The Living Standards Outlook 2023

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January 2023

Acknowledgements

The authors are grateful to The Health Foundation for supporting this work. This research uses data from an online survey conducted by YouGov in November 2022. The total sample size was 10,470 UK adults aged 18+. Fieldwork was undertaken online during 23-30 November 2022. This research also uses data from two further surveys conducted by YouGov during the pandemic in June 2021 and October 2021. The June survey was undertaken by YouGov from the 3rd – 8th June 2021 and was of 8,030 adults aged 18+. The October survey was undertaken from 14th - 25th October 2021 and was of 6,100 working age adults (aged 18 to 64 years). All figures have been weighted and are representative of all UK adults. The figures presented from the online surveys have been analysed independently by the Resolution Foundation. The views expressed here are not the views of YouGov.

The authors would like to thank the Financial Fairness Trust and the Joseph Rowntree Foundation for conversations on survey design. The authors are also grateful to colleagues at the Resolution Foundation for input on the analysis and early findings, in particular Torsten Bell and Lindsay Judge for comments on earlier drafts, and to Molly Broome, Adam Corlett, Karl Handscomb and Jack Leslie for their analytical contributions. All errors remain the authors' own.

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M Brewer, E Fry & L Try, *The Living Standards Outlook 2023,* Resolution Foundation, January 2023

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Executive Summary

The past year was a disaster for UK living standards. As inflation reached its highest level in 41 years driven by globally rising prices for energy and goods, the Government responded with household cost of living support of £58 billion in 2022-23. Facing a tight labour market, employers raised nominal pay by its fastest rate since 1991. But real pay still shrunk, and government support was not enough to prevent median household incomes from falling by 3 per cent in real terms in 2022-23. To deepen our understanding of where this crisis leaves Britain, our fifth Living Standards Outlook uses two approaches. First, a new survey of 10,000 adults in the UK explores how households are coping with the current crisis and what its lasting effects may be. Second, our modelling helps us to understand what the latest economic developments and planned government policy mean for household incomes and poverty this year and beyond.

The cost of living crisis is widely felt, but not all households are affected equally

The cost of living crisis is affecting almost everyone, but some are much more deeply impacted than others, with poorer and prime age (25-55) adults especially in the front line. Just over three-quarters of UK adults reported in November that they tried to cut back on overall spending. This pattern of some belt-tightening hardly varies by income, but working adults in lower-income households were much more likely than those in higher-income households to report that they had tried to cut back a lot, and more likely to say that their financial situation was worse since the start of 2022. 42 per cent of workers in the bottom income quintile reported that they had tried to cut back a lot on overall spending, twice as many as in the top income quintile, and 63 per cent of workers in the bottom income quintile reported being worse off since the start of 2022, compared to 50 per cent of workers in the top income quintile. There is also a noticeable variation by age, with those aged 65 and above appearing to be relatively insulated, and tried to cut back at similar levels, on average, to workers in the top income quintile; they are also half as likely to have tried to cut back a lot on overall spending compared with those aged 35-44 (18 per cent versus 35 per cent).

While cutting back is widespread, there is a worryingly large minority of families at the sharper end of the cost of living crisis. There are large increases in people unable to afford essentials compared to the pre-pandemic period: the proportion of adults unable to replace electrical goods when needed has rocketed from 8 per cent in 2019-20 to 23 per cent (or 12 million adults), and the proportion unable to save £10 or more a month has risen from 6 per cent to 27 per cent (or 14 million adults). The 70 per cent rise in the cost of energy between 2019-20 and 2022-23 has led the proportion of adults reporting being unable to afford to switch the heating on when needed to rise from 5 per cent to 27 per cent (or 14 million adults). Instances of food insecurity have more than tripled from pre-pandemic levels, and now cover almost a third of adults; in November 2022, 28 per cent (up from 9 per cent pre-pandemic) of adults say that they could not afford to eat balanced meals, and 11 per cent or 6 million adults (up from 5 per cent pre-pandemic) reported being hungry in the past month but they didn’t eat as they lacked enough money to buy food.

