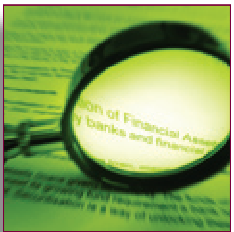
# Closer to Crisis?

## how low earners are coping in the recession



Resolution Foundation

## SUMMARY

This report shares the findings of the Resolution Foundation's project exploring the impact of the recession on low earning households – that is, those with below median income who remain broadly independent of state support. There are 14.3 million adults living in 7.2 million low earning households in the UK.[1] As a group low earners are squeezed: too poor to benefit from the full range of opportunities provided by private markets, but too rich to qualify for substantial state support.

The conclusions set out here have been developed through a mix of quantitative and qualitative work, with input from a series of expert seminars held in September 2009. Our ambition was not only to understand what impact the economic downturn was having, but also to develop some specific recommendations which we believe will support low earners through the recession and into recovery. Our findings show that:

**1. Low earners are more at risk of being hit by this recession than other groups**

Although the biggest increases in unemployment were initially in banking, since then rises in unemployment have been steeper in industries, occupations and areas where low earners are concentrated:

- Between Q2 and Q3 2009, output decreased by 1.0 per cent in the low earner sector of *distribution, hotels and restaurants*, compared to 0.1 per cent in the *business services and finance* sector.[2]
- People working in typical low earner occupations are more likely than higher earners to remain out of work for more than six months: among those leaving the JSA claimant count in May and June 2009, nine out of ten managers had been in receipt of the benefit for 26 weeks or less, compared with three quarters of people in elementary occupations.
- The unemployment rate in the West Midlands, which has the highest concentration of low skilled workers, increased by 1.1 percentage points between 2007 and 2008, compared to a 0.3 percentage point increase in the South East, which has the lowest concentration of low-skilled workers.

Low earners are more reliant on their earned incomes than benefit-dependent groups, and also less likely than higher earners to have a cushion of savings and insurance to fall back on – just under half of working-age low earners have less than a month's salary in savings. In the previous three recessions of the 1970s, 1980s and 1990s, incomes in the middle of the distribution fell by more than those at the bottom. There is further to fall this time round: out-of-work benefits are now worth 40 per cent of the poverty line, compared with 55 per cent just before the last recession for single people under the age of 25.[3] Similarly the out of work income for a couple with two children aged five and 14 is 67 per cent of the poverty line.[4]

**2. There are groups of low earners who are particularly exposed**

There are 14.3 million low earners in the UK, of who 9.4 million are of working age. Clearly this is a large and diverse group. Our analysis highlights which groups of low earners are particularly exposed to today's economic circumstances.

- The 7 million low earners with low skills levels[5]
  *Members of this group are more vulnerable to job loss than those with higher skill levels because they are easier and cheaper to dismiss and replace. They are also less likely to be offered in-work training. For those who do lose their job they are likely to take longer to return to the labour market than others with higher skills.*
- The 11.1 million low earners who were in poor financial health before the recession, and the 3.4 million low earners who were putting more than a quarter of their monthly income towards debt repayment in 2008
  *The recession has reduced the affordability and flexibility of existing credit, as well as limiting access to new credit and pushing levels of indebtedness for the low earning group up.*
- The 1.2 million low earners who have bought a home within the last decade
  *The recent drop in house prices puts the 340,000 low earner households who reported having a loan-to-value mortgage of more than 75 per cent at the end of 2008 at risk of negative equity, despite historically low interest rates.*

[1] Unless otherwise stated, all the figures in this report are drawn from Resolution Foundation analysis. Please see the technical annex for more information on our methodology. We have made the data used for this report available on our website, www.resolutionfoundation.org. Further detail can be found in *Squeezed: the low earners audit* (March 2009, updated August 2009). The next update of this will be published in December 2009. http://www.resolutionfoundation.org/documents/200908audit1_001.pdf
[2] Office for National Statistics, *Labour Market Statistics Statistical Bulletin*, 14th October 2009 http://www.statistics.gov.uk/pdfdir/lmsuk1009.pdf
[3] Muriel, A. and Sibieta, L., *Living Standards during Previous Recessions* (Institute for Fiscal Studies, 2009) http://www.ifs.org.uk/bns/bn85.pdf
[4] Child Poverty Action Group, *Parliamentary Briefing on Benefits Simplification*, December 2007
[5] 49 per cent of working age low earners have qualifications at or below NVQ Level 2, which is equivalent to five GCSEs.

### 3. Despite a swift response by government, further action is necessary and feasible

Our research shows that further action is necessary and feasible and should focus on four key areas:

- Sustaining the position of low earners (page 15)
- Smoothing transitions (page 19)
- Building on low earners' capabilities (page 22)
- Shaping markets (page 26)

Detailed recommendations in each of these areas are outlined further on in this report. These could have a material impact on low earners. Specific examples include:

- On *unemployment*, we propose that the formal skills assessment be brought forward from 26 weeks to 13 weeks of unemployment, and argue for a change in Jobcentre Plus targets to encourage greater skills participation and a focus on getting people into sustainable employment
- On *sustaining* work, we believe the goal should be to make it easier for people to combine real jobs with useful training, particularly during the recession, for example through allowing training to count in the eligibility criteria for Working Tax Credit, and through removing the disincentives for one partner to take on a job if the other is accessing state-supported training
- On *housing*, the immediate priority is to strengthen the Pre-Action Protocol between government and mainstream lenders and do more to engage sub-prime and second charge lenders in this agreement. We also believe that existing government schemes to support struggling home owners, such as the Support for Mortgage Interest Scheme, need to be more carefully targeted
- On *finances*, we argue that a national Money Guidance service should be rolled out as a matter of urgency in 2010, and this service should be set up to deliver holistic financial advice and guidance. And we highlight the importance of existing savings initiatives for low earners, and advocate their extension where possible

The report goes beyond these immediate recommendations to set out some short- to medium-term priorities, which we believe will ensure that low earners do not lose out in a period of recovery. For example:

- We call for a review of the current systems of in-work support for low earners and an overhaul of the current approach to funding and delivery of intermediate skills
- We support moves to create a more responsive, employee-led system of skills but argue that it is essential that these commitments add up to more than another restructuring of the adult education system – Skills Accounts must put genuine purchasing power in the hands of low earners, and be attached to the right support and advice
- We believe there is a pressing need for further work between government and private markets to develop a sustainable investment model for the private rented housing sector, given its rapid expansion in recent years
- There is also a timely opportunity to diversify the affordable credit market in a way that draws in the capital required to build sustainable models

Government will not be able to achieve these changes alone: it must recognise that across housing, employment, skills and financial health there are mixed markets in play. How public value is created through private vehicles is just as important as getting the right mix of fiscal, monetary, regulatory and legislative policy when it comes to protecting low earners and ensuring that they do not lose out either now during the downturn, or as we move towards a period of recovery and a public spending squeeze.

## CONTENTS

## Table 1: Summary data for households, benefit units and individuals by income group: UK 2007-08

| 000s | Benefit-dependent | Low earners | Higher earners |
|---|---|---|---|
| **Households**[1] | | | |
| Total | 7,000 | 7,200 | 11,200 |
| With children | 1,900 | 2,400 | 3,400 |
| Without children | 5,100 | 4,800 | 7,800 |
| **Individuals within households**[2] | | | |
| Total adults | 11,300 | 14,300 | 24,300 |
| Women | 6,700 | 7,700 | 12,000 |
| Men | 4,600 | 6,500 | 12,300 |
| Economically active | 2,600 | 7,500 | 19,800 |
| Full-time employee | 600 | 4,000 | 14,600 |
| Part-time employee | 700 | 2,100 | 3,000 |
| Full-time self-employed | 400 | 800 | 1,500 |
| Part-time self-employed | 200 | 200 | 400 |
| Unemployed | 700 | 300 | 200 |
| Economically inactive | 8,700 | 6,800 | 4,500 |
| Retired | 4,500 | 4,900 | 3,000 |
| Student | 300 | 300 | 300 |
| Looking after family/home | 1,000 | 600 | 500 |
| Permanently sick/disabled | 2,100 | 700 | 400 |
| Temporarily sick/disabled | 200 | 0 | 0 |
| Other inactive | 700 | 300 | 300 |
| Total children | 4,600 | 3,800 | 5,500 |
| **Benefit units**[3] | | | |
| Total | 8,900 | 6,800 | 14,700 |
| Family type | | | |
| Pensioner units | 3,300 | 2,700 | 2,400 |
| Pensioner couple | 900 | 1,300 | 1,300 |
| Male pensioner single | 600 | 400 | 400 |
| Female pensioner single | 1,900 | 1,000 | 700 |
| Working-age units | 5,600 | 4,100 | 12,300 |
| Couple with children | 800 | 1,300 | 3,600 |
| Lone parent | 1,200 | 500 | 500 |
| Couple without children | 700 | 800 | 4,400 |
| Male single without children | 1,600 | 800 | 2,300 |
| Female single without children | 1,200 | 700 | 1,600 |

Notes: [1] 'Households' are defined as 'a single person or group of people living at the same address who either share one meal a day or share the living accommodation, i.e. a living room'. So, for example, a group of students with a shared living room would be counted as a single household even if they did not eat together, but a group of bedsits at the same address would not. Households are divided by income group based on the distribution of equivalised income. 'Low earner' households are defined as having equivalised income in the 3rd, 4th and 5th deciles; that is, equivalised income between £257 and £492 per week. Any household receiving 20 per cent or more of its total income from income-related benefits is automatically classed as 'benefit-dependent'.

[2] Individuals within households are allocated to income groups based on the status of their household.

[3] 'Benefit unit' is a standard DWP term that relates to the tighter family definition of 'a single adult or couple living as married and any dependent children'. A dependent child is aged under 16 or an unmarried 16 to 19-year-old in full time non-advanced education. So, for example, a man and wife living with their young children and an elderly parent would be one household but two benefit units. The distribution of benefit units across income groups shown here do not map directly to the households the units live in. Instead, benefit units are divided by income group based on the distribution of equivalised income across this measure. 'Low earner' benefit units are defined as having equivalised income in the 3rd, 4th and 5th income deciles; that is, income between £261 and £443 per week. Any benefit unit receiving 20 per cent or more of its total income from income-related benefits is automatically classed as 'benefit-dependent'.

Source: DWP, *Family Resources Survey 2007-08*

# PART 1: THE IMPACT OF THE RECESSION ON LOW EARNERS

Alan, Sarah and their two children live in the house they bought five years ago. Alan works in IT and Sarah works for the local council. They are both worried about the impact of the recession on their jobs. They worked hard to buy their house, and are determined to stick with their 5.3 per cent fixed term repayment mortgage that costs them £600 a month. Compared to the £500 they have to pay towards an outstanding credit card debt that landed them in court a few years ago, it doesn't seem like such a bad deal. Childcare costs them another £300 as the government support they receive only covers term times, and their jobs don't give them the flexibility to be around during the holidays.

Sarah spends a great deal of time on saving money. She and her mum have a list of key ingredients and they are well-versed on which supermarkets have the best prices. She is proud of the fact she can put a meal for four on the table for £2. It helps that they have an allotment, and that Sarah prefers to shop online rather than going to the supermarket – 'I can avoid the temptation of the clothes aisles'.

Alan recently decided that, after little improvement in his salary in the eight years he'd been in his job, it was time to get some training. But he has found it hard: 'I'm an in-betweener – I earn too much and I'm too qualified for much help…I'm too old for all those youth schemes, too young for older people's schemes. I've been in the same job for too long but I can't get my boss to pay £175 for a course I want to do. At 38 I'm getting overtaken by younger people who know more about IT these days'.

Alan recently bought a moped after the couple realised that they were spending £1,600 a year on public transport to get to work. But Sarah isn't sure how else they can economise – 'the next thing I could cut is the food – I can't believe how much more it is costing us these days'.

### *Low earners and jobs*


**Summary**

- Low earners are more vulnerable to job losses and business closures because of the areas, industries and types of businesses in which they are concentrated
- Low-skilled low earners are more vulnerable to job losses than higher-skilled workers, whichever industry or sector they work in
- Low earners who fall out of the labour market are more likely to become long-term unemployed than higher earners
- Low earners who remain in work are likely to find it harder than before to access training and skills development


In the immediate aftermath of the international banking crisis, the biggest increases in redundancies were in banking and manufacturing. However, as Table 2 shows, by the start of 2009, the highest number of redundancies were in hotels, restaurants and distribution, manufacturing, and construction, as well as finance and business services. Together these sectors employ five million low earners. These are also the sectors that have experienced the sharpest rises in redundancy rates: between Q3 2008 and Q1 2009, redundancies in distribution, hotels and restaurants grew from 30,000 to 71,000; in manufacturing they grew from 26,000 to 67,000, and in construction redundancies grew from 31,000 to 49,000.

Looking at overall patterns since the recession began, it is the 'real' economy that has taken the hardest hit, despite the origins of today's circumstances in the financial services sector. Since Quarter 3 2008, growth has declined by 5.3 per cent in *distribution, hotels & restaurants* and by 13 per cent in *construction* (which employs 600,000 low earners and many more self-employed low earners) compared to 4.5 per cent in *business services and finance*.

The latest Office for National Statistics (ONS) figures published in October 2009 show that there were some small signs of a levelling out of the recession between July and September, with job vacancies remaining unchanged since the last quarter, redundancies falling, and rises in unemployment and the claimant count being less steep. So the deterioration is slowing. Nevertheless as Table 3 confirms, the direction of travel is still downwards, and projections – shown in Chart 1 – indicate that, as in previous recessions, unemployment will continue to grow for some time after the economy begins technical recovery. In the 1980s and 1990s, it took five to seven years before unemployment returned to pre-recession levels.

**Table 2: Workforce jobs and redundancies by industry: UK**

| | 000s of workforce jobs held by individuals living in low earner households *2007-08* | Proportion of workforce jobs held by individuals living in low earner households *2007-08* | Change in number of workforce jobs *Q2 2007 - Q2 2009* | 000s of redundancies in past year *May 2009* |
|---|---|---|---|---|
| Distribution, hotels & restaurants | 2,400 | 35% | -3% | 199 |
| Education, health & public administration | 1,800 | 23% | +3% | 54 |
| Finance & business services | 1,200 | 18% | -3% | 221 |
| Manufacturing industries | 800 | 25% | -9% | 211 |
| Other services | 600 | 30% | +1% | 31 |
| Construction | 600 | 26% | -3% | 170 |
| Transport & communications | 500 | 28% | +0% | 71 |
| Agriculture, forestry & fishing | 200 | 36% | +7% | : |
| Mining, energy & water supply industries | 0 | 12% | +2% | : |

Notes: Low earners defined on basis of gross household income equivalised for household size and composition. Households in receipt of income-related benefits worth 20 per cent or more of their total income are considered benefit-dependent.

Total number of workforce jobs is greater than total number of low earners in employment because the figures capture jobs rather than employees. One employee may have more than one job.

