Section 4

Prospects for household wealth in the aftermath of the pandemic

For aggregate household wealth to rise during a recession is unique in recent history, and it has important distributional consequences. Gaps between households have been exacerbated by the pandemic: the gap between average wealth for those in the fifth decile of the distribution and those at the top increased by over £40,000; and the gap between the middle of the distribution and the bottom has increased by more than three times than it did over the previous decade.

While it is key for policy makers to understand the changes in the level and distribution of wealth during the pandemic, it is also important to consider prospects for the future. Whether these gaps persist will depend on what happens to asset prices and how families respond to changes in their wealth. On the former, while there is inevitably significant uncertainty, it seems unlikely that all of the recent rises in prices will reverse (although it is possible that house prices fall in the coming months after the end of the stamp duty holiday, and with the prospect of a rise in unemployment).

Evidence on the behavioural response of families suggests there is significant uncertainty about whether the changes we have seen during the pandemic will unwind. Those households which have increased savings report that they are unlikely to draw them down and may even continue to accumulate savings at a faster rate. This would be consistent with the response to past recessions, and also with the idea that the pandemic has raised fears about future crises. Meanwhile, those households who had to increase debts during the pandemic report that, for the most part at least, they are not expecting to pay down those increased debts in the near term. Taken together, then, the legacy of the pandemic looks set to be a continuation of the pre-pandemic trends: continued growth in overall total wealth with a sizable minority of the population less able to cope with any future income falls.

This has been the first recession in at least 70 years in which household balance sheets have improved

The good news is that Covid-19 pandemic has – unusually for a recession – led to a rise in wealth and falling debts in aggregate. While it is common for households to respond to negative economic shocks by raising saving rates and reducing debt – as happened after the financial crisis, for example – the scale of the increase in total wealth since March 2020 is remarkable. In order to get economic policy making right during the recovery period, it is important the Government understands the nature of the changes in wealth and the impacts this might have, and so this Section explores the likely implications of the increase in aggregate wealth, as well as its distributional consequences.

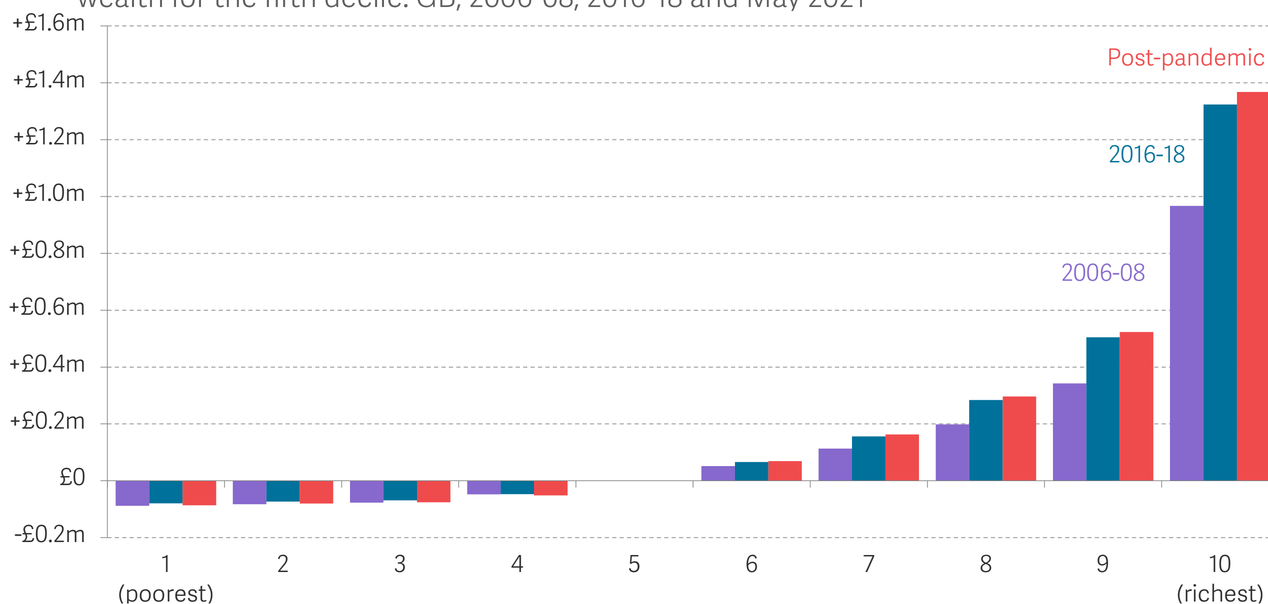
But families will feel the economic effects of the pandemic through wider wealth gaps