These very alarming outcomes are more common among groups known to experience disadvantage. We find that 23 per cent of those receiving means-tested or disability benefits are severely food insecure this winter, up from 4 per cent pre-pandemic. Similarly, rates of food insecurity are much higher among families with three or more children, single parent families, and among certain non-white ethnic groups. Social renters were almost twice as likely as those living in other tenures to say that they could not afford to switch the heating on when needed this winter (45 per cent compared with 19 per cent for those who own their home outright).

The soaring cost of energy and other essentials will have longer-term impacts on financial resilience and health

While some of these impacts may be short-lived, there are signs that the cost of living crisis will leave a long-term mark on people's finances and health.

Unsurprisingly, rises in the price of essentials are making some families' budgets unsustainable, and debts are starting to accumulate particularly among low-income households. People are twice as likely to be increasing their debts now compared with the pandemic. In November, 11 per cent of respondents said that their debts had increased moderately or substantially in the past three months, rising to 20 per cent amongst workers in low-income families. This compares with 7 per cent of adults, and 12 per cent of low-income adults, who saw debts rise during the pandemic (comparing February 2020 to May 2021). As well as increasing their debts, people are increasingly falling behind on bills: 10 per cent of people – and a quarter of workers in poorer households - have missed at least one payment of a priority bill over the past three months (with 40 per cent of those blaming higher costs of energy or price rises of other essentials).

In addition, families are taking other actions to cope with higher costs today which will worsen their future financial resilience. In November 2022, just over one-quarter of adults (27 per cent) report using their savings to help make ends meet in the previous four weeks up, from one-in-five (20 per cent) in June. In the four weeks preceding the survey, 12 per cent of workers in the lowest income quintile report selling or pawning possessions they would have preferred to keep, 7 per cent have cancelled or not renewed their insurance, and 7 per cent say they have stopped or reduced pension contributions to save money.

There are not just financial consequences of the cost of living crisis; it is causing difficulties for people's mental and physical health. Consistent with findings from the ONS, our survey suggests that mental health has worsened since the pandemic, with the percentage of people facing emotional distress increasing from 40 per cent in October 2021 to 47 per cent in November 2022. The mental health of Black and Mixed-race people has worsened by more than other groups between the end of 2021 and 2022, with their emotional distress rising from 35 and 40 per cent to 50 and 58 per cent respectively. And there is a clear link between lower financial resilience and emotional distress. Those receiving state benefits (excluding Child Benefit or the state pension) are increasingly in emotional distress, with 64 per cent affected, compared to 42 per cent for those who do not receive any benefits. 41 per cent of people who are not behind on any bills feel that they are constantly under strain, but 72 per cent of those who are behind on two or more bills feel that they are constantly under strain. More generally, 21 per cent of people say that their health has been negatively affected by the rising cost of living, rising to one-third amongst poorer households.

We are only half way through a two-year crisis when it comes to household finances

Our survey shows us how people were coping in the run up to Christmas, but the rest of this financial year will still be grim. 45 per cent of respondents, or 24 million people, are fairly worried or very worried about their energy bills over the winter months, but this rises to 63 per cent of workers in the bottom income quintile, and 62 per cent of those paying their energy bills using a pre-payment meter (PPM) (compared with 43 per cent of people who pay energy bills using direct debit). This reflects that a typical household with a PPM will face costs of £250 in January alone to keep their heating and lights on, given that households typically use 45 per cent of their annual gas consumption in the period January to March.

But we cannot just think about this year. Although policy makers can hope that 2023 will bring better economic news than 2022, households' living standards are set to get worse before they get better – it is best to see this as a two-year crisis. Inflation may have peaked in late 2022 and is forecast to fall to 5.5 per cent in 2023-24, but lower price rises do not mean a lower cost of living. Food price inflation will continue to pose a particular problem for low-income households. In addition, although wholesale energy prices are now falling, retail prices paid by consumers will, on the very latest forecasts, rise, rather than fall, next year, because of the scaling-back of government support: the energy bill for a typical household in 2023-24 is set to be £850 higher (or 43 per cent more) than in 2022-23.