Sources: DWP, *Family Resources Survey 2007-08*

ONS, *ELMR*, Table 2.06

**Table 3: JSA claimant count by 'usual occupation' of claimant: UK Sep 2009**

| | 000s of jobs held by individuals living in low earner households *2007-08* | Proportion of employees living in low earner households *2007-08* | Year-on-year change in number of JSA claimants (000s) *Sep 2009* | Quarter-on-quarter change in JSA claimants (000s) *Sep 2009* |
|---|---|---|---|---|
| Elementary occupations | 1,300 | 42% | +147 | +1 |
| Administration & secretarial occupations | 900 | 27% | +67 | +8 |
| Personal service occupations | 800 | 36% | +34 | +12 |
| Sales & customer service | 700 | 38% | +105 | +21 |
| Associate professional & technical occupations | 600 | 15% | +50 | +10 |
| Process, plant & machine operatives | 600 | 35% | +73 | -11 |
| Skilled trades occupations | 600 | 30% | +94 | -10 |
| Managers & senior officials | 500 | 14% | +40 | -2 |
| Professional occupations | 300 | 10% | +33 | +10 |

Notes: Low earners defined on basis of gross household income equivalised for household size and composition. Households in receipt of income-related benefits worth 20 per cent or more of their total income are considered benefit-dependent.

Sum of individuals living in low earner households does not match number of low earners in work because number of jobs set out in ASHE are not definitive.

Sources: DWP, *Family Resources Survey 2007-08*

ONS, *NOMIS database*

ONS, *2008 Annual Survey of Hours and Earnings*

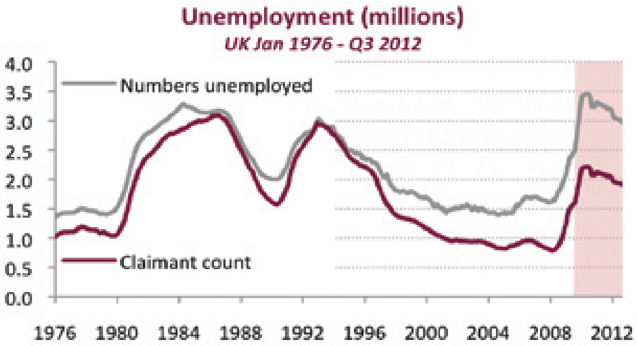



**Chart 1: Unemployment: 1976-2012**

Note: Projections based on analysis of independent forecasters' annual averages.

Sources: Outturn: ONS Time Series, *BCJD & MGSC*; Projection: HMT, *Forecasts for the UK economy: A comparison of independent forecasts*, August 2009, Table M5

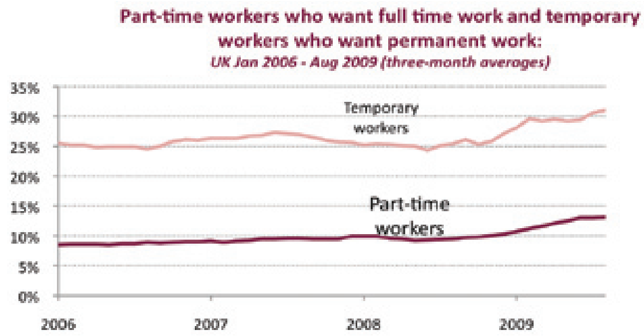



**Chart 3: Temporary workers who want permanent jobs and part-time workers who want full-time jobs**

Source: ONS, *Labour Force Survey: Reasons for Temporary or Part-time working*

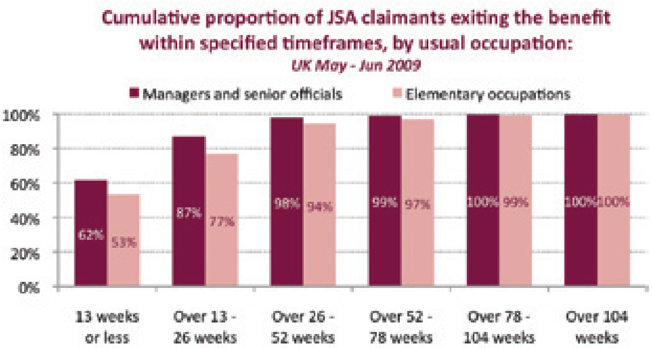



**Chart 2: Time spent on JSA by usual occupation of claimant**

Source: ONS, *NOMIS database*

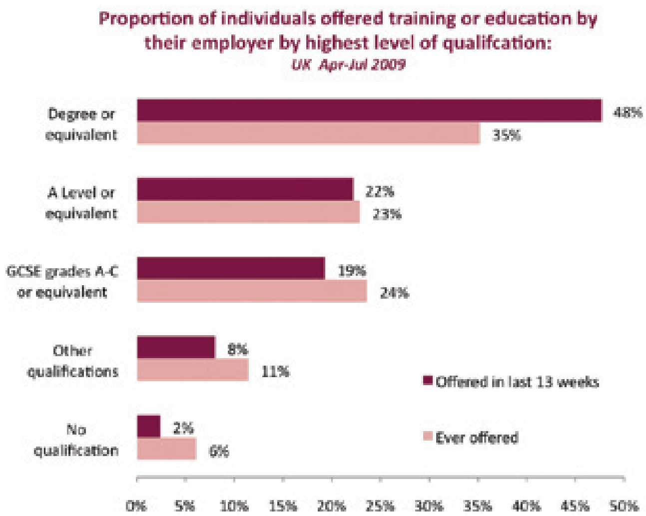



**Chart 4: Access to in-work training by level of qualification**

Source: ONS, *NOMIS database*

The ONS figures also show that there has been a growth in long-term unemployment of six months or more. While the number of people claiming Job Seekers Allowance for less than six months has fallen by 57,000, the number of people claiming for between six and 12 months increased by 74,000, and the number of people who have been unemployed for over 12 months increased by 72,000. Table 3 indicates that the numbers of people in long-term unemployment are highest in those sectors where most low earners work.

Chart 2 compares the time spent on JSA by managers and senior officials with the time spent by those in elementary occupations. It shows that those in the low earner sector are more likely to enter long-term unemployment than those in the higher-earner sector: while nearly nine out of ten managers and senior officials find work again within 26 weeks, only three quarters of people in elementary occupations move off the claimant count.

As well as being at greater risk of becoming long-term unemployed, there is strong evidence that low paid workers are likely to be caught in 'revolving-door' employment, with low earners being less likely to stay in their jobs over time. 76 per cent of low earners who were employed in 2000 were still in their jobs in 2005, compared with 83 per cent of higher earners. Furthermore the recession is reversing the trend away from temporary working that we had seen during the previous period of economic growth.[6] Chart 3 shows that since the recession began there has been a rise in involuntary temporary work and a similar rise in the numbers of people who are working part-time because they could not find a full-time job.

[6] Trades Union Congress, *Recession Report Special*, June 2009 http://www.tuc.org.uk/extras/junerecessionreport.pdf

Not all low earners will lose their jobs as a result of the recession but they are still vulnerable due to reduced opportunities to progress. There is some evidence that businesses are cutting back on workforce development during the downturn, with lower numbers offering training in November than June 2008 and a growth in the number of businesses saying they were not planning to offer training in the next 12 months.[7] A third of companies did not train their staff, and eight million workers received no training at all.[8] These patterns will compound an existing situation, shown in Chart 4 – that low earners have always been less likely to be offered skills and training than higher-earning colleagues. Less than a fifth of individuals with Level 2 training were offered training by their employer between April and July 2009, compared to nearly half of degree-qualified employees. In part this is a product of where low earners work. However it is also as a result of their low skill levels in the first place: research has shown that there are few incentives for employers to offer training to less qualified staff.[9]

### *Low earners and money*

**Summary**

- Low earners are experiencing significantly higher debt-to-income ratios than higher earners, despite historically low interest rates
- Low earners are finding that their existing debt is becoming more expensive to service due to tighter lending practices and fewer lenders offering products that meet their credit needs
- Low earners are finding that it is harder for them to access mainstream credit in the first place due to tougher borrowing requirements
- Low earner levels of anxiety about their financial situation are rising
- The recession has not had a significant impact on savings activity, but overall low earners were under-saving before the downturn and they remain equivocal about the value of saving. Rises in food and fuel costs in 2008 may have limited the amount of money some low earners could put aside

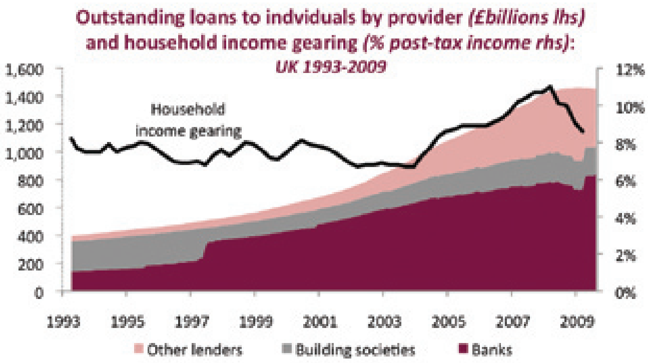



**Chart 5: Trends in household borrowing and income gearing**

Sources: Bank of England *datasets*;
Bank of England, *Inflation Report*, August 2009, Chart 2.6

As Chart 5 shows, before the global financial crisis, credit had become a part of people's everyday lives, and an important mechanism by which to manage household finances. The historically low interest rates of the decade preceding the credit crunch made it easier than ever for households to borrow: in a generation, credit card debt rose from £32 million in 1970 to £54 billion in 2008. What Chart 5 shows is that despite low base rates, the ratio of debt-servicing to household incomes grew steadily in the period from 2004. While dramatic cuts in the Bank of England's official rate since 2008 have lowered this ratio, it remains high by historical standards.

[7] Ipsos MORI, *National Business Survey: national report*, January 2009
[8] Department for Innovation, Universities and Skills, *Time to Train: consulting in a new right to request time to train for employees in England* (HMSO, 2008)
[9] Keep, E., *Initial Submission on Adult Learning in the Workplace – explaining current patterns and their outcomes*, (NIACE, 2007)

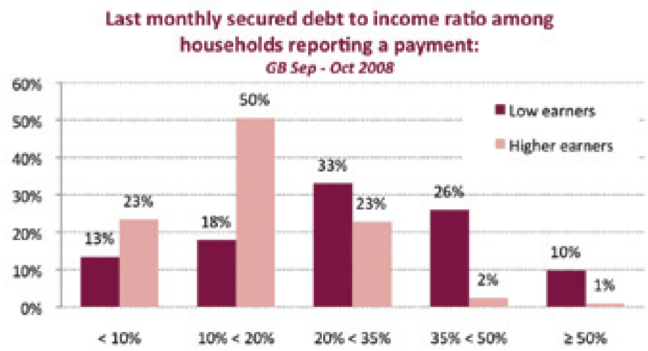



**Chart 6: Secured debt-income ratios among low earner and higher earner mortgagors**

Note: Income groups defined on basis of deciles ranked by gross household income.

Source: Bank of England, *NMG Research*, various

Our analysis shows that at the end of 2008, despite these low interest rates, 24 per cent of low earners were spending more than a quarter of their monthly household income on debt repayment – double the number of households that were in this situation in 2005. A fifth of low earners were reporting in 2008 that their debt repayments were 'heavy', compared to just one in eight in 2005. Chart 6 shows that 36 per cent of low earner mortgagors, compared to 3 per cent of higher earner mortgagors, had a secured debt-to-income ratio of over 35 per cent in the same period; one in ten low earners reported a ratio of over 50 per cent, compared to one in 100 higher earners.

Since 2007 there has been a sharp drop in credit and lending. According to the Bank of England, annual growth in secured lending was 9.5 per cent between 1996 and 2007; by December 2008 it had tumbled to 3.4 per cent. Similarly, the annual growth in consumer credit was 13.8 per cent on average between 1996 and 2007 – falling to just 5.0 per cent by 2008.

The shape of the credit market has changed as a result of the financial crisis. Chart 5 shows that, while there was a sharp drop in lending by mainstream banks and building societies at the end of 2008, the continued activity of 'Other' lenders (which includes online credit card providers) meant that overall lending levels stayed constant after a period of unprecedented growth. However the sub-prime market that was serving ten million people evaporated. In March 2007 there were 6,501 subprime mortgage products available; within a year this had declined by 71 per cent.

As well as the exodus of sub-prime from the market, remaining lenders have curtailed their practices since 2007. The gap between base rates and mortgage rates has grown as rates have come down, and consumers have limited options for re-financing. As well as becoming less affordable, credit is also less accessible in the first place. Lenders have tightened their credit scoring criteria, reduced the availability of unsecured loans, and lowered the limits of credit cards and overdrafts.

The net result of this is that low earners are finding it harder to find lenders who are willing to meet their needs. Despite recent attempts to expand the affordable credit market, for example through the expansion of the Growth Fund, the Financial Inclusion Taskforce estimates that there remains an unmet demand for small-scale credit of around £1.2 billion each year.[10]

As significant as what is actually happening in the credit markets are low earner perceptions of what is going on. By March 2009, three million low earners were worrying 'all the time' about their finances, double the number who felt this way in 2007. Chart 7 shows that while fewer felt constrained by the cost of borrowing in 2008 (compared to 2006), there was a rise in the number of low earning households reporting that they were put off spending more because of concerns about credit access.

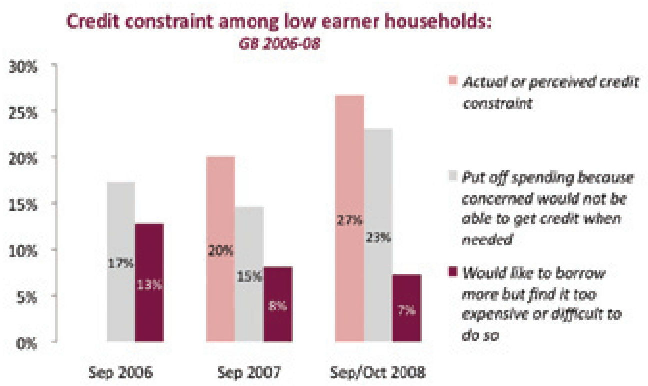



**Chart 7: Credit constraint among low earner households**

Note: Income groups defined on basis of deciles ranked by gross household income.

Source: Bank of England, *NMG Research Survey*, various

Anxiety levels are also evidenced in the significant increase in demand for debt advice. This was already rising before the recession took hold but it has grown more sharply over the last 18 months. Demand for Citizens Advice services grew by 50 per cent between 2006 and 2008 and the Money Advice Trust experienced a 100 per cent rise between 2007 and 2008. Some services are reporting that demand is outstripping supply by a factor of two to one, because of gaps in funding and capacity.[11] As well as a growth in requests for help, there are changes in who is asking. A number of advice providers have noted that demand is rising up the income scale – in other words, indebtedness and money worries are spreading from those on very low incomes to those closer to, or even above, the median income.

