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## Household incomes: overall trends and the impact of tax and benefit changes

Robert Joyce

# Outline

1. Chancellor and the Leader of the Opposition made contrasting claims about living standards yesterday
  - Will assess these and put them in wider context
2. Will focus on specific role of tax and benefit changes and how they have affected incomes across the distribution

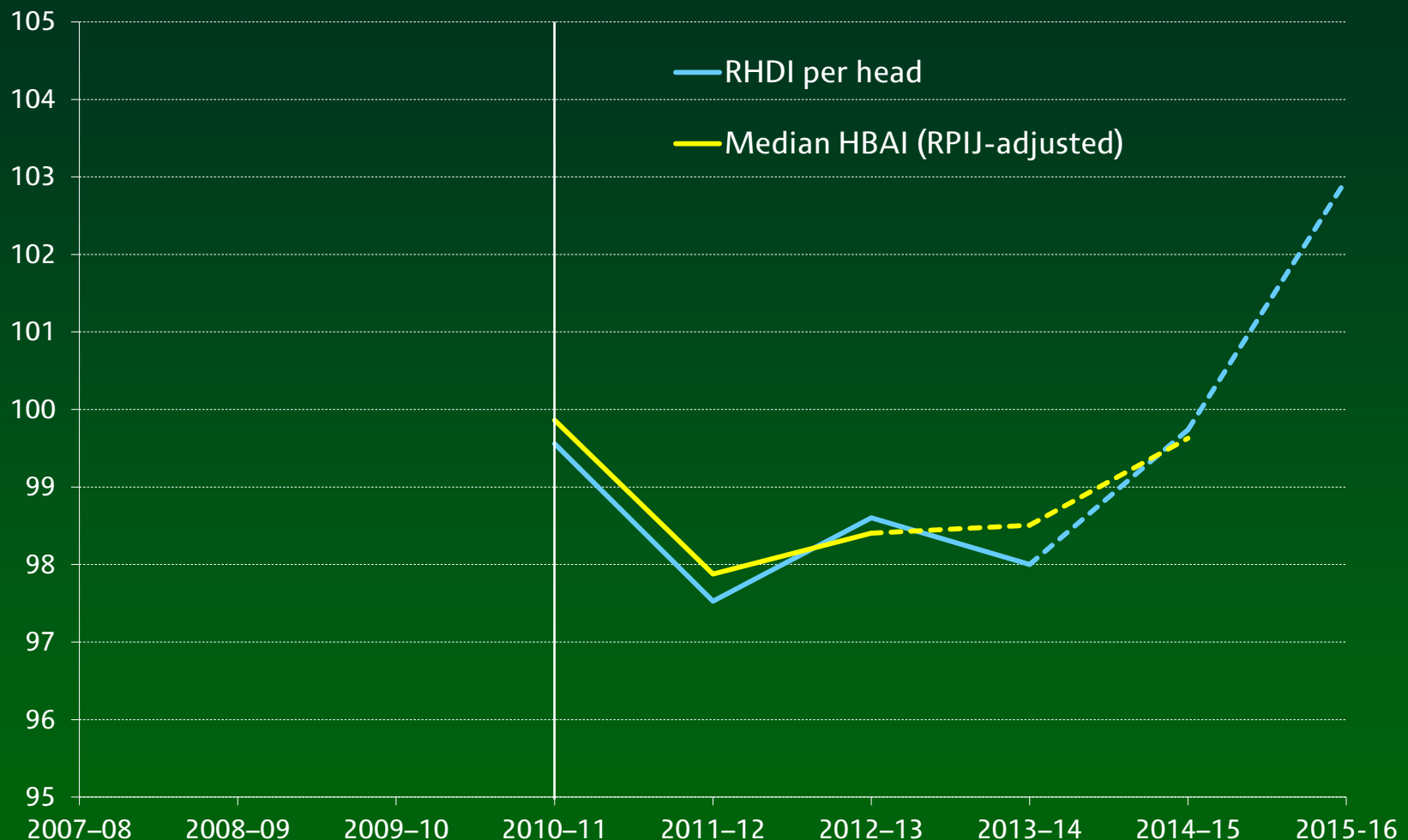
# Average household incomes in recent years