One clear impact of this crisis on household wealth has been a rise in the gap between families across the wealth distribution. Figure 26 updates the Figure 3 on the gap between average wealth between deciles to include an estimate of the gap post-pandemic. Wealth gaps have risen across the entire distribution: the gap between average wealth for those in the fifth decile of the distribution and those at the top, which increased massively between 2006-08 and 2016-18, grew by a further 12 per cent, or over £40,000, during the pandemic.[35] The gap between the middle of the distribution and the bottom had the largest proportional increase, where wealth increased for those in the fifth decile by £7,000 more than it did at the bottom. Gaps between the middle and the bottom have risen proportionally by more than elsewhere for two reasons: first, average wealth rises at the bottom have been moderated by low passive wealth gains and smaller absolute rises in savings (or larger absolute increases in debt); second, wealth rose in the middle of the distribution more because of higher exposure to house price appreciation.

35 This is likely to be an underestimate of the increase in wealth gaps because the WAS dataset fails to fully capture the very top of the wealth distribution, and there is clear evidence that wealth has increased at the very top of the wealth distribution substantially faster than for everyone else. The Sunday Times Rich List is the best available data for the value of wealth in the upper tail of the distribution. The 2021 list found that total wealth increased by 22 per cent over the past year, far larger than our estimated increase in wealth at any point in the distribution. For the latest Rich List see: R Watts, The Sunday Times Rich List 2021 revealed, The Times, May 2021 and for more on the materiality of the gap in WAS coverage at the top of the wealth distribution see: A Advani, G Bangham & J Leslie, The UK's wealth distribution and characteristics of high-wealth households, Wealth and Policy, Working Paper 101, October 2020.

FIGURE 26: **Wealth gaps have risen, particularly between the bottom and the middle**

Absolute gap between average family wealth within each wealth decile and average wealth for the fifth decile: GB, 2006-08, 2016-18 and May 2021



NOTES: Data is adjusted using CPIH into April 2021 prices. Wealth is measured at the family unit level - i.e. one or two adults living as a family plus any dependent children. Family composition is accounted for by taking wealth per adult within the family. The definition of wealth excludes physical wealth and private business wealth. This is because the definition of physical wealth is more subjective than other asset classes and is inconsistently defined compared to other asset classes. Private business wealth was poorly captured in the 2006-08 wave of the WAS and so is removed to reduce measurement changes over time. Post-pandemic results rely on modelling partially based on YouGov survey results. Base of analysis is all adults who responded with valid information about saving and debt changes (n=4606). These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of ONS; Wealth and Assets Survey; Bank of England, Effective interest rates; FTSE Russell, FTSE All-Share Index TR; MSCI, MSCI World Index TR; S&P Global, S&P UK Gilt Index; and ONS, UK House Price Index; YouGov, adults age 18+ and the Coronavirus (COVID-19), June 2021 wave.

Such rising wealth gaps have real impacts on the economic experience of families. Holding more wealth in absolute terms confers a range of benefits. For example, it provides higher investment income; provides greater financial resilience and enables consumption smoothing; lowers housing costs (for those able to purchase homes); and is associated with higher subjective measures of wellbeing.[36] But it is not just the level of wealth holdings that matters, but also the gaps between households. One clear example is the extra difficulty of becoming a homeowner as a result of higher house prices. Buying a property lowers housing costs relative to renting and creates a large exposure to wealth rises through increased house prices, something that is unavailable through other means (families cannot get mortgages to purchase bonds or shares, for example).[37] Wealth gaps also have a direct impact on household wellbeing – there is long-established research