Furthermore, real wages are expected to keep falling until the second half of 2023 as inflation continues to outstrip wage growth. And there are other labour market impacts to come. The slowdown that is inevitable when an economy is hit by an energy shock means that unemployment is expected to rise, providing a concentrated living standards hit for some. The scale of any rise is uncertain, but the Office for Budget Responsibility (OBR) is forecasting 1.1 million more people will be unemployed by Q1 2024 than in early 2023.

Policy will make a difference, too – in both helpful and less-helpful ways. There will be a very welcome 10.1 per cent rise in most social security benefits in April 2023 –in line with last September's rate of inflation – a 9.7 per cent rise in the National Living Wage, and another round of Cost of Living Payments to those receiving social security benefits or the state pension. But personal tax changes will act as a brake on income growth. From April 2023, a typical middle-income household will see their personal tax bills rise by around £700 compared to a world where the Government had indexed all tax thresholds with prices, as is usual practice.

Moreover, the nature of the crisis will evolve as well as deepen in its second year. 2023-24 will see a dimly-remembered phenomenon affecting household finances – higher interest rates. Bank rate is currently 3.5 per cent (up from 0.25 per cent in January 2022), and current yield curves imply that it will peak in October 2023 at 4.6 per cent. This will result in new living standards pain for the around 1.8 million households with fixed-rate mortgages that are set to be renewed in 2023-24, as well as at least 1 million floating-rate mortgagors who face the impact of continued rises in the Bank of England's policy rate. Indeed, the average mortgagor household renewing their mortgage in 2023 will face a £3,000 annual increase in their mortgage costs.

The result of all this is that the second year of this living standards disaster which lies ahead of us may be as bad as the first. The typical after housing costs income of non-pensioner households is set to fall by 3 per cent in 2022-23, and fall by an even larger 4 per cent in 2023-24. A fall of that scale in 2023-24 would be the largest single-year fall since 1975, and the two-year fall of 7 per cent (or £2,100 for a typical household) is bigger than in the financial crisis, where there was a two-year decline of 5 per cent in typical working-age incomes. This precipitous decline will take typical real-terms incomes in 2023-24 back to where they were in 2018-19.

Income falls are bigger for higher – but not the highest – income households, but a crisis driven by the higher cost of essentials will always be tougher for those at the bottom

In both years of this two-year living standards disaster, income falls are generally greater as we move up the income distribution. Over the course of the two-year squeeze, real incomes among the poorest fifth of households will fall by 4 per cent, compared to 9 per cent for rich households (in the 19th vigintile of the distribution). This largely reflects government decisions to protect benefit income from high inflation, with Cost of Living Payments in both years being worth more to lower-income households than those on higher incomes, and benefits being uprated by 10.1 per cent in April 2023. Low-income households are also less affected by higher mortgage bills.

But the rising interest rates that drive those higher mortgage bills also raise the incomes of some households who see their savings and investment incomes rise. For the top 5 per cent, these income boosts are sufficient to offsets the drop in real earnings on average (their typical incomes are on course to rise by 4 per cent between 2021-22 and 2023-24), although higher interest rates are also likely to be associated with falling asset prices, and therefore wealth, for this group.

In setting policy for the year ahead, the Government has rightly prioritised support for lower-income households. This is the key response required when a country sees the cost of (largely imported) essentials rise swiftly. But the fact that poorer households are not seeing the biggest income falls during this crisis does not mean they are protected from the impact of the cost of living crisis for a number of reasons.

First, our headline results above follow the customary approach of assuming that the same inflation rate is suitable for all households. This is not the case at present, with rapid price rises in energy and food meaning that lower-income households, who tend to spend more of their budgets on these goods, facing higher-than-average effective inflation rates. We estimate that in November 2022, for example, the richest 10 per cent of households in effect faced an inflation rate 1.5 per cent lower than the poorest 10 per cent. Adjusting the pattern of income changes for these different inflation rates makes the fall in household incomes this year and next shared more evenly. When differential inflation is taken into account, real incomes among the poorest fifth of households will fall by 5 per cent, compared to 8 per cent for rich households (in the 19th vigintile of the distribution).