- Main source for household income data is the HBAI series
  - Based on annual survey of about 20,000 households
  - Measures household income after taxes and benefits
- Latest data cover 2012-13, but IFS researchers recently projected real *median* HBAI income up to 2014-15
  - This suggested that, in 2014-15, median income was back to around its 2010-11 level (and growing)
  - Any significant growth in 2015-16 would take it above 2010-11 level

# What was the Chancellor referring to?

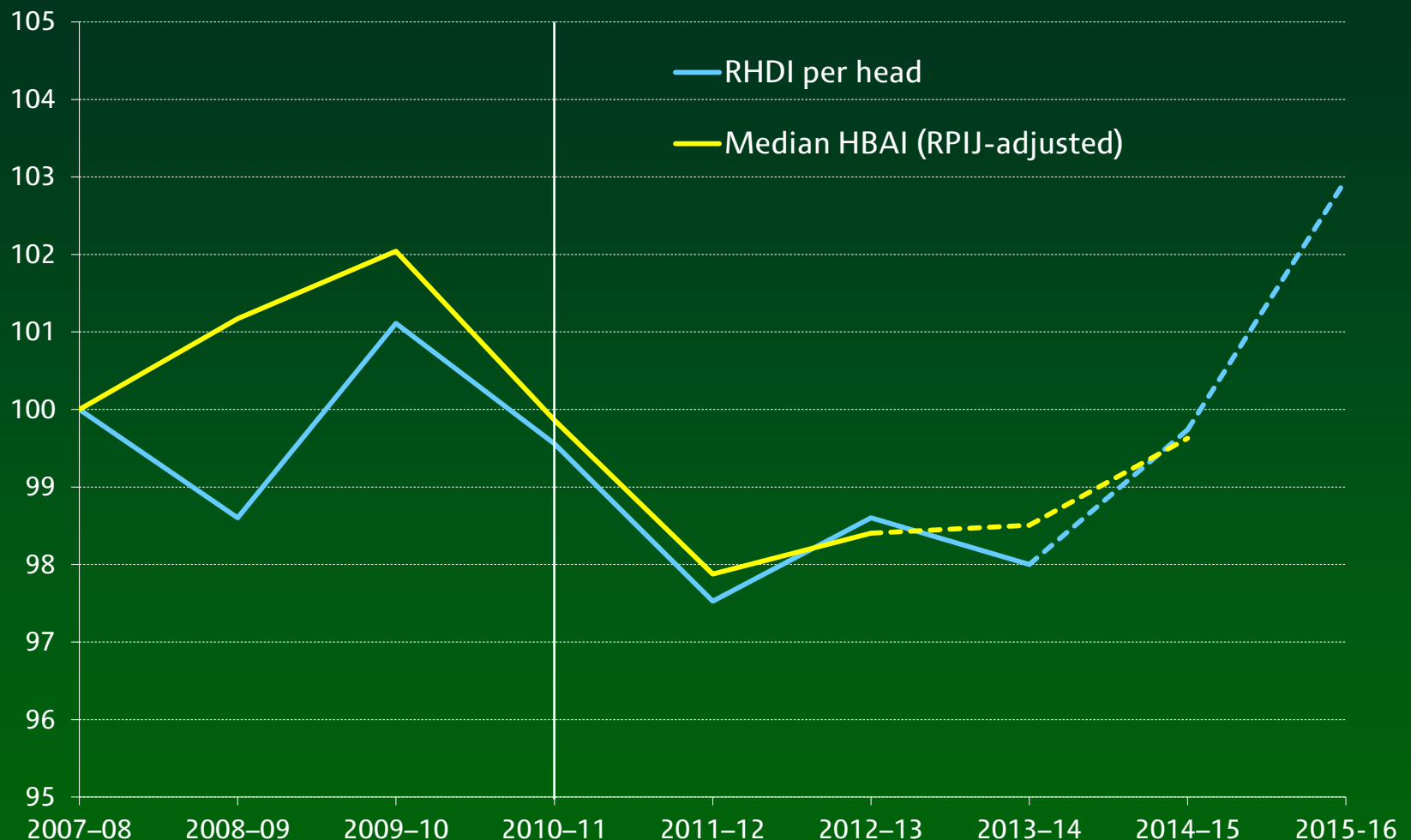
- Real Household Disposable Income (RHDI), from National Accounts
  - Essentially tries to capture the part of national income that flows to household sector (rather than companies and the public sector)
- Chancellor referred to RHDI per head and per household (effectively measures of *mean* income):
  - **“On that measure [RHDI per head] I can confirm, on the latest OBR data today, living standards will be higher in 2015 than in 2010.”**
  - **“The facts show households on average will be around £900 better off in 2015 than they were in 2010”**
- Very likely these measures will be higher in 2015 than 2010
  - OBR thinks RHDI per head in 2014 was around its 2010 level – similar impression to IFS projections of median HBAI income
  - OBR expects RHDI per head to grow by 3.1% in 2015
  - £900 is forecast rise in RHDI per household between 2010 and 2015