36 For more details on the link between wealth and living standards see: G Bangham & J Leslie, Rainy days: An audit of household wealth and the initial effects of the coronavirus crisis on saving and spending in Great Britain, Resolution Foundation, June 2020.
37 The financial benefit of becoming a homeowner and how the costs of becoming a first time buyer have increase are covered in detail in: L Judge & J Leslie, Stakes and ladders: The costs and benefits of buying a first home over the generations, Resolution Foundation, June 2021.

showing that relative differences in incomes and wealth are key to household wellbeing, with larger relative gaps leading to lower happiness for the less well-off.[38]

Early evidence suggests that changes in household wealth will have a longer-run legacy

The additional increases in wealth gaps brought about by the pandemic sit on top a decade in which wealth has become more unequally held, and it is important that Government policy takes the implications of this into account. For example, those facing a reduction in UC in the coming months are also those who are least likely to have benefited from asset-price-driven wealth increases during the crisis. Moreover, there are good reasons for thinking that these increased wealth gaps are likely to persist into the future.

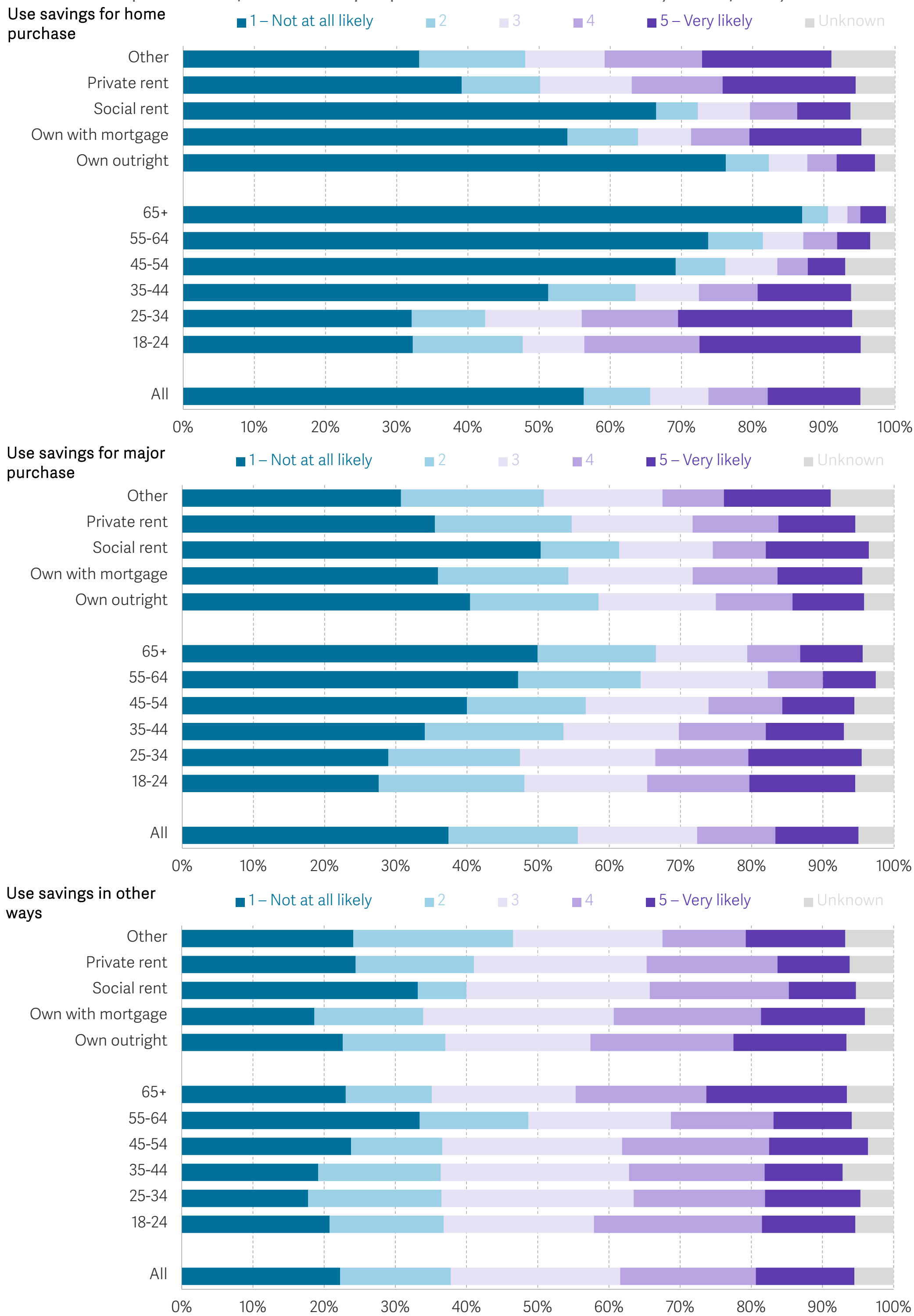
First, although the outlook is inevitably uncertain, asset price increases – the biggest driver of the wealth gaps – are unlikely to fully reverse. Financial asset prices have tended to recover in the aftermath of recessions and, for the most part, have maintained those gains until the next recession. Prices may well be volatile in the recovery, but it is likely that changes in financial asset prices will persist. As discussed above, the most important asset price for UK families is the price of housing. Here, there is a risk that house prices could fall as the stamp duty holiday ends or unemployment rises later in the year. But increases in UK house prices have been similar to those in other developed countries, suggesting a broader trend.[39] This trend could reflect that a higher prevalence of home working has boosted demand for residential space. Unless this fully reverses post-pandemic, this suggests that there could be a lasting change in the relative price of housing. Moreover, the falls in interest rates since the start of the pandemic are expected to persist, further supporting house prices.