[10] Financial Inclusion *Taskforce Working Group, Towards a step-change in third sector lending coverage and capacity* (2008)
[11] Transact presentation of findings of their annual survey of members, presented at Resolution Foundation's expert seminar on household finances, 8th September 2009 http://www.resolutionfoundation.org/documents/TransactPresentation.pdf

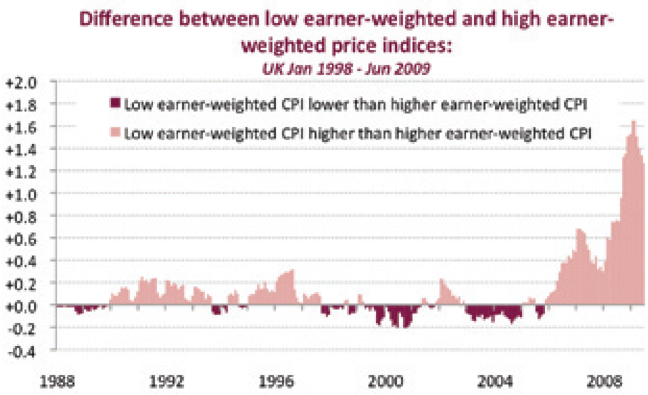



**Chart 8: Low earner and higher earner inflation**

Note: Low and high earner CPI weights based on proportion of total expenditure spent on CPI components in 2007. Income groups defined on basis of deciles ranked by gross household income definition.

Sources: ONS Time Series;

ONS, *Family Spending: A report on the 2007 Expenditure and Food Survey*, 26 November 2008, Table A8,

ONS, *The effects of taxes and benefits on household income*, 2006/07, Table 14

These levels of anxiety do not appear to be translating into more saving activity among low earners during the recession. Over half of low earners do save, albeit in small amounts and not always consistently.[12] However one-third of low earners say that they would like to save £10 a month but that they cannot afford it – something which may well have been exacerbated by the significant rises in the cost of essentials such as fuel and food in 2008. As Chart 8 shows, although differences in inflation experienced by low earners and higher earners were relatively small between 1998 and 2006, low earners have subsequently faced significantly higher levels of inflation, particularly from the latter half of 2008.

The Association of British Insurers' Savings and Protection Survey indicates that 13.9 per cent of low earners are 'under-saving'.[13] These findings are reinforced by our own analysis, shown in Table 4, of the Family Resources Survey. This shows that 44 per cent of low earners aged between 30 and 54 have less than a month's income saved, and that nearly three quarters have less than two months' income in the bank. The lack of a safety net is also underlined by the fact that only 39 per cent of low earners have a life insurance policy, compared with 58 per cent of higher earners – a pattern that is mirrored in ownership of payment protection, contents insurance, income protection and critical illness insurance products.

There is also an age dimension to low earner saving patterns, as Table 4 shows. 50 per cent of low earners aged between 55 and 64 have the equivalent of six months income saved, compared to just 15 per cent of low earners aged between 30 and 54. This may reflect a lifecycle pattern, but it could also be a generational effect, reflecting the fact that older low earners had more opportunities to save when they were younger, thanks to lower house prices.

Over half of low earners – in line with other groups – say that current economic circumstances have not changed their attitudes towards savings, or the amounts they are putting away. That said, the recent ABI survey shows that for those people whose attitudes *have* been affected by the recession, roughly two times as many individuals say they are likely to save less rather than more. Furthermore 65 per cent of low earners perceive that the benefits of saving have gone down a little or a lot, even if their behaviour has not changed significantly.[14]

**Table 4: Savings adequacy among low earners, by age of head of benefit unit: UK 2007-08**

| *Savings equivalent to* | 16-29 | 30-54 | 55-64 | 65+ | All ages |
|---|---|---|---|---|---|
| Less than one month's gross income | 14% | 44% | 13% | 5% | 20% |
| More than one but less than two months' gross income | 63% | 30% | 23% | 19% | 32% |
| More than two but less than six months' gross income | 14% | 11% | 15% | 15% | 14% |
| More than six months' gross income | 9% | 15% | 50% | 62% | 34% |

Note: Low earners defined on basis of gross benefit unit income equivalised for unit size and composition. Benefit units in receipt of income-related benefits worth 20 per cent or more of their total income are considered benefit-dependent.

Source: DWP, *Family Resources Survey 2007-08*

[12] Association of British Insurers, *Savings and Protection Survey*, Quarter 3 2009. We are grateful to ABI for their further analysis of the findings by income group. http://www.abi.org.uk/Publications/ABI_Publications_Q3_2009_ABI_Savings_and_Protection_survey_cb3.aspx
[13] ABI, ibid
[14] ABI, ibid

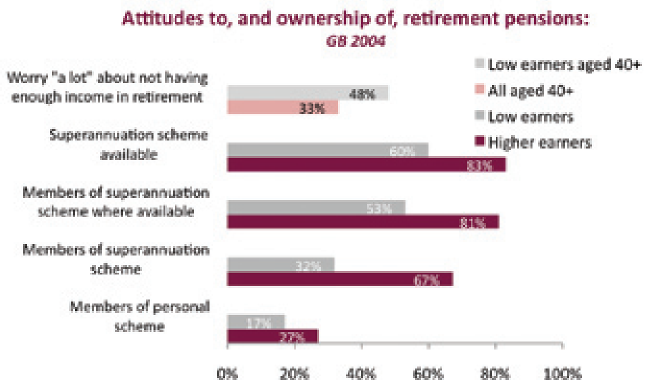



**Chart 9: Attitudes to, and ownership of, retirement pensions**

Note: Low earners defined on basis of income and benefit receipt: includes members of low earner households *and* low earner individuals living in non-low earner households.

Sources: Alliance for Health & the Future, *Living in the Advice Gap: An Investigation into the Resolution Foundation's Target Group*;

Resolution Foundation, *Closing the Advice Gap*, January 2007

It is too early to tell what impact the recession may have on pension saving activity specifically, although it is obvious that time spent out of the labour market and not saving has an impact on future pension income. We know that before the recession, low earners were less likely to have an occupational pension than higher earners. As Chart 9 shows, in part this is because their employers are less likely to offer them in the first place; however what we can also see here is that even where pension schemes are available, only 53 per cent of low earners had joined their schemes, compared to 81 per cent of higher earners. 55 per cent of low earners believe that the state pension will be their main source of retirement income, compared to 44 per cent of the overall population.[15]

### *Low earners and housing*


**Summary**

- Home ownership has become harder to sustain for low earners who have bought in recent years and they are exposed to negative equity, high repayment rates and repossession as a result of job loss or inability to maintain payments
- Low earners are experiencing more constrained access to home ownership in the first place – though many were already priced out of the market. The credit crunch and recession have compounded this situation
- Low earners who cannot buy are also finding it harder to access social housing, so greater numbers of low earners are entering the private rental sector. This reflects a more general trend in the housing market, but not all low earners are making an active choice to rent – it is often their only option


It is important to take account of wider changes to the housing market over the last century when considering the impact of the recession on low earners' housing situation. Chart 10 shows some significant changes in the last one hundred years and indeed since the last recession of the 1990s. Having had a steady trajectory of growth since the post-war period, home ownership has stagnated since the early 1990s. Social housing, which was also growing – albeit at a slower rate – until the early 1980s, has declined over the past 20 years, reaching a low plateau towards the end of the century. In contrast, the private rental sector, which represented nearly 80 per cent of the market a hundred years ago, has experienced a steep decline. It is only since 1992 that this sector has grown, almost doubling in size since then to now represent 14 per cent of the market.

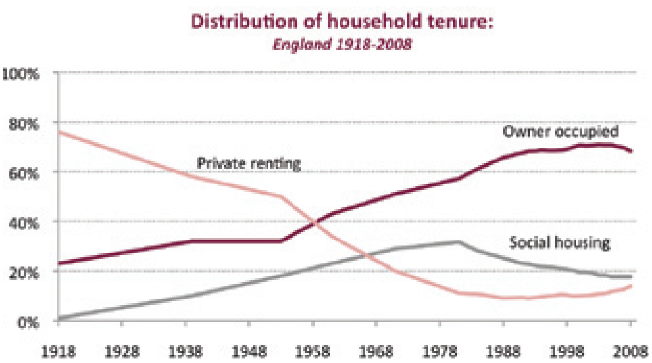



**Chart 10: Trends in housing tenure**

Source: CLG, *Survey of English Housing: Preliminary Report 2007-08*, Table 1

Compared to 1990, there are now more homeowners from low income groups. This development has been supported by a policy agenda that has sought to promote home ownership and expand it. What started with the 'right to buy' agenda in the 1980s has been continued under this government with the creation of Low Cost Home Ownership schemes, and a supportive tax environment. The expansion of the sub-prime market, itself a product of the 1990s recession, opened out access to mortgages. The value of private housing assets stood at £1.44 trillion in 2008 – almost three times GDP.

[15] ABI, ibid

Table 5 shows that 72 per cent of low earners now own their properties. There is significant variation between age groups: while 81 per cent of low earners aged 55 to 64 are homeowners, just 29 per cent of 16 to 29 year olds are. Many low earners bought before the steep rise in house prices. The impact of the recession on those low earning home owners who own outright is much less significant than for the 28 per cent of low earner households who own with a mortgage, and particularly the 16 per cent of low earner households who have bought in the last decade.[16]

**Table 5: Housing tenure among low earner households by age of head of household: UK 2007-08**

| | 16-29 | 30-54 | 55-64 | 65-79 | 80+ | All ages |
|---|---|---|---|---|---|---|
| Owners | 29% | 66% | 81% | 84% | 80% | 72% |
| *Owned outright* | 2% | 14% | 60% | 78% | 78% | 44% |
| *Owned with mortgage* | 27% | 52% | 21% | 6% | 3% | 28% |
| Social rented sector tenants | 29% | 21% | 14% | 12% | 14% | 17% |
| *Rented from council* | 17% | 12% | 8% | 8% | 7% | 10% |
| *Rented from housing association* | 12% | 9% | 5% | 4% | 6% | 7% |
| Rented privately | 43% | 13% | 5% | 4% | 6% | 11% |
| *Rented privately - unfurnished* | 24% | 11% | 4% | 3% | 5% | 8% |
| *Rented privately - furnished* | 19% | 3% | 1% | 0% | 1% | 3% |
| All households | 100% | 100% | 100% | 100% | 100% | 100% |

Notes: Income groups based on gross benefit unit income equivalised for unit size and composition. Benefit units in receipt of income-related benefits worth 20 per cent or more of their total income are considered benefit-dependent.

Source: DWP, *Family Resources Survey 2007-08*

The risk profile of this group of low earners was high before the recession began and subsequent falls in house prices pushed a number in the group into, or close to, negative equity. As Chart 11 shows, at the end of 2008, 14 per cent of low earner mortgagors reported a loan-to-value ratio of 75-100 per cent and 4 per cent said they were already in a position of negative equity. By contrast just 12 per cent of higher earner mortgagors and 11 per cent of benefit-dependent groups had LTVs above 75 per cent. While negative equity is not necessarily a problem in itself, it limits household mobility – at precisely the time it may be essential to move in order to find work. It can also limit the availability of options for households experiencing difficulties with their finances.

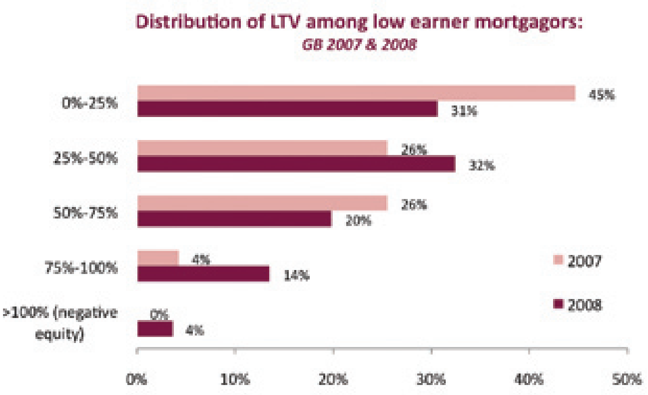



**Chart 11: Loan-to-value among low earner mortgagors**

Note: Low earner households defined on basis of deciles ranked by gross household income.

Source: Bank of England, *NMG Research*, various

A more risk-averse and smaller market of mortgage lenders has compounded these risks. As the credit market has contracted, there are far fewer re-financing packages on offer, making it harder for low earners to shop around for a better deal. In August 2009, there were just 32,000 remortgage loans advanced, a 22 per cent decrease on July, and a 57 per cent decrease on August 2008.[17]

Those low earners who are not homeowners are also finding it harder to buy than before, despite the recent drop in house prices, for two reasons. First, since 2007, the availability of mortgages has plummeted. While there is some evidence of a gradual recovery in house purchase loans more recently, with activity in August 2009 at twice the level of that recorded at the start of 2009, it is still hovering around half the August average of seven years before the credit crunch.[18] Furthermore, as we noted above, the sub-prime market that was an important source of lending for low earners has shrunk significantly since the credit crunch.

[16] Department for Communities and Local Government, *Survey of English Housing 2005-06* http://www.communities.gov.uk/publications/housing/hss26
[17] Council for Mortgage Lenders, *Two Speed Mortgage Market in August*, 12th October 2009 http://www.cml.org.uk/cml/media/press/2424
[18] CML, ibid.

Secondly, lenders are becoming more risk averse, introducing tougher and more constrained lending practices. Mortgage approvals for low earners have fallen faster than for other groups: in Q2 of 2009, just over 8,500 mortgages were approved for people earning between £10,000 and £20,000, a drop of 84 per cent since 2006. Deposit requirements demanded by mortgage lenders are now extremely high, sometimes between 30 and 40 per cent or more. These have made parental assistance an essential pre-requisite for homeownership, and the Council of Mortgage Lenders estimates that families assist 80 per cent of first time buyers. Given the low level of savings that many low earners have, the 'bank of mum and dad' is unlikely to be there to help them out.

The impact of these changes in lending practices is that low earners who might have been able to buy even three years ago are not able to now. Access to social housing is extremely constrained, and this makes it a limited option for low earners: two-thirds of social tenants have incomes within the poorest two-fifths of the overall income distribution. These forces are driving low earners towards the private rented sector. For some younger low earners, difficulties in accessing mortgages may mean deferring home ownership and staying in the family home or private rented accommodation for longer. This is not without its difficulties. But the problem is greater in cases where limited affordability is leading low earners to become excluded from property ownership altogether, with the benefits which that brings in the current UK tax system, and becoming permanently stuck in inappropriate and insecure private rented housing.

Despite being the dominant tenure a century ago, the private rented sector has been overlooked in recent years. For some low earners it is a flexible and convenient form of accommodation but the difficulties they have in accessing the housing market, coupled with a growth in repossessions as a result of the recession, is driving them in greater numbers into this sector through necessity rather than choice.

Conditions vary significantly across the sector, and for many it is a tenure characterised by poor conditions, few rights and great insecurity. Repossessed low earners are at risk of losing their private rented homes as well, as the boom in Buy-to-Let in recent years has given way to a growth in the number of landlord repossessions with obvious consequences for tenants. Furthermore, low earners can find it hard to even access housing in this sector, as deposit requirements can be prohibitively high, and landlords can choose not to accept tenants on Housing Benefit – which 16 per cent of low earners in rented accommodation receive.