# Measures of average living standards (2007-08 = 100)



Notes: RHDl figures are presented for financial (not calendar) years, and are expressed per person (rather than per person aged 16+). In both cases this is consistent with HBAI, but different to the OBR figures underlying the Chancellor's Budget speech. This makes a negligible difference. HBAI figures from Cribb, Hood and Joyce (2015), at <http://www.ifs.org.uk/publications/7615>

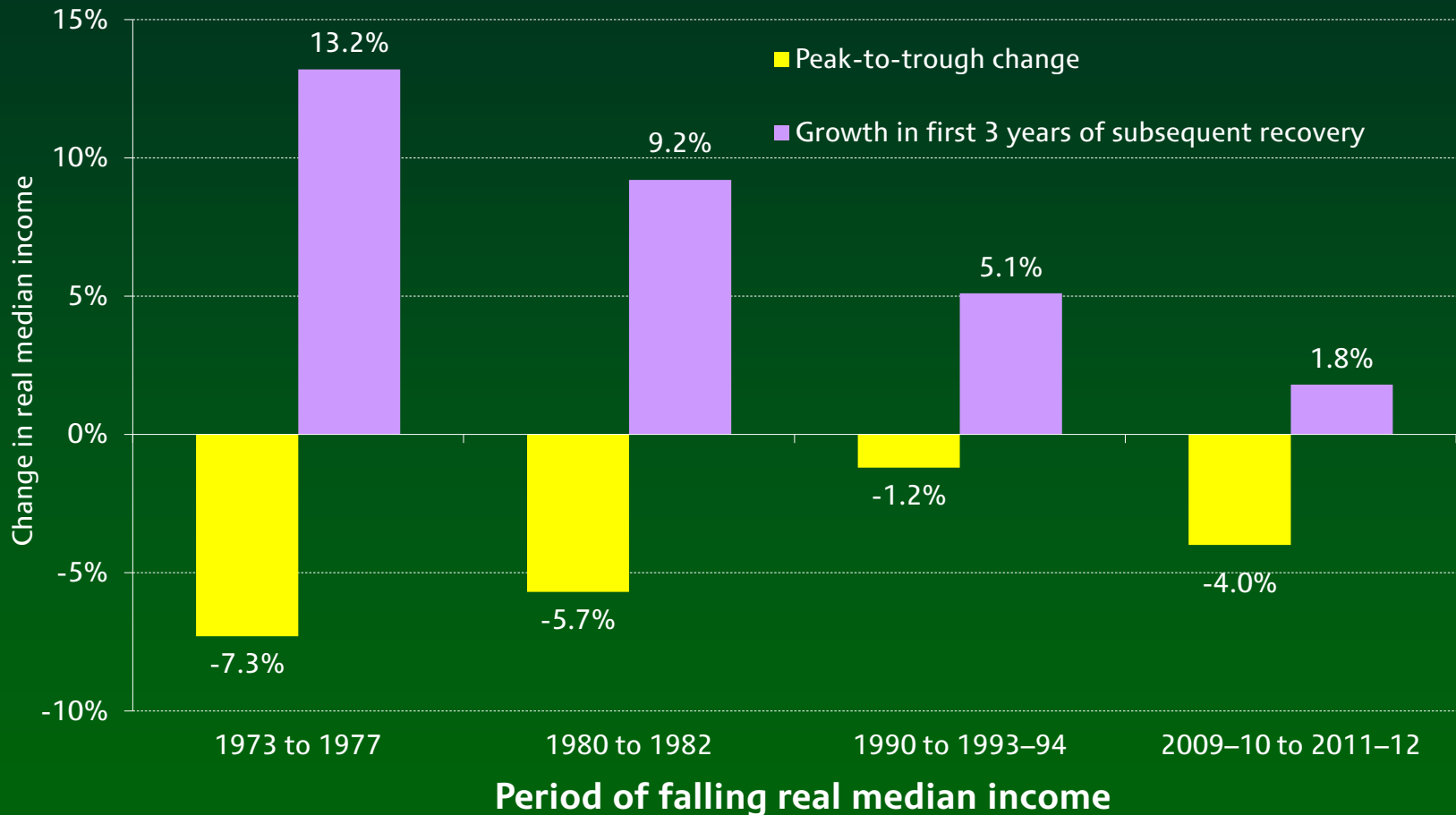
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# Recovery has been historically slow