38 See A Clark, P Frijters & M Shields, Relative Income, Happiness, and Utility: An Explanation for the Easterlin Paradox and Other Puzzles, Journal of Economic Literature, March 2008.

39 N McCarthy, The Countries With The Biggest House Price Increases In 2020, Forbes, March 2021. A Stamp Duty Land Tax (SDLT) holiday which increased the threshold at which it became payable from £150,000 to £175,000, was previously implemented in September 2008 and continued until December 2009. The policy, however, appeared to have little impact on house prices: this may be due to the fact that SDLT at the time was payable as a flat rate on the total value of a property, and so the policy only impacted the subset of the housing market valued between £150,000 and £175,000.

FIGURE 27: **Few people are definitely planning to use additional savings built up during pandemic**

Proportion of families with increased savings planning to use additional savings for home purchase, other major purchase or in other ways: UK, May 2021



NOTES: NOTES: Base is all those whose savings increased and in each of the categories listed. All (n=2238), 18-24 (n=225), 25-34 (n=509), 35-44 (n=411), 45-54 (n=353), 55-64 (n=273), 65+ (n=467), own home outright (n=705), own home with mortgage (n=837), rents home in social sector (n=117), rents home in private sector (n=366), and other or unknown housing tenure (n=213). These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ and the Coronavirus (COVID-19), June 2021 wave.

Second, there is evidence to suggest that families will not act to completely unwind changes in wealth. One way in which wealth gaps could reverse is if families plan to spend down the additional savings accumulated, or even go further and use the increase in wealth levels to fund higher consumption over the longer-term. Figure 27 presents mixed evidence on the likelihood that savings levels will be drawn down. It is important to keep in mind that this evidence relates to intentions about the future, and so comes with significant uncertainty. Nevertheless, it is striking that only around 14 per cent of people who increased saving levels over the pandemic are "very likely" to use the additional savings for some form of purchase. This would indicate that savings levels will remain elevated. However, there is some heterogeneity between groups: young people and those renting in the private sector were particularly likely to report plans to put the savings towards buying a home (which would not represent a change in wealth gap: it would be substituting one asset for another). Although relatively few people were very confident in their plans to use savings, it is also the case that relatively few people are certain to keep the additional savings. The largest group who fall into this category are the over 65s, of whom 50 per cent were "not at all likely" to use additional savings for a major purchase. Taken together, this seems to be tentative evidence that additional savings are unlikely to be fully drawn down, meaning wealth gaps are unlikely to shrink in future.[40]

