Rates of change

The impact of a below-inflation uprating on working-age benefits

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Next week will see the publication of September's inflation figure, the basis on which key working-age benefits are normally uprated in the following April. But with the public finances under real pressure, and prices expected to fall in the coming months, there are signs the Government is considering a departure from standard practice by under-indexing key working-age benefits in 2024-25.

This would be a very bad idea indeed. A decision not to uprate working-age benefits in line with inflation would affect more than four-in-ten (9 million) working-age households in the UK. And the losses for many would be material: if key benefits were frozen, a single adult working at least 20 hours a week at minimum wage with an illness or disability claiming UC would see their annual income fall by £628, for example; a working couple with two children on UC earning the same would experience a £1,241 shortfall over the course of the year; and a similar working couple with three children in receipt of UC would suffer a dramatic £1,678 fall to their income next fiscal year.

Freezing benefits in 2024-25 would drive up inequality and impoverish many: 400,000 more children would grow up in poverty next year as a result. Some may argue that this approach is needed to 'correct' for the 'generous' uprating decision of last autumn, but this is wrong: if working-age benefits were uprated next April in line with September's inflation figure, they would still only return to the real value they had on the eve of the pandemic.

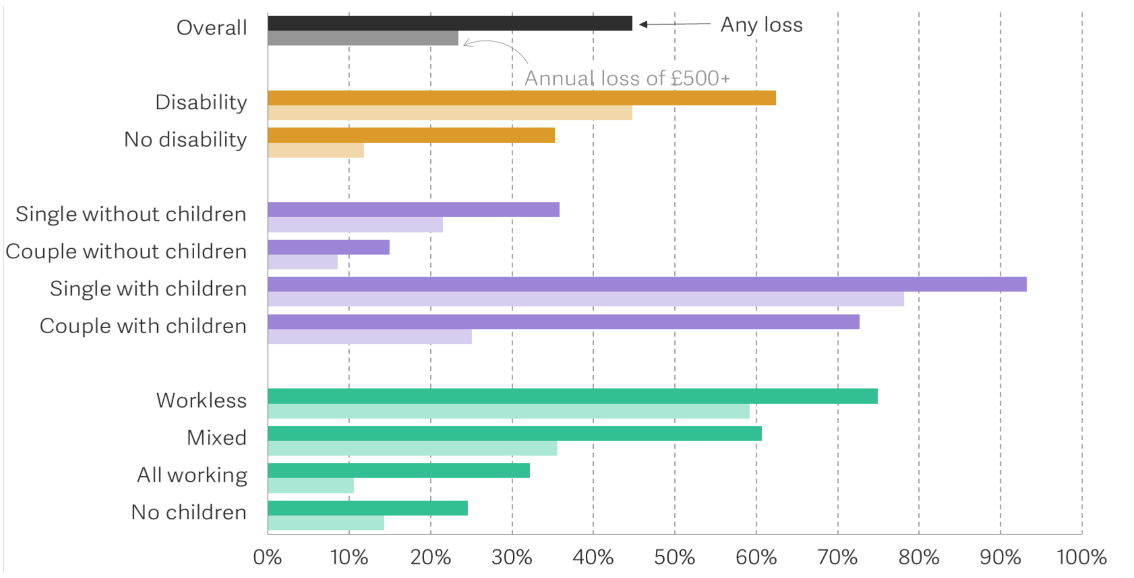
Rishi Sunak has shown a marked appetite in recent weeks for taking 'difficult' decisions – and all the more so if they save significant amounts of money in these straitened times. So, could another such decision be in the Government's sights? Next Wednesday (18 October) will see the publication of September's annual inflation figure, a critical number not just because it has implications for future interest rates, but also because it is the basis on which most working-age benefits should be uprated in April 2024. Inflation is expected to be far lower than last year: the most recent forecast from the Bank of England is that CPI will stand at 6.9 per cent for the third quarter of 2023, compared to 10.1 per cent in September 2022. Nonetheless, there are signs that the Government is considering under-indexing working-age benefits next year, in contrast to the principled approach it took last autumn.[2]