## Comparison of periods of falling real median HBAI income



Note: The '1.8%' figure for growth in the most recent recovery is based on an IFS projection up to 2014-15

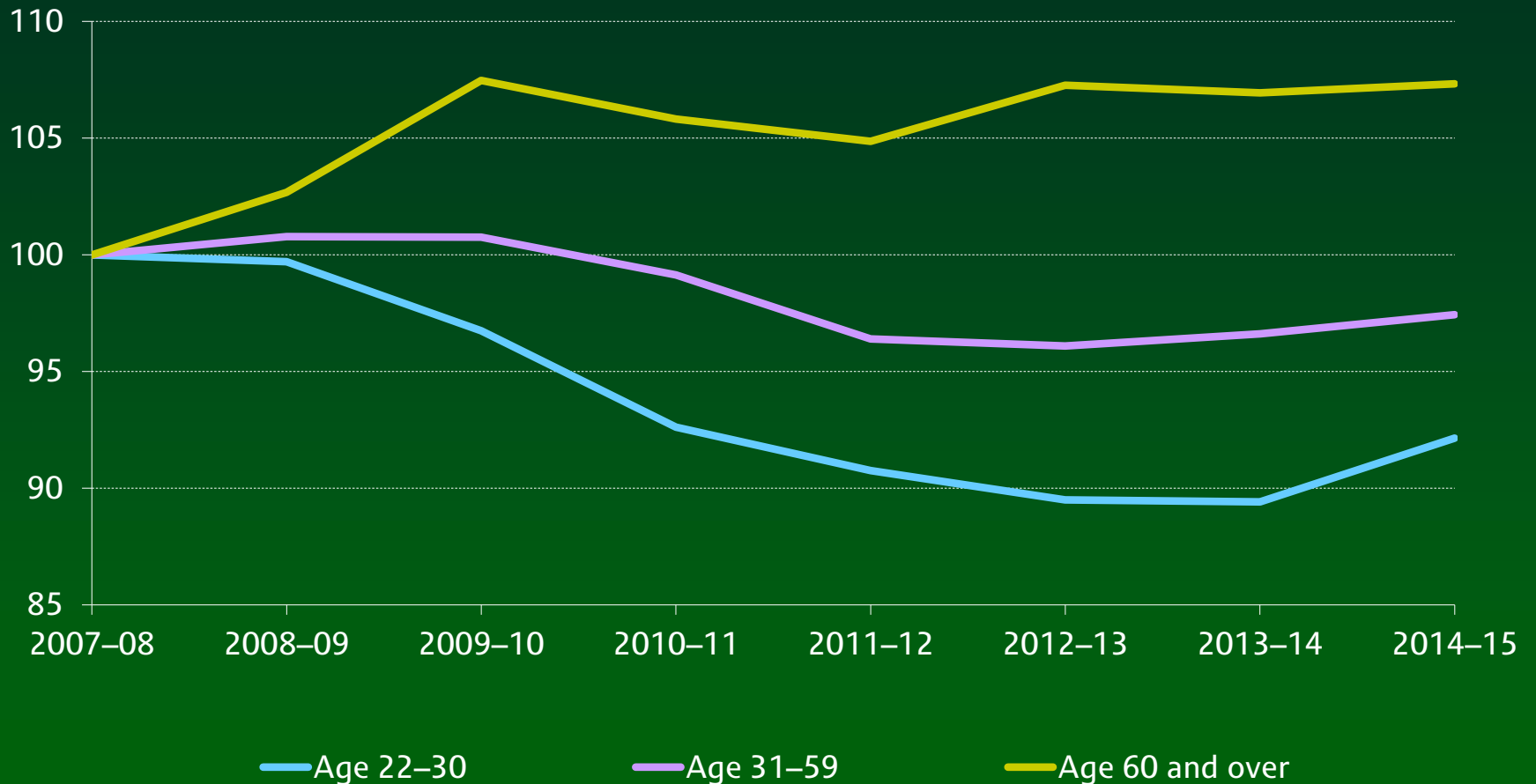
Source: Cribb, Hood and Joyce (2015), available at <http://www.ifs.org.uk/publications/7615>