The recession has not only hit homeowners and tenants but also builders and property developers who have been faced with a contraction in development finance as well as a decline in demand. In the good times, getting affordable housing built came to be based upon a complex model of speculative private development, whereby private developers entered into Section 106 agreements with local councils to build affordable housing as part of any new development. This cross-subsidy model was significantly undermined by the credit crunch, and many Section 106 agreements have either dried up, or have required government bail-out. At this stage in the economic cycle, it is not yet clear what a more sustainable model for building affordable housing might be.

## PART 2: RECOMMENDATIONS: AN AGENDA FOR LOW EARNERS

Although there continue to be debates about the speed at which the public deficit needs to be brought down, and the severity of public debt levels in the UK, there is no question that the recession will give way to a period of fiscal consolidation and a public spending squeeze.

There will be difficult decisions to make about priorities and programmes. To date, many of the debates have centred on what kinds of cuts are necessary, and when they should be made. The challenge is to make these decisions in such a way that existing inequalities are not reinforced.

To achieve this, as well as making cuts, our analysis suggests that there are particular areas of public spending which would merit further scrutiny in order to ensure that limited budgets are being put to best use. These include certain tax breaks, for example on equity-based ISAs, the Train to Gain and Low Cost Home Ownership schemes, and the administrative costs associated with the current tax credit system.

A number of the measures we propose here do not call for direct state action. Instead they would require the government to play an active role in shaping a mixed market, working for example with employers or the financial services industry to bring about an improvement in the situation of low earners. This is an important point: across all the areas we have considered, there are mixed economies where government alone cannot achieve the outcomes it desires.

The following sections of this report are organised thematically. We consider issues around:

- Sustaining the position of low earners
- Smoothing transitions
- Building on low earners' capabilities
- Shaping markets

Within each theme we make a number of suggestions relating to jobs, housing and finances which government and others should consider, to protect low earners and to ensure that they do not bear a disproportionate burden of a straitened spending environment. Based on our analysis of how the recession is impacting on low earners, some of these suggestions are specific actions that could be taken immediately; some are proposals where we believe further work should be done to ensure that the needs of low earners are addressed as we move from recession to recovery.

## (1) Sustaining low earner positions

*For many low earners, the recession heightens insecurity in jobs, housing and finances. The primary focus of all measures to support low earners over the next 12 to 18 months must be on ensuring that low earners are not pushed from a state of coping to a state of crisis. Given the evidence on the negative impact of long periods out of work on health, relationships and future employability, sustaining jobs, or at the very least, sustaining low earner proximity to the real labour market is a priority.*

**Summary – work**

- Work with the full range of employers to develop initiatives to avoid redundancies, and particularly with small and medium sized businesses where low earners are concentrated
- Connect *all* welfare-to-work schemes, not just those for the under-25 age group, with real jobs through Job Guarantees and incentives for employers to invest in training and development. Use the existing 'work for your benefits' scheme budget to extend Future Jobs Fund to older age groups
- Ensure that youth unemployment schemes reach non-graduates who are more vulnerable in the long-run to the 'scarring' effects of early-age unemployment

There is already much anecdotal evidence of efforts being made by employers to avoid redundancies: for example JCB employees voted in favour of a reduction in the working week in order to avoid 350 redundancies and KPMG has introduced a pay freeze as well as giving their staff the option of a four day week. **The government could do more with low earner employers and companies in low skill sectors** to encourage them to introduce such schemes where appropriate, and to avoid laying people off as a result of the recession wherever possible.

Clearly it is not realistic to hope that a recession will not lead to any job losses whatsoever. But **for those people who do lose their jobs, as much as possible should be done to maintain their proximity to a real labour market**. More recent schemes, such as the £1 billion *Future Jobs Fund*[19] and the coalition of 150 employers behind *Backing Young Britain*,[20] have taken positive steps towards this goal. These initiatives are designed around commitments to job guarantees, decent wages and incentives for employers to invest in training and developing young people.

It is essential that all government schemes are also tested against the labour market proximity measure. For example, the ambition to create 250,000 apprenticeships in 2009/10[21] is a good one, but the **quality of these apprenticeships must be maintained**, and employers participating in the schemes should make commitments to meaningful development and progression in exchange for incentives and support from government.

Similarly, the £15 million 'work for your benefits' pilot scheme,[22] designed for over-25s who have been out of work for more than two years, must not send people to work experience that is disconnected from genuine prospects. Like the Future Jobs Fund, schemes for older workers and the long term unemployed should **focus on real experience with the possibility of a real job** at the end of a period of training. This is particularly important for low-skilled older workers who do not have access to the recession-driven schemes introduced for younger people. **Government should consider redirecting the future budget for 'work for your benefits' into more employer incentives** in order to extend the Future Jobs Fund model to older workers too.

Finally, the government has rightly focused a great deal of energy and resources on ensuring that young people are at less risk of becoming long-term unemployed. Table 6 shows that while the fall in employment for graduates has been dramatic, the rise in unemployment for non-graduates has been more significant. **It is essential that government support reaches those young people who are not graduates** for whom the risk is not only deferred entry to the labour market, but also permanent exclusion from it.[23]

19 http://campaigns.dwp.gov.uk/campaigns/futurejobsfund/index.asp
20 http://interactive.bis.gov.uk/backingyoungbritain/
21 http://www.dcsf.gov.uk/14-19/index.cfm?go=site.home&sid=3&pid=370&ctype=TEXT&ptype=Single.
22 http://www.dwp.gov.uk/supplying-dwp/what-we-buy/welfare-to-work-services/opportunities-to-tender/workforyourbenefitpilots.shtml
23 Bell, D. N. F. and Blanchflower, D. G., *What Should Be Done About Rising Unemployment in the UK?,* (IZA Discussion Papers 4040, Institute for the Study of Labour, 2009)

**Table 6: Economic activity among 21-25 year-old graduates and non-graduates: UK 2008 & 2009**

| | Apr-Jun 2008 | | Apr-Jun 2009 | | Change | |
|---|---|---|---|---|---|---|
| | Graduates | Non-graduates | Graduates | Non-graduates | Graduates | Non-graduates |
| Numbers (000s) | | | | | | |
| Employed | 690 | 2,282 | 649 | 2,184 | -41 | -98 |
| Unemployed | 42 | 249 | 61 | 374 | +19 | +125 |
| Inactive | 110 | 843 | 132 | 812 | +22 | -30 |
| All | 843 | 3,374 | 842 | 3,370 | -1 | -3 |
| Proportions | | | | | | |
| Employed | 82% | 68% | 77% | 65% | -6% | -4% |
| Unemployed | 5% | 7% | 7% | 11% | +44% | +50% |
| Inactive | 13% | 25% | 16% | 24% | +20% | -4% |
| All | 100% | 100% | 100% | 100% | -0% | -0% |

Source: ONS, *Labour Force Survey*

**Summary – housing**

- Extend existing monitoring work of high street banks, to enable them to take a pro-active role in identifying vulnerable households and signposting support before households miss their first payment
- Temporarily expand eligibility of the Support for Mortgage Interest scheme from workless households to low-earning households where one person has lost their job
- Clarify minimum forbearance requirements of the Pre-Action Protocol between government and mortgage lenders and extend its coverage
- A landlord's repossession should not become a tenant's eviction – the Pre-Action Protocol should cover of the Buy-to-Let sector

Many banks already monitor people's financial behaviours in order to identify potential theft or fraud. **More could be done to engage high street banks as partners in ensuring people get early support before they hit financial crisis**. Identifying households at risk of missing payments, and signposting them towards available support is a possibility, and engaging high street banks could be a better way of achieving this objective than spending money on government information and marketing campaigns.

Since the start of 2009, the government has already acted swiftly to open up the Support for Mortgage Interest scheme. The size of the mortgage homeowners could claim for was boosted from £100,000 to £200,000, and the waiting time for new claimants was reduced from 39 to 13 weeks.[24] However, it is still only available for those households where no one is working. There is support available for households which have experienced a drop in income through the Homeowners Mortgage Support Scheme,[25] but it only covers a proportion of mortgage interest and not all lenders have signed up to it. For many low earning households, the crisis comes long before both people lose their jobs: often their financial stability was dependent on two incomes. There is some indication that repossessions are rising for households where one member is working and so it is a vital time-limited measure to **extend Support for Mortgage Interest, or to expand the Homeowners Mortgage Support scheme**.

24 http://www.jobcentreplus.gov.uk/JCP/Customers/WorkingAgeBenefits/Dev_016128.xml.html
25 http://www.communities.gov.uk/housing/buyingselling/mortgagesupportscheme/

The introduction of a Pre-Action Protocol between government and mainstream mortgage lenders was designed to ensure that lenders take 'reasonable steps' to prevent repossession.[26] It appears to already be having an impact, with calls to debt advice lines about mortgage arrears falling between January and June of 2009. The protocol has recently been enhanced by a requirement that lenders inform the relevant local authority when they plan to initiate repossession proceedings, in a bid to link up public support for vulnerable homeowners.

An ongoing issue is that not all lenders are showing such forbearance, and in particular non-prime and second charge lenders are not fully engaging with the Pre-Action Protocol. This will need to be clarified to protect low earners, through **clearer minimum forbearance requirements as part of the Pre-Action Protocol**. At the moment it is not enforceable, and it is not precise about the form or extent of alternative options that are available to defaulting borrowers, instead leaving it up to courts to interpret it.

Mainstream mortgage lenders have already moved to help people avoid repossession, offering a range of options such as payment holidays, capitalising arrears, converting people to interest-only mortgages and extending the mortgage period.[27] It is important to **ensure that forbearance measures are not simply storing up problems for the future**; that said, some of the more innovative approaches of lenders to supporting homeowners are welcome – for example, waiving the early redemption charges for borrowers on high fixed rate deals.

There remains a **question about whether lenders are doing enough to pass on the significant reductions in interest rates of the downturn**. Whereas 90 per cent of mortgage rates were within two percentage points of the base rate in Q3 2008, just 32 per cent were by Q1 2009. 0.4 per cent of mortgages were four percentage points above the base rate in Q3 2008, and this had risen to 46 per cent by Q1 2009. While banks say that they cannot build up their reserves as well as pass on savings to borrowers, consumer groups such as *Which?* point to the fact that there is a mismatch between what banks are offering their borrowers and how low the base rate is.

Compared to the moves to support low earning and vulnerable homeowners, there has been considerably less action during this recession to protect people living in the private rented sector. There have been some limited measures to enforce the rights of tenants where landlords going through repossession did not have permission from their mortgage lender to rent in the first place, and there is now a requirement that tenants are notified of a repossession order much sooner than was previously the case. But beyond that, a tenant's security is determined by their landlord's circumstances - not a secure situation when it remains unclear whether Buy-to-Let mortgages are covered by the Pre-Action Protocol in the same way other mainstream mortgage products are.

Landlords also need support during the recession, if tenants are to be protected. More could be done to connect the large number of small landlords in the sector (three quarters of landlords are individuals or couples) with the handful of institutional landlords, for example through **developing internal markets that enable small landlords to exit the market without their tenant having to leave their home**.

**Summary – finances**

- Ensure that proposed reforms to consumer credit market do not have the unintended consequence of making debt repayment unaffordable, or further limiting certain types of credit
- Building on the Debt Relief Orders introduced earlier this year, extend the range of low-cost, out-of-court debt remedies targeted at debtors with low incomes and few assets
- Standardise and share models around debt collection
- Extend forbearance practices to utility companies and public sector
- Tackle poor take-up of in-work benefits – for example, only 50 per cent of people in work who are eligible claim Housing Benefit

[26] http://www.justice.gov.uk/civil/procrules_fin/contents/protocols/prot_mha.htm
[27] Ford, J. and Wallace, A., *Unchartered Territory: managing mortgage arrears and possessions* (Shelter, 2009)

Protecting vulnerable consumers during the downturn is essential, in order to ensure that financial difficulties do not reach crisis point. The already vulnerable position of low earners has been compounded by the tightening of the credit market and the drying up of affordable credit. Whereas before it was possible to smooth the peaks and troughs of unexpected expenses, credit is now harder to access, leaving low earners more at risk of financial difficulty.

For example, low earners are now more likely to enter arrears or fall behind on debt repayments. Charges for late payments, accrual of interest and the accumulation of previously unpaid bills all play their role in increasing the vulnerability of low earners in straitened financial times.

There is some evidence that the market is taking steps to ensure that it treats vulnerable consumers fairly. For example, most of the major credit card companies have signed up to a set of fair principles, including a 30 day breathing space for borrowers in difficulty, and a pledge to maintain rather than raise their interest rates if a customer is seeking debt advice. **These market developments are welcome and should be extended more widely across the industry**.

But the expansion of less positive innovations – such as high-interest money lenders targeting vulnerable consumers – will require tougher enforcement by the regulators. The commitment to cracking down on loan sharks and others who are exploiting people's needs in the recent Consumer White Paper is an important one.[28] The review of credit card and store card regulation that this paper announced is welcome, but it is important that any further regulation does not have unintended consequences. For example, **current proposals to increase the minimum monthly payment on credit cards should only apply to new customers**, to avoid the risk of repayments becoming unaffordable and triggering crisis among existing low earning customers. Furthermore, reforms should not result in the reduction of the already constrained availability of sustainable credit to low earners. Credit remains a vital tool that enables struggling households to manage their money without entering crisis.

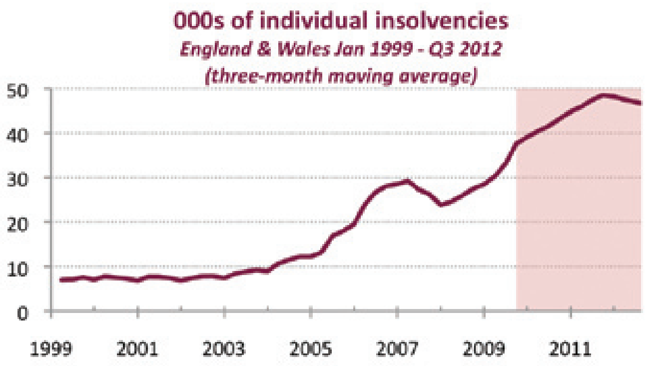



**Chart 12: Individual insolvencies: 1993-2012**

Note: Projections based on Capital Economics and KPMG forecasts for numbers becoming insolvent in each full year.