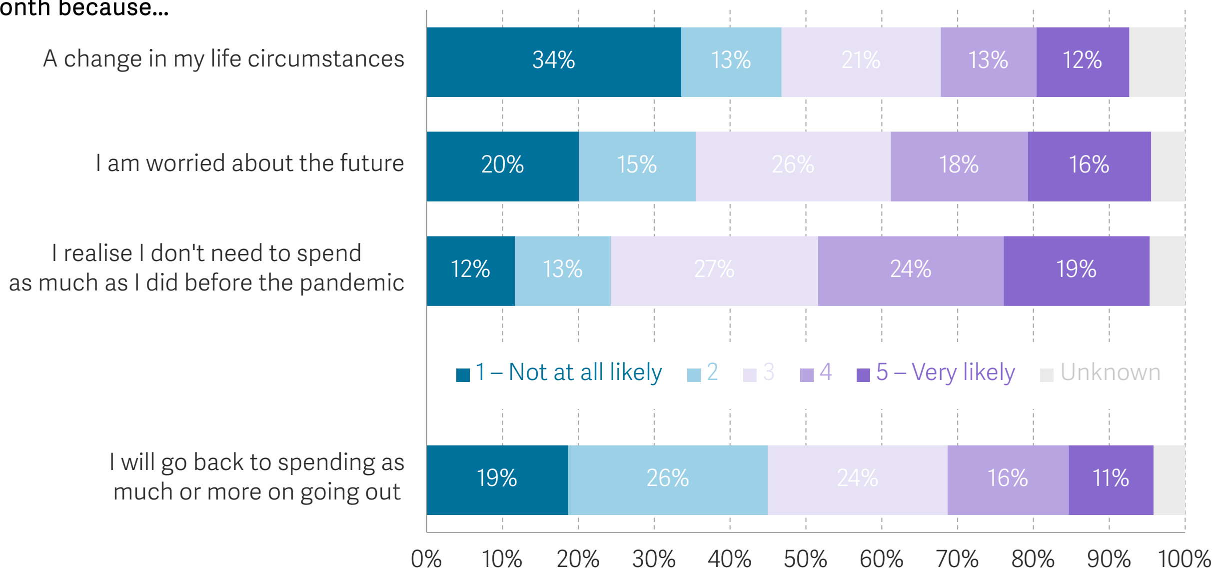
More worryingly from the perspective of the economic recovery, there is also evidence that saving rates may remain elevated for some time after the pandemic is over, as is normal after recessions.[41] If this happens, then wealth gaps could continue to grow. This is because better-off families have more capacity to save money, and so higher average saving rates will tend to lead to growing wealth gaps. This would also mean that overall household spending would remain sluggish even as the pandemic subsides, providing a major headwind to the recovery. Figure 28 presents evidence on households' plans to change saving rates in the future. Again, the evidence is mixed, but suggests that many families will continue to save more. Around half of families say that changing life circumstances are unlikely to be a factor in continuing to save more each month. But a third of families say they are likely to save more as a result of worries about the future: in other words, precautionary saving appears to be an important motivator for some families. And an even larger share – almost half – of families say they will save more because they have learnt they don't need to spend as much as they did before the pandemic. If this is true, this would represent a meaningful shift in household preferences between saving and consumption. Of course, it is hard to interpret these

40 The Bank of England currently judge than 10 per cent of additional savings levels will be used for additional consumption during the recovery. See: Bank of England, Monetary Policy Report, May 2021.
41 The household saving ratio remained above typical pre-financial crisis levels until 2012 and only fell below it in 2016.

results definitively, because the data is just on intentions, and people may not know how permanent are their changed patterns of spending. But the higher saving rates here suggest that wealth gaps could continue to rise.

FIGURE 28: **Most families indicate they are likely to continue to save more each month after the pandemic is over**

Proportion of respondents with increased savings during the pandemic reporting likelihood of changing saving rates in future: UK, May 2021



NOTES: Base is all those whose savings increased between February 2020 and May 2021 (n=2238). These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ and the Coronavirus (COVID-19), June 2021 wave.