## Average changes mask differences across groups

- Advantage of HBAI data is that they allow us to look at variation across population
- Chancellor: **“Compared to five years ago: inequality is lower”**
- Income inequality fell significantly between 2007-08 and 2010-11
- IFS projections for 2014-15 suggest inequality lower than 2009-10
- But very little change in inequality since 2010-11
- Big variation in income trends by age



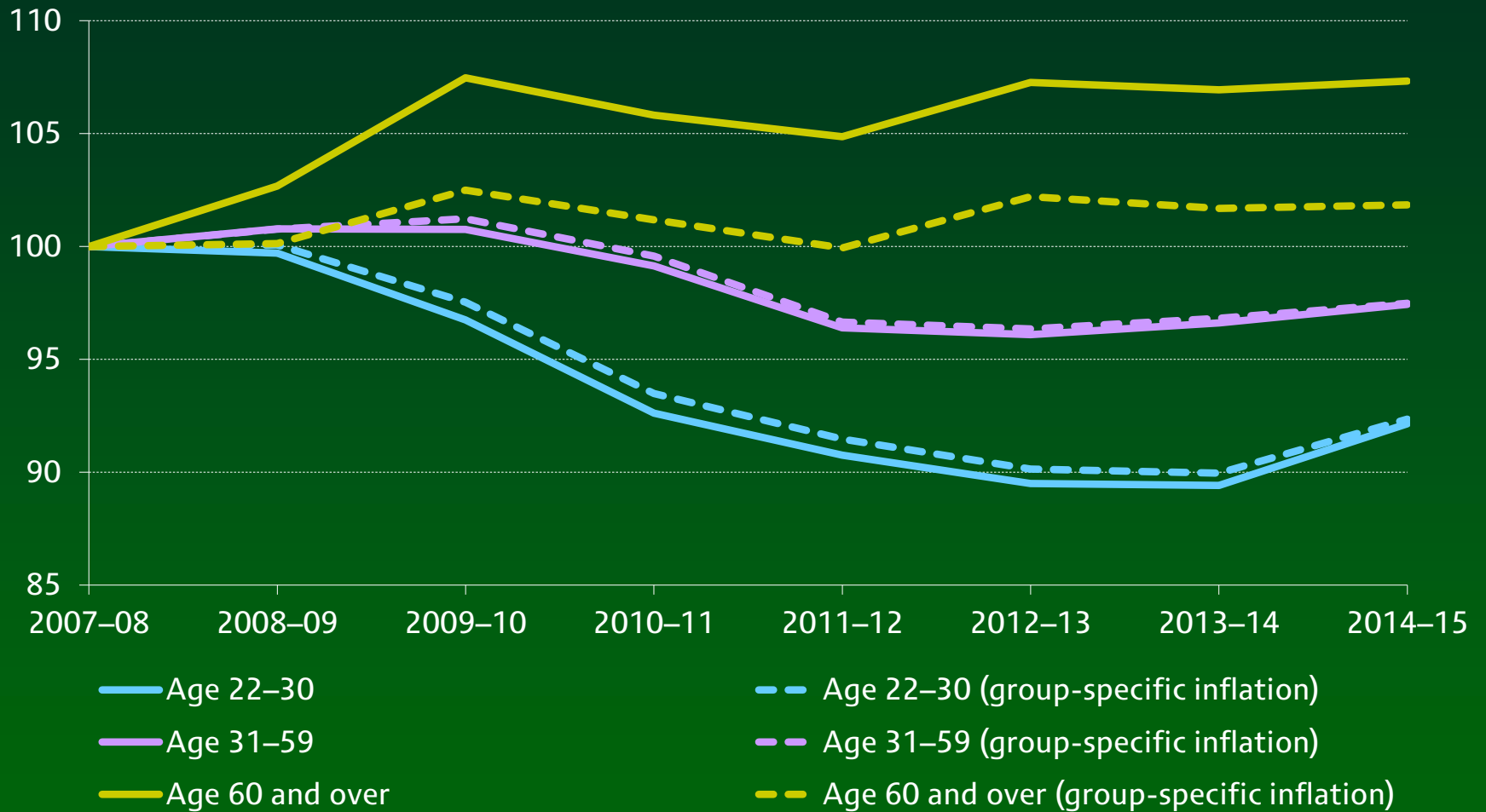
# Real median income by age group (2007-08=100)



