected further fall of 1.2% in 2012-13. As the wage squeeze continues, LMI households are also expected to face a real terms loss of £457 million in tax credits in 2012-13 and a further £107 million in 2013-14. This is a cash loss to households. The projected government savings from these cuts are much greater because previous, more generous spending plans on tax credits have not been implemented.^{vi, viii, xix}

What will this continued squeeze mean for household incomes? Our analysis of projections published by the Office for Budget Responsibility (OBR) for wages, prices and government spending on benefits and tax credits suggests that incomes for the LMI group will continue to fall over the next year, flattening out in the period to 2016-17. From 2017 onwards, when steady economic growth is projected to return, we look at how the group will be affected under two different scenarios. In our 'strong income growth' scenario, we

WHAT KIND OF FUTURE? PROJECTIONS OF AVERAGE DISPOSABLE INCOMES IN LMI HOUSEHOLDS UNDER ALTERNATIVE SCENARIOS (UK 2007-08 TO 2020-21, £ 2010-11 PRICES)^{i, vi, viii, x}





assume that earnings and income grow in line with their trends in 1997-2003. Even under this optimistic scenario, the wages of a typical full-time male LMI worker would be lower in real terms in 2020 (£397 a week) than at their peak in 2003 (£416). Annual household incomes for LMIs would be no higher in 2020 (£21,900) than at their 2007 peak.^{I, VI, X}

In our 'stagnant income growth' scenario, we assume instead that wages and incomes grow at their 2003-2008 rates from 2017 onwards. In this scenario, a typical full-time male LMI worker would be earning just £372 a week in 2020, a real terms drop of 11% from a peak in 2003. By 2020, real household incomes for the group are projected to be 8% lower than their peak in 2007.^{I, VI, X}

Under both scenarios, the gap between LMIs and higher income households gets bigger, with the 'stagnant income growth' scenario resulting in LMI households becoming poorer in absolute terms. There are clearly difficult times ahead for LMIs both in the short and medium term. But this is also a central economic challenge - as a major part of the workforce, low to middle income Britain will have a critical part to play in driving any sustainable recovery. Policy makers anxious to promote a return to growth will need to address the underlying structural problems that caused the wages of ordinary workers to stagnate even when the economy grew. The severity of the decline in living standards faced by the group will take many years to reverse. This will keep the question of living standards high on the agenda long after 2012.



SOURCES

- I. Annual Survey of Hours and Earnings and New Earnings Survey 1977-2011, Office for National Statistics (UK/GB)
- II. British Household Panel Survey Waves 1-18, University of Essex, 1991-2008 (GB)
- III. CML Statistics, Table ML2, Council of Mortgage Lenders, 2011 (UK)
- IV. Donald Hirsch, Childcare support and the hours trap: the Universal Credit, Resolution Foundation, 2011 (UK)
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