Sources: Outturn: Insolvency Service, *Insolvencies in the second quarter 2009*, Table 2;

Projection: *London Evening Standard*, "500,000 to fall into personal insolvency in three years", 7 November 2008; *Banking Times*, "Personal insolvencies up 23%", 3 May 2009

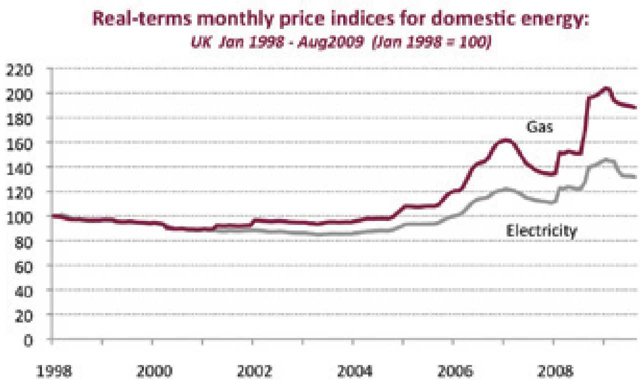



**Chart 13: Trends in domestic energy costs**

Source: DECC, *Quarterly Energy Prices*, Tables 2.2.1 & 2.3.1

Recent action announced to support those low earners who do enter crisis are also steps in the right direction. The Debt Relief Orders introduced in April this year make it easier, and less damaging in the long-term, for people to declare themselves bankrupt. More work could be done to **extend the range of low cost, out-of-court remedies targeted at debtors with low incomes and assets**, given the extremely tight restrictions that surround the Debt Relief Orders. Chart 12 shows how personal insolvencies are likely to lag behind a recovery in output, and so work needs to begin now in order to ensure that a wider range of options are available for 2010 and 2011.

In addition **there needs to be a sharper focus on fair practices around debt collection and recovery** in the first place. For many low earners, their arrears are in their council tax, rents and utility bills. Public bodies and energy providers need to show the same degree of forbearance as many of the mainstream money lenders, focusing on helping people to manage their debts rather than enforcing collection practices that will worsen a household's finances during the recession. **Further work is needed to ensure that utility companies, like credit card companies, are adopting appropriate forbearance practices**. This is particularly important given the sharp increase in fuel costs, shown in Chart 13.

Finally, **efforts must be redoubled to ensure that people are getting the support to which they are entitled**. Take-up rates of in-work support are typically very low – for example, for Housing Benefit it is just 50 per cent. Take-up of Working Tax Credit has been low in families without dependent children, with HMRC estimating that in 2006-7, despite recent increases in take-up, 1.2 million families without dependent children were eligible but had not claimed the tax credit.[29]

[28] Department for Business, Innovation and Skills, *A Better Deal for Consumers: Delivering Real Help Now and Change for the Future*, July 2009 http://www.berr.gov.uk/whatwedo/consumers/consumer-white-paper/index.html
[29] Her Majesty's Revenue and Customs, *Child Tax Credit and Working Tax Credit: take-up rates 2006-7*, (HMSO, 2009) http://www.hmrc.gov.uk/stats/personal-tax-credits/cwtc-take-up2006-07.pdf

## (2) Smoothing transitions

*Transitions matter, as changes in circumstance can often trigger crisis. The recession is increasing the likelihood of transitions for low earners, whether it is losing a job, losing a house or experiencing a drop in income from reduced hours. Ensuring that losing a job does not automatically lead to crisis for low earners is a significant challenge, given the likelihood that they were already living on the edge of their means and supplementing monthly income with the use of credit. But specific actions can be taken to smooth transitions, so that changes in circumstances do not lead to an inevitable crisis.*

**Summary – work**

- Tackle cultural barriers of Jobcentre Plus for low earners and build capacity of staff to deal with a new client base
- Reform welfare to work programmes – through bringing forward the enhanced skills assessment from 26 to 13 weeks, assessing employability by time out of work rather than by time on benefits, and focusing targets – one on incentives for Jobcentre Plus advisers to drive people towards skills and training, and one on sustainable work to improve links between out-of-work and in-work support
- Make it easier to combine jobs and training – for example, widen the eligibility of Working Tax Credit so that training as well as paid work counts – even if for a time-limited period – and remove disincentives for one partner to find a job if the other is accessing state-support training

The Pre-Budget Report of November 2008 committed an extra £1.3 billion to support Jobcentre Plus delivery, including the recruitment of 6,000 new advisers. Since then, the Employment Summit in January 2009 announced a further £500 million to support job seekers. Budget 2009 provided an additional £1.7 billion over two years for the Department for Work and Pensions to ensure that Jobcentre Plus has the capacity to meet the needs of a growing number, and changing profile, of clients. **Ensuring that Jobcentre Plus is configured to help low earners is essential**: before they even walk through the door, many low earners do not perceive that Jobcentre Plus is for them and early evidence suggests that there remains a mismatch between what advisers have been trained to do, and what low earning clients need.[30]

The recession has accelerated the reforms to the welfare-to-work system which were already underway. A shift towards active labour market policies is a step in the right direction, but it remains the case that more could be done to respond to the needs of low earners, many of whom already have the basic qualifications and employability that the current system is designed around. For example, **enhancing the existing 'light touch' skills assessment that takes place 13 weeks after someone has lost their job** could make all the difference to low earners – rather than making them wait the current 26 weeks before being offered a formal skills assessment. This would need to be coupled with **stronger incentives for Jobcentre Plus staff to refer their clients on to skills development and training courses**.

The system also needs to be geared more effectively towards employability and sustainability. This will require a cultural shift, which can be encouraged by refining existing metrics and targets. For example the Social Market Foundation has argued **that measuring someone's total time out of work over the past two years, rather than their total time on benefit**, is likely to be a better guide to understanding what further support that individual needs to be ready for work.[31] We agree, and would also argue for an extension in the definition of sustainable work. '**Sustainable' needs to mean 12 to 18 months, not 13 weeks** – and welfare-to-work providers should be encouraged to focus on this goal by a system of escalating payments. This approach should help to strengthen the connections between out-of-work and in-work support, which are not as strong as they need to be in the current system.

Part of an agenda to manage transitions must also focus on finding more ways of enabling people to combine work and training, even if these are temporary recession-focused measures. There are some specific ways in which this objective could be met. For example, **training could count towards the Working Tax Credit eligibility requirement** to work 16 hours a week. In addition, the strong disincentive that currently exists for one partner to take a job if the other is accessing state-supported training while out of work needs to be removed. The reward for work should be access to training, rather than a reduction in opportunities. Equally, the disincentives for taking on a job while participating in training need to be identified and removed.

[30] McNeil, C. *Now It's Personal: personal advisers and the new public service workforce*, (Institute for Public Policy Research, 2009) http://www.ippr.org.uk/publicationsandreports/publication.asp?id=672
[31] Mulheirn, I., Foley, B., Menne, V., Prendergrast, J., *Vicious Cycles: sustained employment and welfare reforms for the next decade* (Social Market Foundation, 2009) http://www.smf.co.uk/vicious_cycles.html

**Summary – housing**

- Limit the impact of repossession if it does happen – for example, by introducing lower-cost, out-of-court remedies for repossession based on the Debt Relief Order model that was introduced earlier this year
- Exit strategies from temporary recession measures need to take account of projected repossessions and the possibility of a rise in repossessions triggered by any increase in the interest rate in 2010

We have already emphasised the importance of clear minimum forbearance requirements as part of the existing Pre-Action Protocol, as well as ensuring that sub-prime and second charge lenders are engaging in the terms of this protocol as fully as mainstream lenders. Coupled with this, careful thought should be given to the repossession process. Clearly it is never desirable that a family should have to give up their home but in cases where this is the best or only remaining option, the process should minimise the risks of it triggering further crisis in the household. **As well as forbearance measures, making it easier for low earners to move out of unsustainable home ownership as a last resort will be an important part of safeguarding this group**.

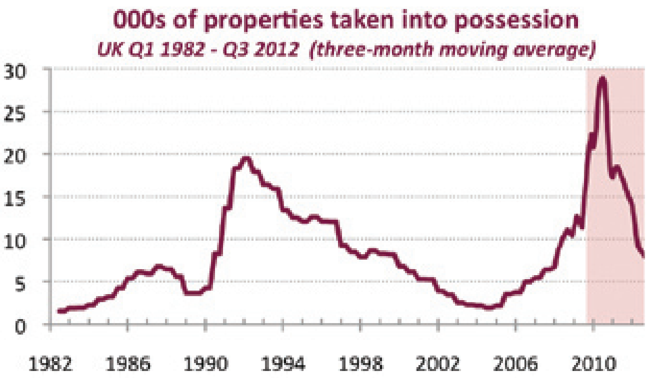



**Chart 14: Repossessions: 1982-2012**

Note: 2009 projections based on analysis of CML forecasts. Projections from 2010 onwards based on assumption that 1 per cent change in unemployment produces a 3 per cent change in possessions.

Sources: Outturn: CML, *Table AP4*;

Projection: CML, *Market commentary,* 22 June 2009*;* HMT*, Forecasts for the UK economy: A comparison of independent forecasts*, August 2009, Table M5

The introduction of the Debt Relief Orders earlier this year was a very positive development that made it much easier for people whose finances were unsustainable to declare bankruptcy without it impacting permanently on their lives. **Similar low-cost out-of-court remedies now need to be designed to ensure that transitions out of homeownership do not have long-lasting impact on people's lives**. This is urgent work as three factors likely to increase repossession come together in early 2010, as Chart 14 shows: first, the continued rise in unemployment; second, an anticipated increase in interest rates during 2010; and third, the increased appeal of repossession as a viable option for lenders thanks to an improved housing market.

This last point underlines the importance of government continuing to work with lenders as the UK officially moves into recovery and house prices begin to improve. **It is vital that measures lenders are putting in place now do not come to an end too abruptly, and that careful consideration is given to exit strategies out of recession-specific government schemes to support homeowners**. Failure to maintain forbearance measures will risk generating a significant growth in repossessions that might otherwise be avoided.

**Summary – finances**

- Speed up processing times for Housing Benefit and Council Tax Benefit; improve run-on times and reduce sensitivity to changing circumstances
- Consider a simplified Housing Benefit and tax credit system where payments are fixed for six month periods to provide greater certainty of income for low earning households and to reduce processing errors and administrative costs

The political prominence of debates around welfare-to-work in recent months has put the spotlight on people's transitions back *into* work. However, the experience of moving from work to unemployment – a key issue during the recession – is also significant for low earners. Ensuring that this transition is smooth, and that benefits and support reach people before they hit crisis, is of vital importance. Given that 44 per cent of working-age low earners have less than a months' income in savings, and given that on average councils take 26 working days to process Housing Benefit and Council Tax Benefit claims,[32] it is clear that **more could be done to improve benefit processing during these transitional periods**. Furthermore the forthcoming review of Housing Benefit should consider the merits of **extending the current 'run-on' time of four weeks**, as well as reducing the complexity of multiple tapers on different benefits as people re-enter work. It may be that in the long-term the only viable solution is the integration of Housing Benefit and Tax Credit systems.

[32] Department for Work and Pensions, Housing Benefit & Council Tax Benefit Claims Administration Quarterly Performance Data http://research.dwp.gov.uk/asd/asd1/hb_ctb/performance/performance.asp

To determine this, further work is needed on these issues. It is vital that this work starts with the reality of life on a low income, rather than with economic modelling that does not pay sufficient attention to the potential gaps between policy intention and implementation. Carefully managed transitions matter as they will affect low earners' views on how risky it is to move back into work. **For many living on low incomes, it is consistency and predictability in income that matters as much as the amount of money**. Changes in benefit levels, tax credits and other forms of support can be incredibly complex as people's situations change and the risk is that this complexity acts as a disincentive to move back into work as people fear that a further change of circumstance would put the security of their income, of 'knowing where they stand', at risk once more.

Many commentators have called for reforms to the system of tax credits and benefits over the years. There is no question that the current system is complex and that it has not been designed to cope with the reality of fluctuating incomes and changing circumstances that characterise many low earners' lives. We argue in the conclusion of this report that there is a need for a major review of income support in the round. **As a transitional measure, the government should consider a simplified tax credit system where payments are fixed for six month periods**, as was the case in the Family Credit that preceded the Working Families Tax Credit introduced in 1999. This would provide low earners with much-needed security. It would reduce the risks of processing errors and the administrative costs of maintaining the complexity of the current system.

## (3) Building on low earners' capabilities

*People who juggle life on a low income are often proud of their ability to cope with limited resources, and this resilience should be supported in every way possible, all the more so at times when the risk of job loss could threaten to destabilise and demoralise low earning households. Empowering low earners to take control of their own futures should be an integral part of responding to the economic downturn. The recommendations in this section are primarily focused on how to begin to address issues that cannot be resolved immediately, but which have been highlighted as priority areas by the recession.*

**Summary – work**

- Attract greater numbers of small and medium sized enterprises to participate in the recently expanded Local Employment Partnerships
- Introduce more incentives and requirements on employers entering Local Employment Partnerships – for example, make flexible working options available from day one rather than 26 weeks and develop a quality part-time jobs market, as well as making stronger commitments to training and job guarantees
- Ensure that the individual Skills Accounts pass genuine purchasing power into the hands of low earners through attaching real money to them, and coupling the accounts with meaningful advice about careers as well as individual qualifications or courses

As Chart 3 showed, there are some indications that the recession has led to an increase in low paid temporary employment and zero hours contracts, and also that the people doing these jobs are not always choosing them. The growth of such casualised labour has obvious implications on opportunities for workers to learn new skills through their employers and this, coupled with poor incentives for companies to invest in low-paid workers, leaves low earners in a position of potential weakness when it comes to progressing in the workplace.

Furthermore as we showed at the start of this report, the recession is hitting those areas which were already short of jobs, with weak economies. For low earners, concentrated as they are in these areas, it will be vital to build coalitions of local skills providers and local employers in order to identify real jobs and connect them to meaningful training opportunities. In this context the commitment by the Department of Work and Pensions in September 2009 to invest more in Local Employment Partnerships is welcome.

**More should be done to attract small and medium sized enterprises – major employers of low earners – into these partnerships**. And there could be greater incentives and requirements placed upon the employers who join these partnerships to make commitments to investing in the training and development of their workforces. For example, **employers joining the LEP could be required to offer flexible working options from day one, rather than at 26 weeks**, thus overcoming some of the barriers to work that low earners face. They could be encouraged to **lead the way in developing a quality part-time jobs market**, so that people unable to work full time are not forced to downgrade their pay or skills in order to find work that fits with the rest of their lives.

The right to request time at work for training, introduced in 2008, aimed to give employees a better chance of investing in their own career, giving them a better chance of accessing learning if they want it. But this measure alone is unlikely to be enough to empower low earning workers, all the more so as a tighter economic climate may increase the chances of that request being turned down.

What holds more promise are the current trials of Individual Skills Accounts, due to be rolled out nationally in 2010. By attaching funding for adult education to the individual, there is a greater chance that government money is spent on developing the UK workforce, rather than subsidising individual employers whose main interest is likely to be in ensuring people can do their current jobs rather than preparing them for their next move. Low earners whose options for progression are often limited should benefit from this approach, and it could potentially enable them to access the 37 per cent of vacancies that were not filled because employers could not find a suitably qualified candidate.[33] However we have some concerns that the current direction of travel is not bold enough: to work for low earners, **the skills accounts must pass genuine purchasing power into learner hands**.