Note: Figures for 2013-14 and 2014-15 are IFS projections

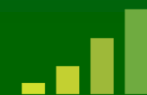
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## Ed Miliband: “People are £1,600 a year worse off”

- This is change in median pre-tax annual pay for employees between April 2010 and April 2014, adjusted for CPI inflation
  - Source: Annual Survey of Hours and Earnings (ASHE)
- Relevant number which highlights that pay levels have fallen a lot
- Why so different to Chancellor’s numbers? Reasons include:
  - Ignores taxes and benefits: sizeable chunk of the £1,600 would have been paid in income tax and NICs anyway; doesn’t pick up impacts of tax and benefit reforms
  - Doesn’t account for rising employment rate
  - Measures one source of income (albeit the largest) for subset of population, e.g. says nothing about most pensioners’ incomes
  - Goes up to April 2014: real earnings growing in 2015

## Household incomes: summary

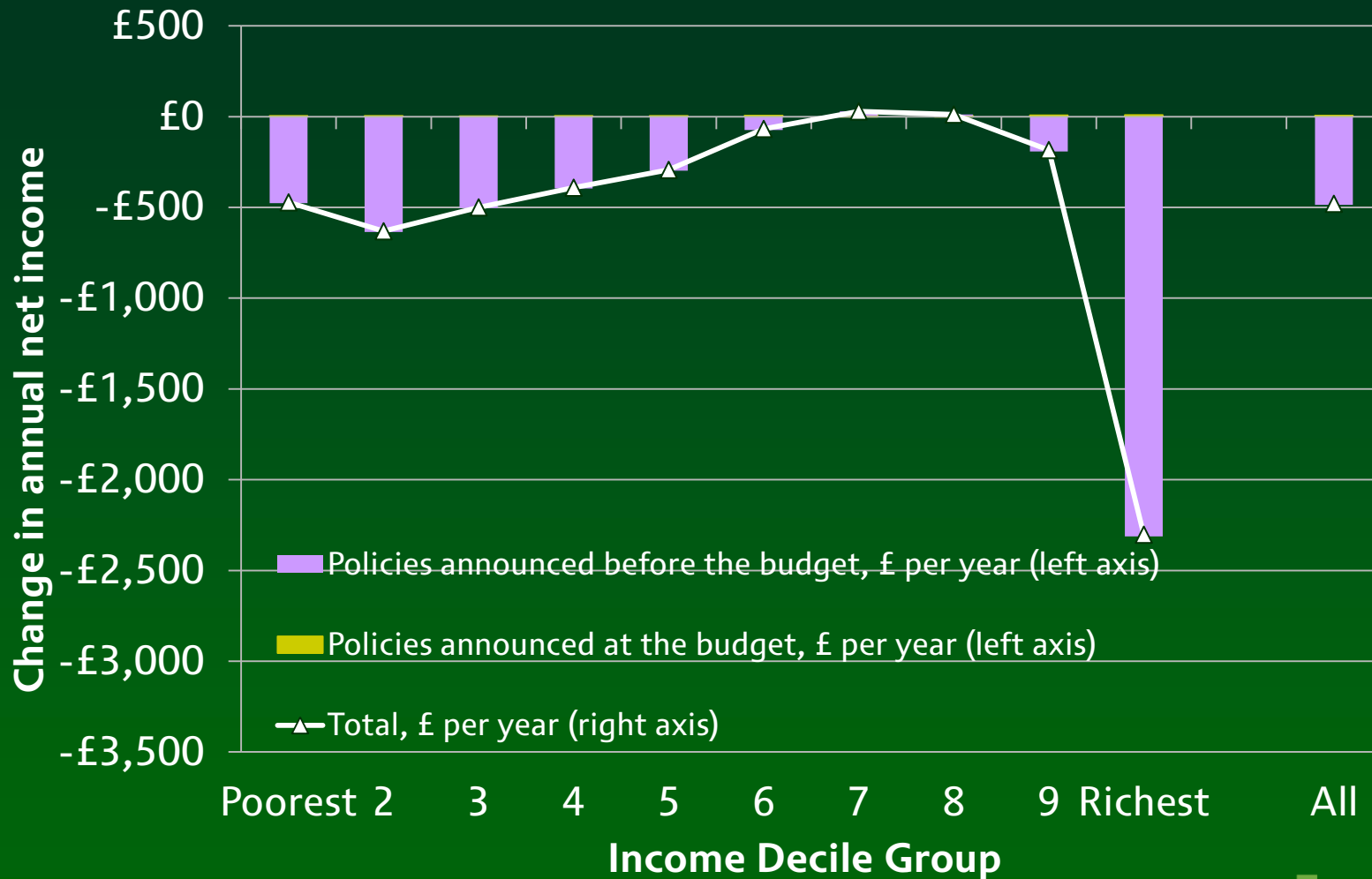
- Reasonable to think real average incomes across whole population will surpass pre-crisis and 2010 levels in 2015. But:
  - This is a low bar: we've had very slow recovery
  - Fixation on 2010 is economically arbitrary: big falls occurred between 2009 and 2011; election happened to fall in middle
- Labour's number on the fall in real pay among employees between 2010 and 2014 also relevant and interesting
- Some of the reasons why Labour's numbers look less positive than the Chancellor's are interesting in themselves
  - Real pay has fallen substantially, but:
  - Pensioner incomes have done much better than average
  - Proportion of people in work has risen
  - Things likely to get better in 2015