Why might it choose to adopt such a strategy? The answer to that question is simple: uprating decisions can save the Government a huge amount of money, especially when inflation is riding high. If Universal Credit (UC) rates were frozen (the most extreme scenario) rather than uprated by 6.9 per cent in April 2024, for example, this would save the Treasury £2.9 billion in 2024-25 alone (savings, of course, would also accrue in future years unless the benefit was over-indexed at some later point).[3] Likewise, freezing the value of all other 'non-protected' working-age benefits such as Child Benefit (CB) , tax credits, Job Seekers Allowance (JSA), Statutory Maternity and Paternity Pay (SMP/SPP) and Maternity Allowance (MA) would bring in a further £1.3 billion in 2024-25.[4] With the costs of servicing public debt at a near all-time high, this £4.2 billion of savings would be very welcome indeed.[5]

But savings to Government are losses to families who are in receipt of benefits, and Figure 1 shows how widespread shortfalls would be. More than four-in-ten (45 per cent) working-age households would see a drop in their real income as a result of a benefit freeze in April 2024, equivalent to over 9 million households. That figure rises to more than six-in-ten (62 per cent) households where at least one member has a disability (4.4 million households); seven-in-ten (73 per cent) couples with children (4.2 million households) and more than nine-in-ten (93 per cent) single parents (1.7 million households).[6] Strikingly, one-third (32 per cent) of households where all adults are in work would also face a fall in real income in the event of a benefit freeze next year.

Figure 1 **Freezing benefits in the next fiscal year would put pressure on more than four-in-ten working-age households in the UK**

Proportion of working-age households with any real income fall, and an annual real income fall of £500-plus, as a result of freezing rather than uprating benefits in line with September CPI, by household type: UK, 2024-25



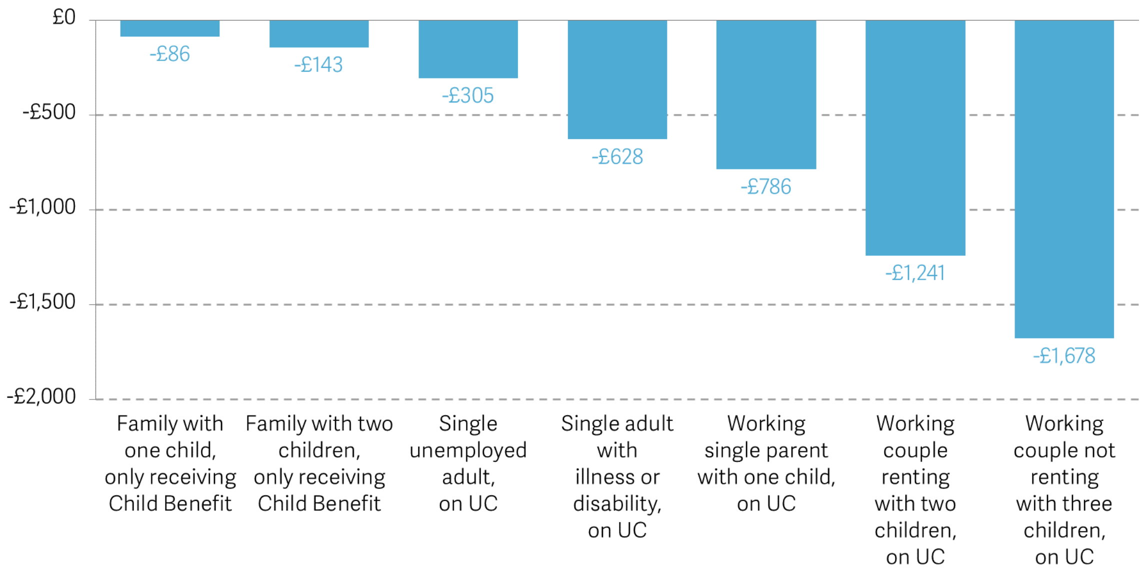
Notes: Assumes all 'unprotected' working-age benefits are frozen at 2023-24 nominal levels rather than uprated by 6.9 per cent. 'Unprotected 'benefits are: Universal Credit (excluding housing element); contributory JSA and ESA; tax credits; non-contributory JSA and ESA; income support; bereavement benefits; Statutory Maternity and Paternity Pay; and Maternity Allowance.
Source: RF analysis of DWP, Households Below Average Income using the IPPR Tax-Benefit Model.