Second, the impact of income falls is greater for lower-income households because they went into the crisis with lower financial resilience. Pre-pandemic, the lowest-income households were four times as likely to have no savings as the highest income households, while 36 per cent of respondents to our survey (or 20 million adults) said they had savings of less than £1,000 this winter, with 21 per cent reporting that they had none at all. This is more severe for low-income families: 24 per cent of workers in the bottom income quintile had no savings at all, as well as 46 per cent of those who were out of work and on benefits. Our survey raises particular concerns about people in some ethnic groups: more than 52 per cent of Black people reported savings of less than £1,000, about double that of White people (28 per cent). Just 16 per cent of Black people (compared to 42 per cent of White people) say that they could use existing savings to pay for an unexpected expense, leaving them more likely to cut back on non-essentials (18 per cent) and essentials (14 per cent).

Overall, then, the lived experience of the crisis shows that the impact is worse for those on lower incomes. Almost one-in-five (19 per cent) of people in our survey – or 10 million – are not confident about their finances as a whole over the next three months, but for workers in the bottom income quintile, this rises to 32 per cent, and to 43 per cent for those not working and on benefits. And the overall falls in living standards mean that absolute poverty is set to rise in the short-run, from 17.2

per cent in 2021-22 to 18.3 per cent in 2023-24 (or an additional 800,000 people in poverty). Absolute child poverty is set to rise particularly quickly – by 2.9 percentage points (or 400,000 children) from 2021-22 to 2023-24, whereas absolute poverty among pensioners falls in 2023-24.

The end of the crisis brings the UK's fundamental living standards challenge back into focus, but also reveals some new directions in inequality

On the basis of current official forecasts, the cost of living crisis should ease in 2024: the OBR is currently assuming that falls in international gas prices could even drive negative inflation in 2024-25 and 2025-26. But the recovery is forecast to be slow, throwing attention back on the underlying driver of Britain's wage stagnation: weak productivity growth. Earnings are expected to grow a lot more slowly in the recovery from 2024 than they shrank during 2022 and 2023, with real wages not returning to their Q1 2022 level until the end of 2027 – nearly six years later.

Similarly, although incomes are set to grow in 2024-25 (except where the loss of the £900 Cost of Living Payments pushes incomes down at the bottom), this is set to be the worst Parliament on record for living standards for almost all parts of the income distribution. Indeed, typical incomes are set to be below their real-terms pre-pandemic (2019-20) level even in 2027-28. But higher wage growth could improve this scenario. If real wages grew by 1 percentage point more per year than projected, median incomes would reach their pre-pandemic level in 2025-26.

The forecast growth in incomes from 2024-25 looks set also to increase relative poverty (although relative poverty is set to fall considerably in 2022-23 and 2023-24, as typical income falls by more than that of low-income households). Worryingly, relative child poverty returns to its upward trend when the cost of living crisis ends, as the two-child limit, the benefit cap and frozen Local Housing Allowance (LHA) rates continue to drag down income growth at the bottom of the distribution. Child poverty in 2027-28 is forecast to be the highest since 1998-99, meaning 170,000 more children will be in poverty than in 2021-22. This rise is driven entirely by large families: child poverty for families with three or more children is set to hit 55 per cent in 2027-28, and 77 per cent of children in families with four or more children will be in poverty by 2027-28.

New patterns of inequality, though, will arise as we return to an era of higher interest rates. Rising mortgage costs will see typical incomes among mortgagors fall by 12 per cent between 2021-22 and 2023-24, significantly more than average. This will reduce the relative living standards advantage that mortgagors have built up over other households in recent decades as interest rates have trended downwards: the typical income of mortgagors will fall from 30 per cent higher than the overall median in 2021-22, to 22 per cent by 2024-25. This will still be higher than the 16 per cent premium that mortgagors had in 2007-08, so represents only a partial correction to the long-term trend for mortgagors' living standards to grow faster than other households.