# TAX AND BENEFIT CHANGES

# Tax and benefit changes to April 2015

- Only measures announced yesterday for this April are cuts to alcohol duties
  - Total cost of £185m in 2015-16
  - 2% (2.9%) nominal (real) cut to beer and spirit duties
  - Nominal freeze (0.9% real cut) to duties on wine

# Impact of tax and benefit reforms between April 2010 and April 2015 (excluding universal credit)



Assumes full take-up of means-tested benefits and tax credits.

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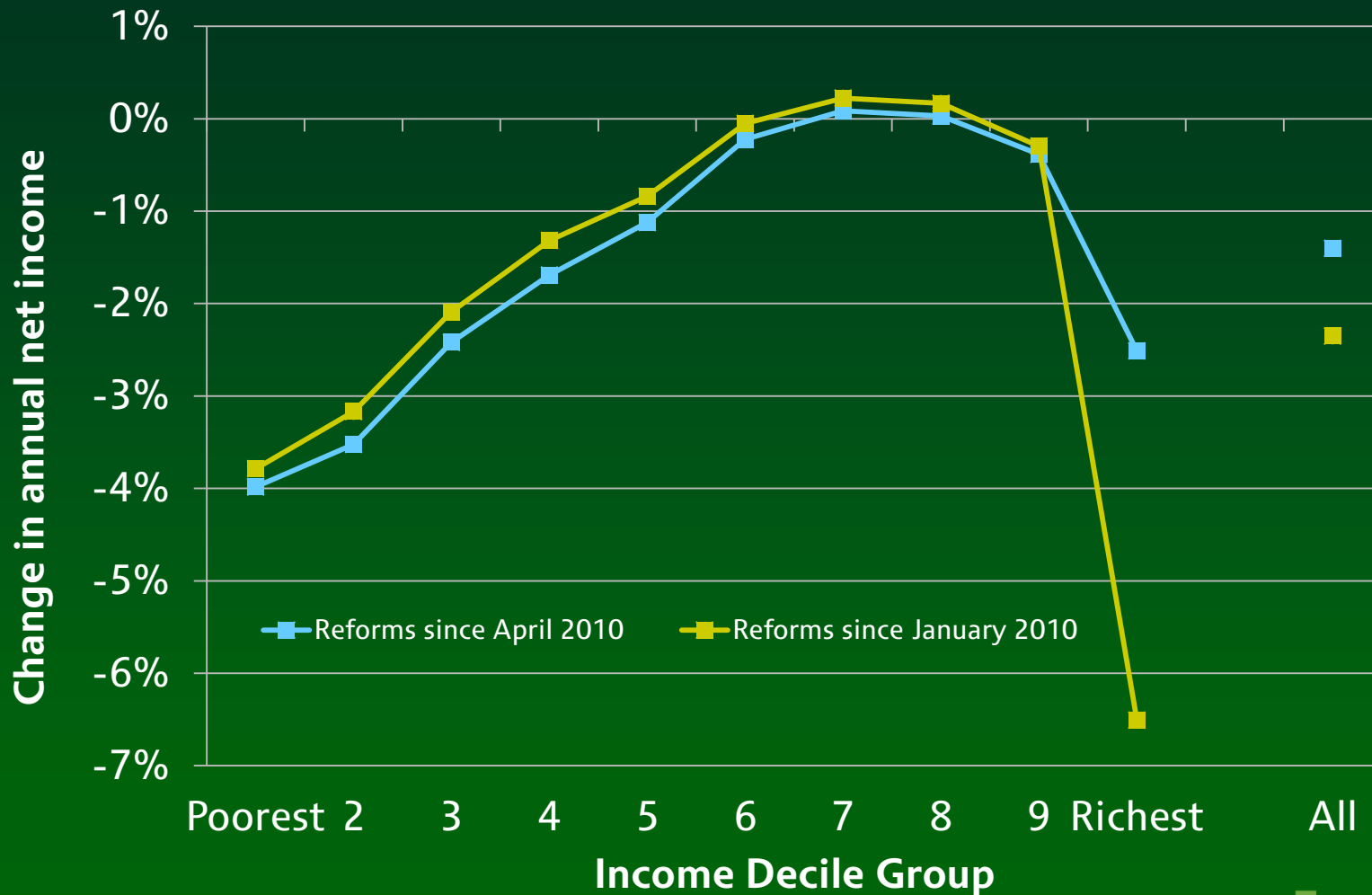


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- Distributional impact of all measures implemented by coalition:
  - Biggest losers are bottom half of income distribution (working-age social security cuts) and top decile (tax rises)
  - Treasury analysis suggests smaller losses / bigger gains, particularly at bottom: they model fewer measures, and try to account for non take-up of benefits (but probably overstate its extent)
- Looking at whole fiscal consolidation period, top decile hit considerably harder
  - Due to tax rises implemented by Labour in April 2010



# Impact of tax and benefit reforms up to April 2015 (excluding universal credit)



Assumes full take-up of means-tested benefits and tax credits.

## Next parliament: other changes

- Income tax personal allowance to continue to increase faster than inflation, to £10,800 in 2016–17 and £11,000 in 2017–18