Moreover, as Figure 1 also shows, for many households the losses would be material. We estimate that half (52 per cent) of the households who would lose were working-age benefits frozen in April 2024 would see their annual income fall by £500 or more (4.7 million households in all). And for some family types, the share affected experiencing a large-scale income loss is higher still: 1.4 million single parent households would see their annual income fall in real terms but £500 or more, for example (84 per cent of all those affected); 3.2 million households containing at least one member with a disability would be equally hard-hit (72 per cent of all those affected); and likewise 1.4 million households where at least one member is in work (33 per cent of all those affected).

Figure 2 drives home the gravity of the income hit for some family types in the event of a benefit freeze. A household with two children in receipt of Child Benefit only would experience a real-term loss of £143 over the course of 2024-25 if benefits were to be frozen, for example. But a single adult with an illness or disability claiming UC would see their annual income fall by £628, more than four-times that amount; a working couple with two children on UC would experience a £1,241 shortfall over the course of the year, eight-times more than the family claiming Child Benefit only; and a working couple in receipt of UC with three children (all born before April 2017 and therefore not affected by the 2-child limit) would suffer a dramatic £1,678 fall in their annual income, a hit almost twelve-times as large as a two-child family in receipt of Child Benefit alone.[7]

Figure 2 **UC claimants with children would be especially hard-hit by a benefit freeze**

Example losses to real annual income from freezing rather than uprating benefits in line with September CPI: UK, 2024-25

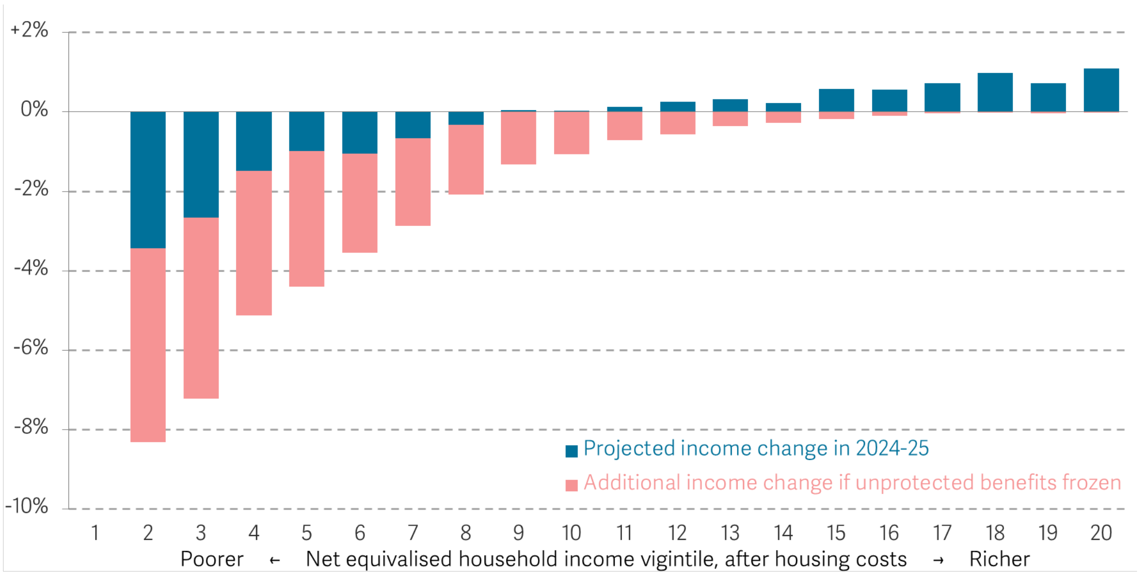


Notes: Assumes all 'unprotected' working-age benefits are frozen at 2023-24 nominal levels rather than uprated by 6.9 per cent. 'Unprotected 'benefits are: Universal Credit (excluding housing element); contributory JSA and ESA; tax credits; non-contributory JSA and ESA; income support; bereavement benefits; Statutory Maternity and Paternity Pay; and Maternity Allowance. Single parent with one child in work is assumed to be renting, working at least 20 hours a week earning NLW, and have a child born after 6th April 2017. Working couple with two children is assumed to be renting, working at least 20 hours a week earning NLW, and have two children born after 6th April 2017. Working couple with three children is assumed to be renting, working at least 20 hours a week earning NLW are to have three children born *before* 6th April 2017.
Source: RF analysis of DWP, Households Below Average Income using the IPPR Tax-Benefit Model.