However, those at the very top of the income distribution will do very well from rising interest rates. Overall, the OBR expects a rise of around £65 billion in gross household interest receipts between 2021-22 and 2023-24, and they also project that interest receipts as a proportion of income will rise from just over 1 per cent in 2021 to 6 per cent in 2024. This boost to household income will be heavily skewed towards the top of the distribution, as high-income households are much more likely to have money in savings or other financial investments. Indeed, although income inequality across the bulk of the distribution will fall during 2022-23 and 2023-24, this rapid growth in investment income means that the Gini coefficient, while highly uncertain, is currently projected to rise in each of the next five years, and under our forecasts would reach a record high of 40.8 per cent in 2027-28.

Policy can make a difference this winter, in the tough year ahead, and in addressing our long-term stagnation

These are clearly worrying findings about how low-income households are coping this winter, and truly terrible forecasts for household living standards over the medium-term.
Our findings also highlight that policy is already making a significant difference, protecting (in relative terms) lower-income households' incomes, and point to several areas where debates about further government action are likely to focus.

The fact that wholesale gas prices have now fallen, while retail energy prices households face are set to rise, means there is likely to be a renewed debate about the level of the Energy Price Guarantee and whether it should rise above its current £2,500 level in April. To help households through this and future winters, the Government could look at the Cold Weather Payments. These have the huge advantage of being paid automatically to households on some means-tested benefits when the temperature dips. But they could protect more households from the worst impacts of winter if the trigger temperature was raised, so that they are paid more often, and eligibility extended to more working-age households receiving benefits.

Looking further ahead, the Government is currently considering how to support households with energy bills from April 2024, when the Energy Price Guarantee is due to end. It is welcome this includes considering the practicalities of a social tariff, which offers the only route to being able to target support at a wider range of lower-income households than those claiming benefits, and to recognise big differences in energy needs between households. It goes without saying that in the medium-run, better insulation is key to reducing household energy bills and easing the transition to net zero. With both main political parties now saying this is a key priority, a recent report from the Resolution Foundation suggests turning that rhetoric into reality will require a greater focus on the most difficult part of the challenge: inefficient walls in the UK's homes.

For 2023-24, the Government has decided to focus support for households on those receiving social security benefits or the state pension. This makes it more important than ever that those entitled to those benefits claim them – there are 850,000 people going without Pension Credit, for example – and the Government (and other organisations) should be doing what they can to encourage take-up of means-tested and disability benefits. Discretionary local authority-run schemes will have an important role to play in this crisis, but the fact that as many as one-in-four local authorities in England do not provide crisis support as part of these schemes is of real concern. The UK Government should mandate a minimum provision of crisis support by local authorities, if necessary with ring-fenced funding (but without setting targets on what proportion of support should be allocated to a certain demographic group, as these reduce local authorities' ability to target help where it is needed).

A consistent theme in our findings is how outcomes are considerably worse for families with three or more children than those with one or two children, whether that is food insecurity in the current crisis, or relative poverty. In the short-run, it is unfortunate that the same Cost of Living Payments are being made to all households on Universal Credit regardless of whether this is a single person or a family of five or more; varying the payments by family size would have allowed them to match energy need more closely. In the medium-run, it is clear that families with three or more children are heavily affected by the two-child limit, the benefit cap (although this is being increased by inflation this year, its first nominal increase since its introduction in 2013), and the post-pandemic freeze in LHA rates. All of these policies should be reviewed.

Finally, stepping back, it is clear that, since 2019-20, two major economic crises have combined with the UK's long-standing weakness in productivity to create eight wasted years for household living standards. With the Covid-19 pandemic and the current cost of living crisis coming after a fifteen-year period characterised by low growth and high inequality, there is a real risk that the UK is cemented as a stagnation nation. Measures that could help solve those fundamental weaknesses of the UK economy are the subject of our ongoing project with the Centre for Economic Performance at the London School of Economics; this work will conclude in late 2023.