  - Basic rate taxpayers gain £48 a year in 2017–18
  - Higher rate taxpayers with income below £121,520 gain £72
  - Costs about £1.5 billion in 2017–18
- Total cost of changes to personal allowance and higher rate threshold between 2010–11 and 2017–18 will be about £10bn
  - Basic rate taxpayers will be £597 a year better off in 2017–18 as a result of these changes
  - Higher rate taxpayers will be £535 a year worse off
- Yet another real cut to fuel duties
  - Brings total annual cost of coalition's real fuel duties cuts to £4bn

# Fuel duty: to uprate or not to uprate? ~~Act VI~~ Act VII

Dates uprating due before Budget 2011	Budget 2011	Autumn Statement 2011	June 2012	Autumn Statement 2012	Budget 2013	Autumn Statement 2013
<b>Apr 2011</b>	Jan 2012	Aug 2012	Jan 2013	Cancelled	Cancelled	Cancelled
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<b>Apr 2016</b>	Apr 2016	Apr 2016	Apr 2016	Apr 2016	Apr 2016	Apr 2016	Apr 2016

# Personal tax and benefit measures: summary

- Some small new measures announced, largely repeating old themes
  - Rise in personal allowance, cuts in fuel and beer duties
- Taking all measures implemented by coalition, top and bottom of income distribution have lost most
  - In comparison, middle and upper-middle heavily favoured by these changes on average
  - Losses at top considerably bigger if whole consolidation is considered (adding in Labour's tax rises in April 2010)