Given that benefits make up a larger share of household income for poorer families than they do for richer households, it is no surprise that those on lower incomes would be hardest hit were the Government to under-index key working-age benefits next year. As Figure 3 shows, this looks set to make an already bad prognosis for 2024-25 (driven largely by the end of Cost of Living Payments) worse. We have previously shown that, even if benefits are indexed fully in line with September's CPI figures, lower-income households (those in vigintiles 2 to 8) face the prospect of a real-terms fall in after housing costs incomes in 2024-25, in contrast to those in the top half of the income distribution.[8] A benefit freeze would exaggerate this picture. Those in vigintile 2, for example, would see their incomes fall by 8 percentage points in such an event, as opposed to just over 3 per cent if working-age benefits keep pace with inflation in 2024-25. Income inequality would increase as a result.

Figure 3 **A benefit freeze would drive up income inequality in 2024-25**

Real change in average equivalised working-age household disposable income, after housing costs, by income vigintile (base case and benefit freeze scenario): UK, 2024-25



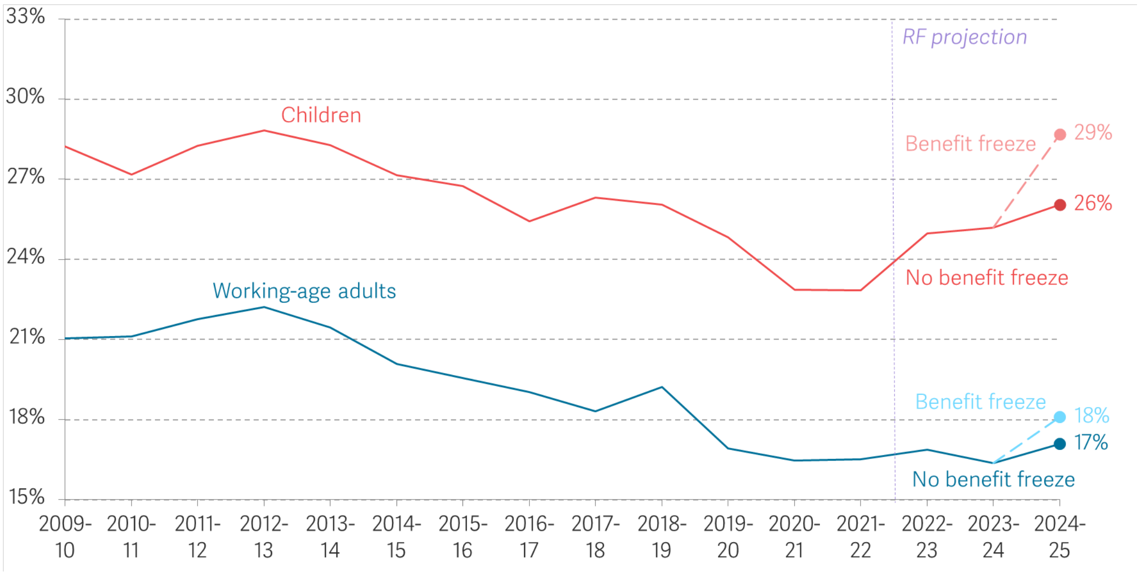
Notes: We exclude the bottom 5 per cent, due to concerns about the reliability of data for this group. Base case scenario is from A Corlett, The Living Standards Outlook – Summer 2023 Update, Resolution Foundation, September 2023. Benefit freeze assumes all 'unprotected' working-age benefits are frozen at 2023-24 nominal levels rather than uprated by 6.9 per cent. 'Unprotected 'benefits are: Universal Credit (excluding housing element); contributory JSA and ESA; tax credits; non-contributory JSA and ESA; income support; bereavement benefits; Statutory Maternity and Paternity Pay; and Maternity Allowance.

Source: RF analysis of DWP, Households Below Average Income using the IPPR Tax-Benefit Model.; ONS, Wealth and Assets Survey; ONS data; Bank of England forecasts; OBR forecasts.