33 Learning and Skills Council, *National Employers Skills Survey 2007* May 2008 http://research.lsc.gov.uk/LSC+Research/published/ness/

This represents a significant development of the current skills policy framework. While the notion of a 'demand-led' skills system is almost as old as skills policy itself, since the publication of the Leitch review of skills in 2006[34] the ambition has been understood primarily in terms of *employers'* demand. As a consequence much of the focus of skills policy in recent years has been about how to engage employers in determining the flow of funding and the balance of qualifications and accreditations. The creation of the Sector Skills Councils and more recently UKCES are just two institutional examples of this policy agenda. At the same time as further restructuring the organisation of adult learning, the introduction of Train to Gain as the primary mechanism for state-supported in-work training aimed to enable employers to seek out the courses they wanted and needed.

In order to widen the meaning of 'demand-led' skills to encompass employees as well as employers, two further elements of the skills accounts are necessary if low earners are to benefit from these latest reforms of the adult learning system. First, **funding for skills must be attached to skilled and appropriate advice about career options**. The Adult Careers Advisory Service which is being rolled out over the next 18 months should focus on careers, not course advice, delivered by personal advisers who are knowledgeable about the full range of options available to someone.

Second, flexibility should be given to personal advisers and their clients when it comes to identifying what training is of real use and value to them. **The emphasis needs to be on improved employability first, and qualifications second**. This shift would require the development of new proxies for measuring skills acquisition that go beyond formal qualifications alone, such as 'improved employability'.[35] It is clear that unless individual skills accounts herald a move towards a genuinely demand-led system, it is unlikely that low earners will benefit from this latest reorgainsation of the adult education system.

**Summary – housing**

- Increase the security of private rented sector for low earning tenants – building for example on the pioneering work in this area in the Republic of Ireland
- Redress the balance between landlords and tenants – through introducing the proposed National Landlord's Register and ensuring that local councils are pro-active in building this register
- Help people who would be able to enter homeownership sustainably to save for a deposit through intermediate rent schemes such as the Rent to HomeBuy scheme

There is a particular need to redress the balance between low earning tenants and landlords. While the flexibility of tenure offered by renting may suit younger low earners who want or need to be mobile, for other low earners, that flexibility translates into insecurity, with short-term tenure arrangements and few tenant rights in place in the UK system.

Such insecurity is not an inevitable characteristic of the sector. For example, in the Republic of Ireland, after a six month probation period, the tenancy is extended to three and a half years. The Irish government has also recently worked with stakeholders to secure even further security when procuring social housing from the private rented sector. The probation period has been reduced from six months to four months in return for a four year secure tenancy following the probationary period. To date this has been deemed a success by tenants and landlords alike, with no increase in failed tenancies or evictions. **Government and landlords could work together to explore similar models to the Irish one that are designed to enhance the security of the private rented sector**.

As the sector grows there is more interest from Ministers and the government in developing a viable private rentals market. The recent Rugg Review made a series of recommendations about how to enforce higher standards and weed out rogue traders.[36] **The commitment to creating a National Register of Landlords in order to identify rogue landlords is a good one and it must be delivered on**. For it to be truly effective, local authorities will need to use this register pro-actively identify bad practice, rather than simply relying on tenure complaint alone – particularly as many tenants do not complain for fear of 'retaliatory eviction'.

[34] HM Treasury, *Prosperity for All in the Global Economy: world class skills* (HMSO, 2006) http://www.hm-treasury.gov.uk/leitch_review_index.htm
[35] This was a recommendation in O'Leary, D., Oakley, K., *The Skills Paradox: confronting inequality in adult learning* (Demos, 2008) http://www.demos.co.uk/publications/theskillsparadox
[36] Rugg, J., Rhodes, D., *Review of Private Rented Sector Housing* (Department for Communities and Local Government/University of York, 2008) http://www.york.ac.uk/inst/chp/Projects/PRSreview.htm

As the first section of this report outlined, accessing a deposit is a key barrier for many low earners who would otherwise be able to enter homeownership sustainably. This situation has been compounded by the recession and overcoming this barrier to homeownership is an important element of empowering low earners. **The UK should incubate and support the development of new intermediate market models**, such as the one being developed by the Bromford Housing Group. They have introduced a 'try before you buy' scheme, which enables qualifying people to live in a new home while paying 80 per cent of market rent. The lower rent level enables them to save for a deposit over three years; after this they can then buy the property on a shared ownership basis of as little as 25 per cent, requiring a deposit only for this part of the property.

**For those low earners only able to build up a small deposit, an insurance scheme could also help**. Again, there are examples that could be developed further, including the Canadian Mortgage Insurance scheme where lenders must obtain insurance on high loan-to-value mortgages. Similarly, it would be helpful to revisit the role local authorities played in providing people with mortgage guarantees throughout the 1970s and into the 1980s. These guarantees meant that building societies relaxed their deposit requirements for low and moderate income households.

**Summary – finances**

- Place the funding for debt advisory services on a more sustainable footing
- Build the capacity and extend the provision of financial advice during the recession so it encompasses financial health in the round as well as debt specifically
- A national Money Guidance service should be rolled out as a matter of urgency in 2010
- Maintain and if possible extend saving products that work for low earners such as the Child Trust Fund and the Savings Gateway. Engage employers in supporting low earners to save
- Deliver on commitment to introducing auto-enrolment for pensions by 2012 and enable employers to participate voluntarily before this date

Debt in itself is not always a problem, and some types of debt are better than others, but it can create difficulties for people when there is a change in income, or a shift in the external environment which makes servicing those debts more expensive. Concern about indebtedness has grown in recent years, and a growing amount of public funding has been given to the debt advice sector. Much of this funding has been distributed via the government's Financial Inclusion Fund, which supports 16 face-to-face debt advice projects across England and Wales, costing at total of £47.5 million between 2006 and 2008.[37] Further funding has been made available for the current spending period (until 2011) of £85 million – an overall reduction on the money available between 2006 and 2008.

Government data indicates that by early 2009, 193,500 people had benefited from these services. There are other sources of public funding, notably the Legal Services Commission. Although it is hard to estimate the total spend on debt advice, government sources provide approximately two thirds of the money for current services, with local councils being the most significant contributors within this.

The recession has reinforced existing debates about the need **to place the funding for debt advisory services on a more sustainable footing**. The Friends Provident Foundation estimates that the financial services industry contributes three per cent of the total funding for debt advice services.[38] Public ownership of banks could be a useful driver for growing this contribution. More could also be done to extend current bank commitments to investing in financial capabilities, such as Nationwide's investment in training 1,300 new voluntary advisers, and NatWest's commitment to providing free and impartial advice at over a 1,000 local branches. The Financial Services and Business Bill being introduced into Parliament in the Queen's speech this autumn includes legislation to fund Money Guidance (generic financial advice aimed at low income households). This will be accomplished by extending the existing levy on FSA-regulated companies to encompass consumer credit firms. **This is welcome but it must complement and support existing advice services, rather than replacing them**.

[37] Gillespie, M., Dobbie, L., *Funding Money Advice Services: exploring sustainable models for the UK* (Friends Provident Foundation, 2009) http://www.friendsprovidentfoundation.org/reports.asp?section=000100010003&itemid=194
[38] Gillespie, M., Dobbie, L., ibid.

As well as expanding and diversifying the funding of the debt advice sector, there is an urgent priority to **build the capacity and extend the provision of debt advice during the recession**. Projections about unemployment, repossessions and personal insolvency indicate that debt problems will continue long after the UK formally enters a period of recovery, and currently the sector is not well-prepared to meet this demand. Creative ways of expanding the sector – for example providing volunteering opportunities for people who have lost their jobs, or seconding financial sector employees into debt advice services during the downturn – should be explored alongside growing mainstream provision.

Thinking specifically about low earner needs, and how these can be met, it is also clear that focusing on debt advice in isolation is not going to be enough to help them avoid crisis during the economic downturn. **Advice needs to be available for low earners before they miss their first payment**. While crisis or remedial work is vital during this period, there needs to be a better balance between this and the equally crucial preventative work.

Earlier research conducted by the Resolution Foundation shows that increased access to financial advice could ultimately boost retirement income for low earners by up to £1500 each year,[39] and save the state up to £100 million within the first ten years as better financial decision making lifts people clear of the threshold for receiving pension credit. **The commitment to rolling out a generic financial advice service, in the form of Money Guidance,**[40] **must be rapidly implemented**. The introduction of Money Guidance provides an opportunity to develop a money advice sector that includes debt advice but which takes a wider view, enabling people to access guidance about the appropriate balance between the use of credit, debt repayment and investing in saving and pensions products. Action to develop the sector and reduce fragmentation within it needs to happen quickly, before interest rates rise again next year, bringing with them a new set of financial difficulties for low earners.

We know that low earners are much less likely than higher earners to have the safety net of savings and insurance products to see them through difficult times. Furthermore, rises in food and fuel costs, plus increased debt payments and sometimes reduced incomes mean that low earners are finding it harder than ever to save, despite the majority of low earners saying this is something they would like to do as a means of looking after themselves and providing security for their families.

More now needs to be done to protect and develop the market for savings products that work for low earners. During a time of public spending cuts, people should be given every possible opportunity to save for their futures. **Evidence to date shows that the Child Trust Funds are a very popular savings product among low earners and such products should be protected for the low earner income group**. Recent research shows that savings rates by families on behalf of their children have trebled since the introduction of the Child Trust Funds, and the amount families are saving each month has also increased by 60 per cent, from £15 to £24. 30 per cent of low income families are paying something into their account each month. Families participating in the research talked of the importance of saving for their children, and of their determination to ensure that they did not have to 'do without'[41].

[39] Resolution Foundation, *A National Dividend: the economic impact of advice*, 2006 http://www.resolutionfoundation.org/documents/Summary.pdf
[40] This has been announced in HM Treasury, *Reforming Financial Markets* (HMSO, July 2009) http://www.hm-treasury.gov.uk/d/reforming_financial_markets080709.pdf
[41] Lawton, K., *When Times Are Tough: tracking household spending and debt through diaries interim report* (Institute of Public Policy Research, 2009) http://www.ippr.org/publicationsandreports/publication.asp?id=705

## (4) Shaping markets

Responses so far to the recession have been led by large-scale state interventions. And yet, across all the areas our report has considered – the labour market, workforce development, consumer credit, savings, home ownership and the private rental sector – a mixed economy is in play. Positive outcomes are shaped not only by government action, but also by a whole host of other players, including employers, banks, third sector organisations and businesses. This is particularly true for low earners, who find themselves squeezed in these mixed economies, too rich to qualify for substantial state support, and yet too poor to benefit from the full range of opportunities provided by private markets.

The recognition that government alone cannot achieve the positive outcomes it desires should not lead to the conclusion that its best option is to step aside. If the recession has reminded us that governments can be powerful, it has also reopened questions about the role of the state in relation to the market.

Too often government sees itself as an agent there to address market failure, rather than understanding its potential role as a pro-active market shaper. In this section we explore what a market-shaping role might look like in practice. The recession has highlighted three mixed markets where more work to develop them would greatly benefit low earners: affordable credit; the private rented sector; and intermediate skills. As the UK moves slowly towards a period of recovery and a public spending squeeze, careful consideration will need to be given to how these markets can develop effectively, fairly and sustainably.

### *Affordable credit*

A positive outcome of this recession would be the emergence of a more diverse, sustainable affordable credit market, in response to the greater expense and reduced availability of credit since 2007.

Attempts to build an affordable credit market have so far relied heavily on government subsidy, primarily through the Growth Fund which has disbursed £80 million to date through Credit Unions and Community Development Finance Institutions. The commitment of a further £18.75 million in 2008 should enable lenders to make an additional 85,000 loans by 2011, saving borrowers the equivalent of £36 million in total. Credit Unions have undoubtedly developed in recent years, with many now offering a range of services including basic banking, new forms of savings products and higher risk models of affordable credit. But it remains the case that Credit Unions are responsible for just £0.4 billion of the £233 billion credit market in Great Britain, and their overall penetration has risen only slightly between 1999 and 2007, with the national membership rate increasing from less than one per cent to 1.5 per cent.

While direct state funding is important, the government also needs to take a pro-active role in encouraging and shaping a more diverse affordable credit market that draws in the capital required to build sustainable models. There are many opportunities to kick-start this work at the moment: the commitment to reform the Social Fund, a new place in the nation's affections for a Post Office People's Bank, and the potential role housing associations and de-nationalised banks could play in this market are all under-realised opportunities currently. The time is right to invest more in developing this market, and to support the innovative ideas that people are already incubating, such as the MyHome Finance model that is being developed by the National Housing Federation.

### *Private rented sector*

The fact that more low earners are being driven to private rented accommodation as a result of the recession has highlighted the need to develop this market, as well as the affordable credit market. The private rented sector resembles a cottage industry with accommodation being supplied by large number of small landlords: 73 per cent of all landlords are individuals or couples.

The private rented sector should be an attractive option for investors, both because of the stable income returns (rent) and high total returns (rent plus capital growth). But barriers stand in the way, including the relatively low level of income return on residential property compared to commercial property and the uncertainty of the income scheme thanks to short-term leases in the UK.

A report by Savills, commissioned by the British Property Federation and GLA Economics, identified a number of recommendations for change, including encouraging the development of a 'build to let sector', through changes to Stamp Duty and more flexible application of Section 106 to the PRS market.[42] There has been some progress through the Home and Communities Agency's Private Rentals Finance Initiative, but this will only produce 10,000 properties over three years.

The question of how to overcome the barriers to large-scale institutional investment needs to be addressed in the next few years as a priority, in order to make renting privately a viable, secure and desirable tenure for people as well as an attractive option for investors. As well as an institutional approach to this question, similar to the German model where investors work side by side with landlords, there is a need to explore a venture capital approach to financing large numbers of small landlords, given the current make up of the UK private rented sector.

[42] See press release http://www.bpf.org.uk/newsroom/pressreleases/document/23388/build-to-let-could-solve-housing-crisis

*Intermediate skills*

One of the premises that current skills policy is based upon is that employers and employees can see a clear return on investment in accessing training, and that the primary explanation for why some employers do not offer training is the complexity and inaccessibility of the adult education system. In fact, this is only true in some circumstances. For example there are clear returns for gaining basic skills rather than no skills, and for acquiring higher level skills. These returns can be shown for the individual, through wage increases, and for businesses and the economy through a growth in productivity.

However these returns are much less obvious for intermediate skills, in particular for Level 2 and Level 3 skills. Of course this is not a universal picture, and there are differences on returns between sectors and industries, and between vocational and academic qualifications, but nevertheless research has shown that the wage premium on qualifications at Level 2 or below are virtually non-existent.[43] Indeed, the rate of return for vocational qualifications does not become positive until after Level 3, and is even higher at Level 4.

To date the government has worked hard to respond to feedback from employers about how to make investment in basic skills more attractive. For example, in October 2008 it was announced that funding rules around full-length qualifications would be relaxed, enabling employers to access funding for 'bite-sized chunks', reflecting the fact that 62 per cent of employers regarded disruption to work patterns as a major barrier to offering training.[44] Responding to the 46 per cent of employers who felt that lack of knowledge about training options was a barrier, the government introduced a network of 'skills brokers' to help small and medium sized employers identify and plan for their training needs.