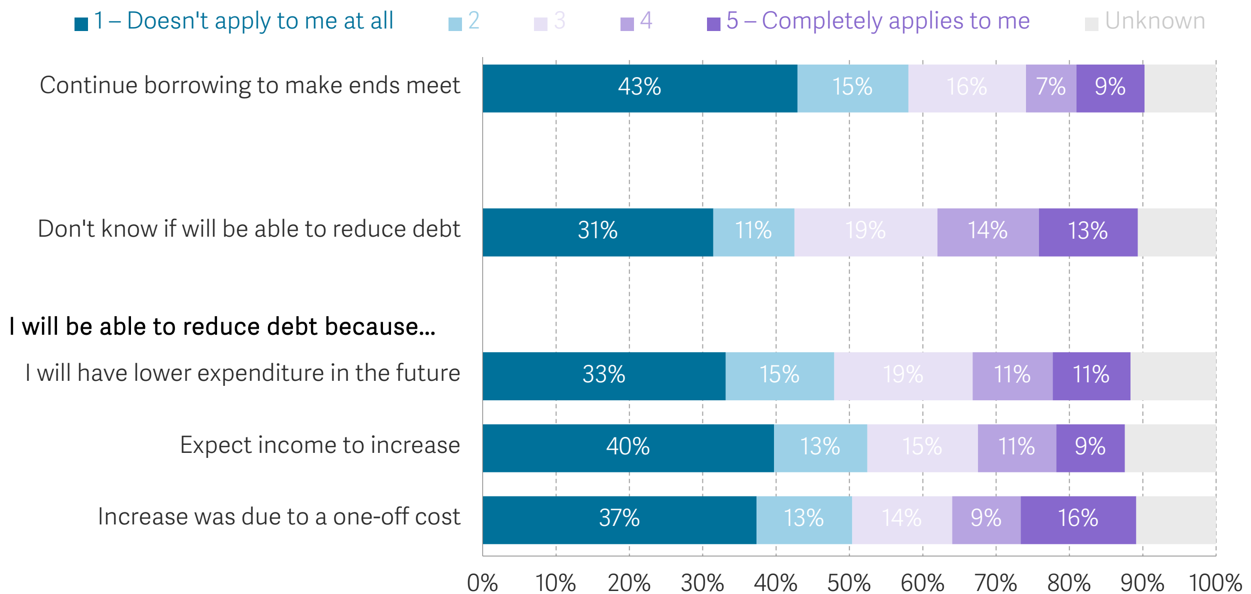
The future of debt holdings is also important for understanding the longer-term impact of the pandemic. While there has been good news, with aggregate debt levels falling over the course of the pandemic, some families have increased their use of debt. The optimistic case for those who increased debt in the pandemic would be that, as the economy recovers, the labour market quickly returns to pre-pandemic tightness, leading to a recovery in incomes and allowing families to reduce the extra debts taken out.

However, as Figure 29 shows, this looks unlikely to be the case – or, at least, families do not currently expect it to happen. Of those who increased debt since February 2020, just 10 per cent are completely confident that debt will fall in the future because their income will rise, while 40 per cent say that does not apply to their situation at all. More encouragingly, our survey found a relatively low proportion of families expecting to increase debt further as they are unable to make ends meet. But given the low confidence that debts will fall in the future, the financial resilience of families who have increased debts is likely to remain precarious. Higher debts reduce the capacity for

families to cope with future falls in income and is also associated with lower levels of wellbeing.[42]

FIGURE 29: **Families with increased debt have low confidence in reducing it in the future**

Proportion of respondents whose debt increased during the pandemic reporting the following statements apply or don't apply to their situation: UK, May 2021



NOTES: Base is all adults who increased debt between February 2020 and May 2021 (n=993). These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ and the Coronavirus (COVID-19), June 2021 wave.

Overall, then, while it is undoubtedly positive that the pandemic has come with aggregate improvements in family finances, it also appears likely that there will be a lasting increase in wealth gaps. In addition, there is a sizable minority of the population less able to cope with any future income falls given higher debts. As we discuss in our concluding section below, this evidence will be vital for policy makers as they grapple with the aftermath of the crisis.

42 S Garforth-Bles, C Warner & K Keohane, The Wellbeing Effects of Debt and Debt-Related Factors, Financial Conduct Authority, November 2020.