As well as worsening income inequality, the failure to uprate working-age benefits in line with inflation in April 2024 would impoverish many more individuals as we show in Figure 4. Absent of a benefit freeze, we estimate poverty for working-age adults will hover around 17 per cent from 2021-22 to 2024-25; that figure would rise to 18 per cent in the event of a zero per cent uprating, And the effect on children is even more stark: child poverty rates look set to rise from 23 per cent to 26 per cent between 2021-22 and 2024-25 even if benefits are uprated in line with inflation, a figure that would increase to 29 per cent in the event of a benefit freeze. Indeed, in this scenario, the number of children growing up in poverty would rise by 500,000 between 2023-24 and 2024-25 (400,000 more than if benefits are uprated in line with inflation). Overall, we estimate poverty would rise by 1.2 million between 2023-24 and 2024-25 if benefits are frozen – three-times as high as if benefits were increased in line with inflation (400,000).

Figure 4 **Freezing working-age benefits in April 2024 would increase child poverty from 26 per cent to 29 per cent**

Proportion of people living in absolute poverty, after housing costs (base case and benefit freeze scenario): UK

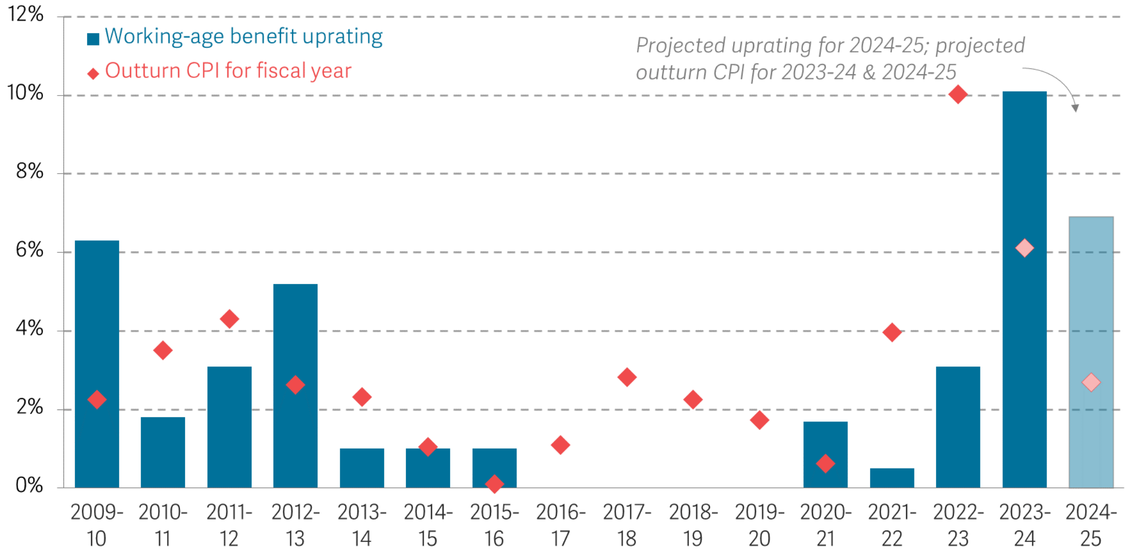


Notes: Base case scenario is from A Corlett, The Living Standards Outlook – Summer 2023 Update, Resolution Foundation, September 2023. Benefit freeze assumes all 'unprotected' working-age benefits are frozen at 2023-24 nominal levels as opposed to uprated by 6.9 per cent. 'Unprotected 'benefits are: Universal Credit (exclude ng housing element); contributory JSA and ESA; tax credits; non-contributory JSA and ESA; income support; bereavement benefits; Statutory Maternity and Paternity Pay; and Maternity Allowance.
Source: RF analysis of DWP, Households Below Average Income, and RF projections including analysis of DWP, Family Resources Survey using the IPPR Tax Benefit Model; ONS, Wealth and Assets Survey; ONS data; Bank of England forecasts; OBR forecasts.