However many of these positive developments have focused primarily on encouraging employers to invest more in basic skills. While this is important work, there is an urgent need to look again at the incoherent approach the UK has to intermediate skills, where it is not clear whether government, employers or individuals are responsible for funding or supporting these skills.

For example, as Table 7 shows, last year just 8 per cent of all qualifications gained through the government-funded Train to Gain scheme were at Level 3. There is little evidence that employers see the value of investing in these skills either: research shows that there are few incentives for businesses producing low value-added products, and as Chart 4 showed, employers are more likely to see the value of investing in high-skilled workers. As long as companies can continue to operate profitable business models that do not require a significant investment in developing their workforces, there is little pressure from the market to focus on intermediate skills.

**Table 7: Train to Gain starts and completions by level of qualification: UK 2007/08**

| | Starts | | Completions (achievements) | |
|---|---|---|---|---|
| | Number | Proportion | Number | Proportion |
| Full Level 2 | 263,900 | 76% | 154,100 | 82% |
| Full Level 3 | 43,000 | 12% | 14,100 | 8% |
| Skills for life (literacy and numeracy) | 39,200 | 11% | 19,000 | 10% |
| Other | 0 | 0% | 100 | 0% |
| Total | 346,200 | 100% | 187,300 | 100% |

Source: ONS, *Statistical First Release on Post-16 Education & Skills: Learner participation, outcomes and Level of Highest Qualification held*, Table 6, June 2009

Other countries have sought to address this issue in different ways. In France the government requires firms to spend a proportion of their wage bills on training. In Singapore, differential tax rates are applied to firms depending on whether they employ high-skilled or low-skilled workers.[46] There is a question about whether employers, government or individuals should hold responsibility for investing in these intermediate skills; evidence to date suggests that the labour market alone will not drive such investment, and this is to the detriment of low earners.

43 Dickerson, A., *A Study on Rates of Return to Investment in Level 3 and Higher Qualifications* (2005). See also Vignoles and Powdvathee, 2006, and Dickerson 2005

44 Shury, J., Davies, B., Riley, T. Skills for the Workplace: employer perspectives (UKCES, 2008) http://www.ukces.org.uk/upload/pdf/Employer%20Perspectives%20Evidence%20Report%20for%20website_1.pdf

45 Mason, G. *Enterprise Product Strategies and Employer Demand for Skills in Britain: Evidence from the Employers Skill Survey* (SKOPE Research Paper Series no. 50, University of Warwick 2004)

46 *Skills Paradox*, ibid.

## Conclusion

The heavy reliance on the financial sector and a booming housing market to fuel growth in the years prior to the recession has led to questions about the extent to which the UK economy is suffering from structural weaknesses rather than cyclical issues alone. Some have argued that actions taken since the recession began – for example keeping interest rates low, introducing quantitative easing to pump credit into the banking system, and allowing the public deficit to grow – have masked the full scale of these structural weaknesses. While there are still questions about how significant changes will need to be to put the economy back on a more stable footing, most analysts now agree that there will be some degree of restructuring as the UK emerges from recession.

In the coming years, at the same time as rebuilding the economy and facing up to the challenges and costs of a rapidly ageing population, government will be under intense pressure to bring down public debt and the deficit. Questions about the urgency of this task or the best way to go about it are still far from resolved. There is little agreement among the public[47] or between politicians, let alone between economists,[48] about the appropriate balance between spending cuts and tax increases, the severity of our current situation, or about the speed with which public debt needs to come down.

Despite these disagreements, it is widely accepted that difficult decisions will need to be made about priorities. Much of the debate is focused on saving money through efficiencies, means-testing benefits that are currently universal, or cutting programmes entirely. **These savings should be made with great care, to ensure that the impact is progressive rather than regressive**, to ensure that low earners do not bear the brunt of spending cuts.

Furthermore, the analysis that underpins this report shows that many of the effects low earners are feeling now are not simply the product of the recession, but also a reflection of trends and patterns that were in existence well before the credit crunch took hold. In other words, the recession has compounded the vulnerable and exposed position low earners were in, even in better times. Protecting low earners from the worst impacts of the recession cannot be done in a vacuum.

It is therefore essential that actions taken now do not run contrary to longer-term priorities. The Work Foundation has argued that actions taken to mitigate the impact of the recession must be timely, targeted and temporary.[49] Our analysis would support this, and we would add that actions should also be governed by the principles of fairness – ensuring that certain groups in society do not disproportionately bear the brunt of the recession – and foresight, to ensure that what is done now does not have unintended consequences in the future.

It is important to distinguish between two policy objectives when it comes to tackling the issues low earners face. One objective is to improve matters for people living on low incomes – ameliorating the worst effects of the situation and maximising the impact of redistributive mechanisms. The other is to build more ladders up and out of the group, focusing on progression to ensure that time spent as a low earner is minimised as much as possible. Our view is that both strategies are necessary and important – but there is a need for clarity about the difference between the two when considering action.

This report has not sought to address these wider questions about redistribution and progression directly. But there is no question that longer-term trends – towards a more stratified labour market, and the regressive nature of many asset-building initiatives such as home ownership, savings and pensions – are just as significant as the recession's direct impact on low earners.

So as well as taking action to protect low earners from the worst effects of the economic downturn, **there is also a need to consider what can be done to ensure this recession does not entrench social and economic trends that have increased the gap between the richest and poorest and reduced social mobility over the last generation**. The question is whether today's exceptional economic circumstances – coupled with an unstable political environment – will open up a useful wider debate about how and why low earners came to be in such a vulnerable position in the first place.

Addressing these questions would require:

- A fundamental review of the nature, extent and mechanisms for **in-work support** – covering the benefits, tax credits and taxation system and the interactions between them

47 Ipsos MORI *Public Spending Index* 2009 http://www.ipsos-mori.com/researchpublications/researcharchive/poll.aspx?oItemId=2374
48 See recent debates between Mervyn King and Adair Turner http://www.guardian.co.uk/commentisfree/2009/oct/25/will-hutton-mervyn-king-bank-reform
49 Brinkley,I., Clayton, N., Coats, D., Hutton, W., Overell, S., *Hard Labour: jobs, unemployment and the recession* (Work Foundation, 2008) http://www.theworkfoundation.com/research/publications/publicationdetail.aspx?oItemId=205

- A focus on the **redistribution of wealth**, as well as income. For example, 55 per cent of the tax relief on private pensions, which adds up to £10.5 billion a year, goes towards supporting those people on or near the upper rate tax.[50]
- Greater **incentives and support** for low earners to save and build assets.
- Making **in-work poverty**, which has stayed constant for a decade, a priority policy agenda. Despite a generous tax credit system and the introduction of a National Minimum Wage, one in three poor families that move into work remain in poverty[51], and over 50 per cent of children living in poverty now have a parent in work, compared to 40 per cent in 1992.[52]
- Putting **quality of work (including part-time work)** alongside increased productivity and global competitiveness when it comes to industrial policy.

The damaging effects of previous recessions on those people worst hit by them has been well documented. Avoiding and minimising this long-term impact must be top of the policy agenda. In addition, as government begins to look towards a period of gradual recovery, coupled with significant public spending cuts and likely tax increases, the challenge is to ensure that this recession does not reinforce or enhance the pattern of polarisation and stratification that could be traced long before the downturn took hold.

A study of previous recessions by the Institute of Fiscal Studies has shown that a rise in inequality is not an inevitable consequence of recessions. Indeed inequality fell in the 1970s recession and stayed steady in the 1990 downturn. However avoiding the sharp rise in inequality that accompanied the 1980s recession will take concerted action – by government, employers, regulators and the market – to guard against low earners bearing a disproportionate burden of this downturn, and to ensure that they can participate fully in a return to economic growth in coming years.

[50] Quoted in Child Poverty Action Group's letter to the Chancellor, November 2008 http://www.cpag.org.uk/info/briefings_policy/CPAG_PBR_letter_041108%20.pdf
[51] Harker, L., *Delivering on Child Poverty: what would it take?* (Department for Work and Pensions, 2006) http://www.dwp.gov.uk/publications/policy-publications/harker.shtml
[52] Kenway, P., Addressing In-Work Poverty (Joseph Rowntree Foundation, November 2008) http://www.poverty.org.uk/reports/in-work%20poverty.pdf

# Annex 1: PROJECTIONS

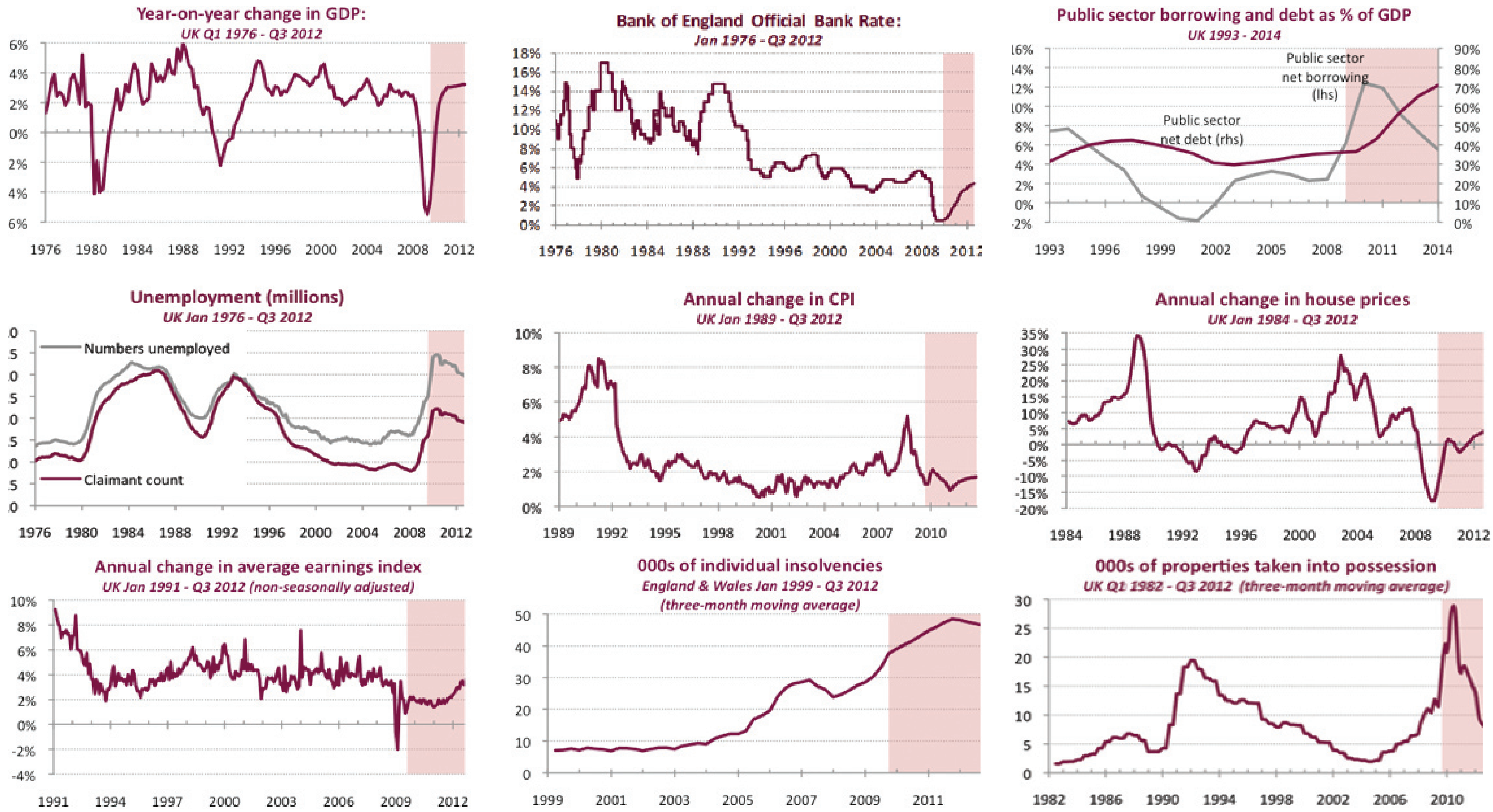



**Chart 15: Economic trends and projections: 1976-2012**

Note: *GDP & CPI* – Bank of England's modal projections, based on Bank estimates of past growth and market interest rate expectations and £175 billion asset purchases.
*Base rate* – Bank of England projections based on forward market interest rates.
*Unemployment & average earnings* – Projections based on analysis of independent forecasters' annual averages. Average earnings projections for 2011 and 2012 based on analysis of Cambridge Econometrics forecasts.
*House prices* – Projections based on analysis of ITEM Club forecast. Repossession - 2009 projections based on analysis of CML forecasts. Projections from 2010 onwards based on assumption that 1 per cent change in unemployment produces a 3 per cent change in possessions.
*Public finances* - Figures exclude liabilities and unrealised losses from financial sector interventions.
*Individual insolvencies* – Projections based on Capital Economics and KPMG forecasts for numbers becoming insolvent in each full year.

Sources: ONS Time Series, *BCJD, D7G7, IHYR, LNMM & MGSC*; • Bank of England, *Inflation Report*, August 2009; • HMT, *Forecasts for the UK economy: A comparison of independent forecasts*, August 2009, Table M5; Cambridge Econometrics, "We expect a weak and protracted UK recovery", press release 20 July 2009; • HBOS, *Halifax House Price Index*; • ITEM Club, *UK housing market*, September 2009; CML, Table AP4;CML, *Market commentary*, 22 June 2009; • HMT, *Forecasts for the UK economy: A comparison of independent forecasts*, August 2009, Table M5; • HMT, *Public Finances Databank*; HMT, *Budget 2009*; • Insolvency Service, *Insolvencies in the second quarter 2009*, Table 2; • *London Evening Standard*, "500,000 to fall into personal insolvency in three years", 7 November 2008; *Banking Times*, "Personal insolvencies up 23%", 3 May 2009

## Annex 2: Steering group members and expert participants

We are very grateful to everyone who participated in developing the analysis and recommendations of this report, particularly those organisations which partnered with us on running our three expert groups: The Work Foundation, Transct and Shelter.

### Steering group members

| | |
|---|---|
| John Andrews | Low Incomes Tax Reform Group |
| Christina Barnes | Equalities and Human Rights Commission |
| Kate Bell | Gingerbread |
| Vera Cottrell | Which? |
| Tony Dolphin | ippr |
| Carl Emmerson | Institute for Fiscal Studies |
| Simon Gallagher | HM Treasury |
| Kate Green | Child Poverty Action Group |
| Suzanne Hall | Ipsos-MORI |
| Roger Harding | Joseph Rowntree Foundation |
| Andrew Harrop | Age Concern/Help the Aged |
| Axel Heitmueller | Policy Adviser to Rt Hon Yvette Cooper |
| Nicola Hughes | Shelter |
| Jeff Masters | 2020 Public Services Trust |
| Liz Phelps | Citizens Advice |
| Peter Robinson | |
| James Sassoon | |
| Nicola Smith | Trades Union Congress |
| Jon Trigg | A4E |
| Peter Urwin | University of Westminster |
| Steve Wilcox | University of York |

### Work and skills seminar, 3 September 2009[53]

| | |
|---|---|
| John Andrews | UKGateway |
| Kat Ashby | The Work Foundation |
| Lynsey Brooks | Federation of Small Businesses |
| Annette Cox | Institute for Employment Studies |
| James Evans | Creative and Cultural Skills |
| Chris Kent | Department for Work and Pensions |
| Christa Masbruch | Turn2Us |
| Abigail Morris | British Chambers of Commerce |
| Denise Morrisroe | Equality and Human Rights Commission |
| Faiza Shaheen | Centre for Cities |
| Gareth Thomas | Learning and Skills Council |
| Matthew Wells | A4E |
| Penny Tamkin (speaker) | The Work Foundation |
| Nicola Smith (speaker) | TUC |

### Household finances seminar, 8 September 2009[54]

| | |
|---|---|
| Yasin Ahmed | Financial Inclusion Champions |
| Kat Ashby | Work Foundation |
| Louise Bamfield | Child Poverty Unit |
| Victoria Burr | HM Treasury |
| Marie Burton | Consumer Focus |
| Adam Clark (speaker) | Transact |
| Sharon Collard | Personal Finance Research Centre |
| Sam Cook | Equality and Human Rights Commission |
| John Cray | Department for Work and Pensions |
| Alison Donnelly | Consumer Council for Northern Ireland |
| Alison Fernando | Financial Services Authority |
| Matt Harris | HM Treasury |
| Axel Heitmueller | Prime Ministers Strategy Unit |
| Chris Hobson | Transact |
| Simon Horner | Shadow Treasury Team |
| Marie Kemplay | Transact |
| Carole King | Provident Financial |
| Kristina Leonnet | Quaker Social Action |
| Matthew Little | HM Treasury |
| Christa Masbruch | Turn2us |
| Gary Millner | pfeg |
| Ayesha Owusu-Barnaby | Independent Consultant |
| Cameron Robertson | Help the Aged and Age Concern |
| Kirsty Robinson | Centrepoint |
| Will Sandbrook | Personal Accounts Delivery Authority |
| Rachel Seal-Jones | ippr |
| Chris Tapp | Credit Action |
| Jon Trigg | A4E |
| Jane Vass | Age Concern and Help the Aged |
| Kathy Wade | Capitalise |
| Gareth Wallace | The Salvation Army |
| Robert Yuille | Financial Services Authority |

[53] A full record of this seminar can be found on our website at http://www.resolutionfoundation.org/documents/LeesWriteup.pdf
[54] A full record of this seminar can be found on our website at http://www.resolutionfoundation.org/documents/HouseholdFinancesnote.pdf

**Housing seminar, 15 September 2009**[55]

| | |
|---|---|
| David Arnold | Unison |
| Yolande Barnes (speaker) | Savills |
| Ravi Baghirathan | Prime Minister's Strategy Unit |
| Kay Boycott (speaker) | Shelter |
| Shane Brownie | Communities and Local Government |
| Vera Cotrell | Which? |
| Caroline Davey | Shelter |
| Abigail Davies | Chartered Institute of Housing |
| Roger Harding | Joseph Rowntree Foundation |
| Naomi Harflett | Money Advice Trust |
| Axel Heitmueller | Prime Minister's Strategy Unit |
| Andrew Heywood | Council of Mortgage Lenders |
| Denise Morrisroe | EHRC |
| Kurt Mueller | British Property Foundation |
| James Lloyd | Social Market Foundation |
| Andrew Pratt (speaker) | Grainger Plc |
| Liz Phelps | Citizens Advice |
| Karen Raven | Places for People |
| Vincenzo Rampulla | National Landlords Association |
| Laura Rous | CB Richard Ellis |
| Gavin Smart | National Housing Federation |
| Richard Tacagni | LACORS |
| Jon Trigg | A4e |
| Anthony Vigor | Prime Minister's Policy Unit |

## Technical annex: Defining low earners

The Resolution Foundation is concerned with improving outcomes for 'low earners'. From a conceptual perspective, we define this group as including those who are squeezed by the workings of the mixed economy: too poor to be able to benefit from the full range of opportunities provided by private markets, but too rich to qualify for substantial state support. From an analytical perspective, we consider the group to include those on below-average incomes who remain largely independent of state support. While median income is relatively straightforward to establish as an upper threshold, defining when people become independent of state support is more difficult, particularly as all income groups are entitled to some welfare payments. The precise definition used has therefore evolved over time and has been dependent in part on the limitations of the data sources we have analysed.

### Low earners and financial advice

Our first major project concerned the provision of financial advice to low earners. We therefore sought to establish thresholds based on the cut-off points for access to financial services industry advice at the upper level and access to services aimed at the poorest and most vulnerable (such as Citizens Advice) at the lower level. Given the subject focus, we were interested in all those without access to financial advice, including both those who lived in **low earner households** and those who could be considered **individual low earners** despite living in non-low earning households, such as young adults living with their parents and people with informal care responsibilities.

We commissioned the Alliance for Health & the Future to produce a picture of this group using data from the British Household Panel Survey (BHPS). Working-age adults were considered low earners if they lived in a household with below median household income (£22,548 in 2005) of which no more than 20 per cent was sourced from state benefits. Working-age adults were also considered to be low earners if they individually had below median individual income (£11,747 in 2005) of which no more than 20 per cent was sourced from state benefits. Older people were counted as low earners if they lived within a household with below median income or had personal income below individual median income and did not receive any means-tested benefits.[56]

Based on these thresholds, the Alliance identified a total of 15 million low earners in Great Britain, suggesting that low earners represented around one-third of the adult population. The total was comprised of 12 million working-age adults and 3 million retired. Among the working-age group, around half were considered low earners on the basis of their position in a low earner household alone, just under one-third qualified on the basis of their individual financial position alone and one-fifth met both the household and individual criteria. Of the total 15 million low earners identified, around one-half were found to have been in the group a decade earlier, pointing to the persistence of low earning for a large number of people.


[55] A full record of this seminar can be found on our website at http://www.resolutionfoundation.org/documents/Lowearnersrecessionandhousingnote.pdfP

[56] Pension Credit, Income Support, Incapacity Benefit, Housing Benefit, Council Tax Benefit, Job Seekers Allowance, Disabled Persons Credit and Disability Living Allowance.

### The low earners audit

In March 2009, we published the first ever audit of low earners. This report was designed to provide a broad picture of the experiences of the group across a wider range of policy areas than just financial advice. Although the report continued to report some of the findings from the Alliance work, we decided to focus new analysis on low earner households only, in order to remove the distortions created by capturing a large number of students[57] and non-working members of high income families.

Because the range of sources consulted for the audit was so wide, we were unable to retain the detailed definition used in relation to the BHPS – which had set specific levels of benefit-receipt as the lower threshold – and instead moved to one that established boundaries based on income only. Having identified in our first project that 30 per cent of adults could be considered low earners, we decided to concentrate on the 30 per cent of households with incomes directly below the median.

By defining low earner households simply as those in income deciles 3, 4 and 5, we were able to define two other income groups in relation to low earners: we labelled households with above-median incomes (income deciles 6-10) higher earners and those in income deciles 1 and 2 as *benefit-dependent*.

By fixing the proportion of households in the group at 30 per cent, we were able to state definitively that the low earner group comprised around 7.6 million households in the UK. However, the specific income values represented by deciles 3-5, and the number of people living in low earner households, varied depending on the method of income distribution used (see Box A1). In deciding which income distribution to base our analyses on, we were led on each occasion by what was provided in available data sources.

Some of the data sources we used in the audit included little or no information on household incomes. We therefore adopted a range of proxies based on what we knew about the group. For example, over 60 per cent of the group were in social classes C1 and C2, and around 80 per cent in C1C2D. Similarly, in determining which industries low earners worked in, we simply compared average salaries across sectors and concluded that low earners were more likely to be over-represented in low paying areas. We argued that gross household incomes of £11,650-£27,150 were equivalent to gross household wages and salaries of £8,750-£20,350 because, on average, earnings represented around three-quarters of low earner households' gross incomes.

**Box A1: Low earner-boundary variations by income distribution**

On a gross household income basis, deciles 3-5 equated to annual income in the range £11,650-£27,150 in 2007. These boundaries included around 13.2 million people: 12.4 million adults and 0.8 million children.[58] On a *disposable household income* (gross income less direct tax) basis, deciles 3-5 equated to annual income in the range £11,150-£22,900. On this measure, there were around 16.0 million people in the low earner group: 12.5 million adults and 3.5 million children.[59]

In order to compare economic well-being, household income can be weighted to calculate equivalised income. That is, household income is adjusted to reflect the cost of living implications of the household composition. For example, for any given level of household income, a household of five adults is likely to achieve a lower standard of living than a single-person household.

The boundaries of *equivalised* gross household income deciles 3-5 in 2007 were £13,350 and £25,600. Table A1 sets out a selection of income thresholds equivalent to the low earner group in 2007 and shows that a single person household could have been considered low earning on this measure if their gross household income was in the range £8,150-£15,600, while a cohabiting couple with three older children could be considered low earning with a household income in the range £26,000-£50,000. The equivalisation process increases the average household size at lower income levels. The 7.6 million low earner households therefore included around 18.0 million people on this basis: 14.5 million adults and 3.5 million children.[60] On an *equivalised disposable household income* basis, deciles 3-5 boundaries were £12,950 and £20,900, capturing around 13.7 million adults.[61]

57 The Alliance for Health & the Future's analysis of young low earners identified in their study of the BHPS found that around three-quarters would leave the low earner group within ten years.
58 ONS, *Family Spending: A report on the 2007 Expenditure and Food Survey*, 26 November 2008, Table A6
59 Ibid. Table A9
60 Ibid. Tables A6 & 3.1
61 ONS, *Effects of taxes and benefits on household income 2007/08*, Tables 14 & 15

**Table A1: Gross household incomes equivalent to decile three to five thresholds for selected household compositions: UK 2007**

| | Weekly income (£) | | Annual income (£) | |
|---|---|---|---|---|
| | Lower | Higher | Lower | Higher |
| Single no children | 157 | 300 | 8,150 | 15,600 |
| Single with child aged 7 | 211 | 403 | 10,950 | 21,000 |
| Single with child aged 14 | 226 | 433 | 11,750 | 22,500 |
| Single with two children aged 3 and 9 | 262 | 502 | 13,650 | 26,100 |
| Couple with no children | 257 | 492 | 13,350 | 25,600 |
| Couple with child aged 1 | 280 | 536 | 14,550 | 27,900 |
| Couple with child aged 15 | 344 | 659 | 17,900 | 34,300 |
| Couple with three children aged 11, 13 and 17 | 501 | 959 | 26,050 | 49,900 |
| Two adults (not couple), no children | 275 | 526 | 14,300 | 27,350 |
| Three adults, no children | 383 | 733 | 19,900 | 38,100 |
| Four adults, no children | 475 | 910 | 24,700 | 47,350 |
| Equivalised income | 257 | 492 | 13,350 | 25,600 |

Note: [1] Equivalised incomes calculated using McClements Equivalence Scale.

Sources: DWP, *Family Resources Survey 2007-08*

ONS, *Family Spending: A report on the 2007 Expenditure and Food Survey*, 26 November 2008, pp26-27

### Determining which low earners are being affected by the recession

The various definitions of low earner households used in the audit were clearly imperfect. A proportion of households in income deciles 3-5 will in truth be reliant on state support and proxies based on social class or individual earnings are likely to be even more tentative. However, the purpose of the original audit was to present a broad description of some of the pressures faced by those who are disadvantaged by the mixed economy, and the use of relatively simplistic definitions allowed us to highlight a number of issues around housing, work and household finances.

Both the audit and the BHPS analysis highlighted the heterogeneity of the low earner group: the challenges faced by older low earners are likely to be very different from those experienced by younger members of the group. In producing this report, we wanted to have a clearer idea about which low earners are being affected by which aspects of the recession. We have therefore returned to a more specific definition and undertaken a deeper analysis, which has allowed us to better understand the characteristics and experiences of different members of the low earner group.

New figures presented in this report are largely derived from an analysis of the *Family Resources Survey 2007-08* (FRS). As before, the upper threshold is based on median income. However, on this occasion, the lower threshold is set as the boundary of deciles 2 and 3 or the receipt of 20 per cent or more of income from income-related benefits. By focusing on income-related benefits we have ensured that those in receipt of universal benefits such as the state pension or child benefit are not excluded from the group. We have presented three alternative measures: **low earner households, individuals within low earner households** and **low earner benefit units**.

*Households* are defined in the FRS as 'a single person or group of people living at the same address who either share one meal a day or share the living accommodation, i.e. a living room'. So, for example, a group of students with a shared living room would be counted as a single household even if they did not eat together, but a group of bedsits at the same address would not. Low earner households are defined as having equivalised income[62] in 2007 between £257 and £492 per week or £13,350-£25,600 per year (see Table A1). Any household receiving 20 per cent or more of its total income from income-related benefits is automatically classed as benefit-dependent. On this measure, around 29 per cent of households are considered part of the low earner group.

[62] As with the low earners audit data, equivalisation is calculated using the McClements Equivalence Scale.

*Individuals within households* are allocated based on the income of the household they live in. On this measure, there are around 14.3 million low earner adults in the UK, representing 28 per cent of the total population, and 3.8 million children, equivalent to 27 per cent of the total.

*Benefit unit* is a standard DWP term that relates to the tighter family definition of 'a single adult or couple living as married and any dependent children'. A dependent child is aged under 16 or an unmarried 16 to 19-year-old in full time non-advanced education. So, for example, a man and wife living with their young children and an elderly parent would be one household but two benefit units. Unlike the *individuals within households* measure, the distribution of benefit units across the three income groups of benefit-dependent, low earners and higher earners do not map directly to the households the units live in. Instead, they are divided based on the distribution of equivalised income[63] across benefit units. Low earner benefit units are accordingly defined as having equivalised income between £261 and £443 per week or £13,600-£23,000 per year. As with households, any benefit unit receiving 20 per cent or more of its total income from income-related benefits is automatically classed as benefit-dependent. Just 22 per cent of benefit units fall within the low earner group.

### Future analysis of low earners

We will continue to review our analytical definition of low earners to ensure that it as closely as possible resembles the conceptual description. However, we are happy that the analysis set out in this report is the most closely-mapped we have yet undertaken.

We have produced a wealth of data which segments the group by age, income, region and gender, which we have used to inform much of the discussion in this paper. While we will continue to use simple income decile definitions and proxies in updates of the audit, to provide a broad picture of the condition of low earners, we will also be including some of this more detailed analysis in future editions.[64]

[63] McClements Equivalence Scale.
[64] The Foundation is aiming to update the Low earner audit three times per year. The next edition is due in December 2009.

## Notes:

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