Increased hardship for millions of vulnerable households; higher income inequality; and 400,000 more children growing up in poverty are all compelling reasons why the Government should not consider under-indexing working-age benefits regardless of where September inflation's figure lands next week. Moreover, it is important not be beguiled by the argument (also made but dismissed last year) that in a period of falling inflation, uprating benefits in April based on the rate of inflation recorded six months earlier results in too 'generous' a settlement for claimants. Year-by-year, it will of course be true that at some points working-age benefits will be uprated in April by an amount that proves to be higher than outturn inflation for that fiscal year. But as Figure 5 shows, the opposite also holds true on numerous occasions too. Indeed, over the last 15 years, key working-age benefits have been uprated by an amount that was lower than outturn CPI in 10 of those fiscal years (including, of course, when there was an active policy decision to under-index, as in 2016-17 to 2019-20). Indeed, if key working-age benefits were uprated in April 2024 in line with this September's inflation figure, they will only just recover the real value they had on the eve of the pandemic, in 2019-20.

Figure 5 **Working-age benefits have not risen at the same rate as outturn inflation for 10 of the last 15 years**

Basis for working-age benefit uprating, and outturn CPI, by fiscal year: UK



Source: RF analysis of P Matejic, Fifty years of uprating, JRF, April 2022; Bank of England forecasts; OBR forecasts.

Finally, there is one further consideration the Government might bear in mind as it decides on the fate of working-age benefits for the next fiscal year. A benefit freeze is a stealthy way of cutting the value of social security (or making savings for the Exchequer, depending on your point of view), and one that rarely attracts the same level of opprobrium as targeted cuts to, say, disability or children's benefits. Nonetheless, there has been a marked turn in public attitudes to benefits in recent years: the latest British Social Attitudes survey shows, for example, that 52 per cent of the population believe taxes should be raised to increase spending on health, education and social security, up from 31 per cent in 2010. Likewise, 43 per cent now disagree with the statement 'Many people who get social security don't really deserve any help', far higher than the 28 per cent who disagreed in 2010. Under-indexing key working-age benefits may have been a relatively easy political sell in the 2010s; there is a risk such a policy may not be as popular today, especially when the contrast is drawn with the 8.5 per cent increase we expect to the State Pension in April 2024.[9]

[1] The authors thank colleagues Mike Brewer and Adam Corlett for advice throughout.
[2] This would also be in marked contrast with the treatment of the State Pension, which the triple lock requires be uprated by average earnings, CPI or 2.5 per cent, whichever is higher. It is expected that in 2024-25, the State pension will rise in line with average earnings which in May-July 2023 stood at 8.5 per cent.
[3] Figure excludes housing support provided through Universal Credit, but includes the capability to work element of the benefit.
[4] This would be slightly more stringent than the benefit freeze of 2016-17 to 2019-20 when some benefits such as parental pay and disability premiums were not frozen. See R McInnes, Benefit uprating 2019, House of Commons Library, March 2019 for more info. For a comprehensive description of which benefits must be uprated at least in line with inflation and which are 'unprotected', see A Corlett & L Try, The long squeeze: Benefit uprating policy for April 2023, Resolution Foundation, October 2022; E Kirk-Wade & R Harper, Benefit uprating 2023/24, House of Commons Library, December 2022.
[5] At the time of the Budget in March 2023, the Government had £6.5 billion of headroom against its primary fiscal target of reducing debt as a share of GDP. Source: OBR, Economic and Fiscal Outlook, OBR, March 2023. Since then, the cost of debt servicing has risen sharply, putting more pressure on the public finances.
[6] These are not exclusive categories, which is why the numbers sum to more than 9 million.
[7] The exposure of families with three or more children to benefit cuts is increasingly well-researched. See, for example, The Larger Families Project.
[8] Even absent of a benefit freeze, average incomes of working-age households in the bottom half of the income distribution are projected to fall by 1 per cent in 2024-25, and an extra 300,000 people are projected to fall into absolute poverty. See: A Corlett, The Living Standards Outlook – Summer 2023 Update, Resolution Foundation, September 2023 for further details.
[9] The State Pension is, of course, subject to the triple lock which ensures it is uprated each year in line with average earnings growth typically over the three months of May-July or September's inflation rate in the preceding year, or 2.5 per cent, whichever is higher. See: J Cribb, C Emmerson & H Karjalainen, The triple lock: uncertainty for pension incomes and the public finances, IFS, September 2023 for further details.