Section 1

Introduction

This is our fifth Living Standards Outlook, our regular assessment of what government policy and economic forecasts mean for household incomes across the income distribution, poverty rates and inequality.[1] This year, our outlook combines our projections for household incomes and poverty levels with the results from a survey fielded by YouGov in late November 2022 of 10,000 adults in the UK, exploring how they are coping with the current crisis.

2022 saw earnings grow rapidly, but not as fast as the cost of living, leading to substantial policy interventions to support households with high costs of essentials

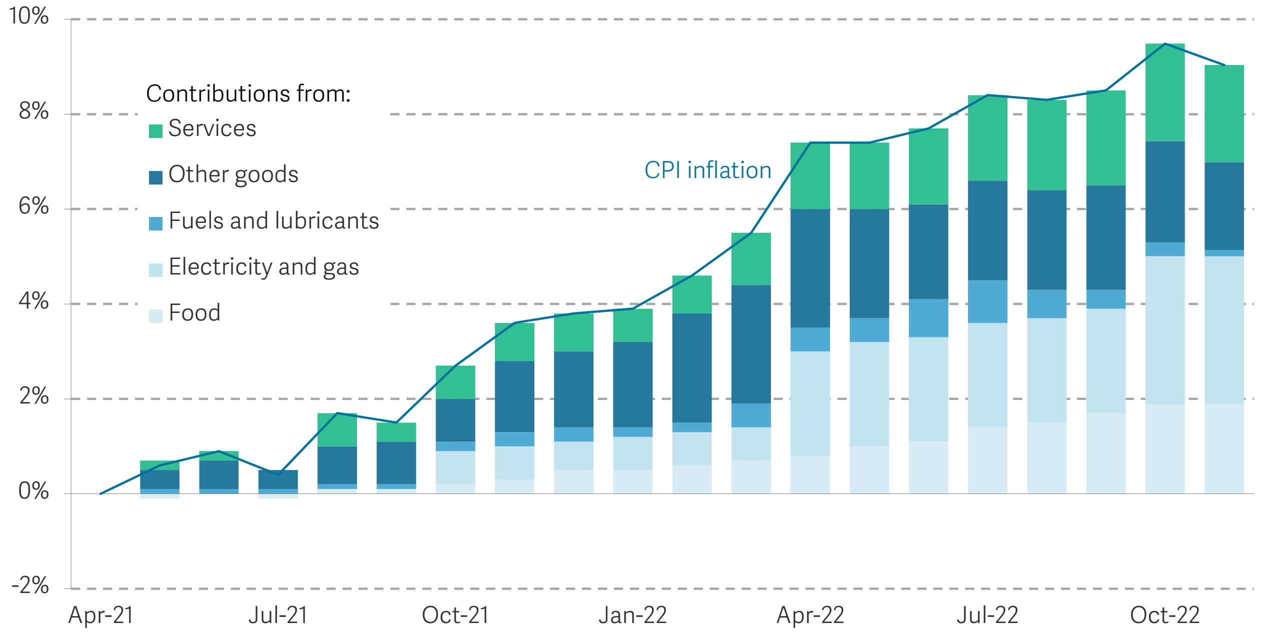
This Living Standards Outlook comes out in the depths of a cost of living crisis. In October 2022, inflation reached its highest level in 40 years, energy bills reached previously unimaginable rates, and earnings fell consistently over the course of 2022. As Figure 1 shows, the UK's high inflation is primarily being driven by rising prices for energy, food, and other goods – with three-quarters of the rise in inflation attributed to these factors. These are all import-intensive – which means that we are beholden to global prices for energy, food and other goods.[2] And as higher global demand following the Covid-19 pandemic, supply chain disruptions, and higher European energy prices have all affected global markets, the effects of this are passed on to consumers in the UK. High and rising energy and food costs are especially worrying, because food and energy take up a higher proportion of low-income households' spending – meaning increases in these essentials harm them more.[3] Furthermore, as essentials take up a larger proportion of low-income households' consumption, it is harder for them to cut back on spending

1 Previous Living Standards Outlooks are: A Corlett, G Bangham & D Finch, The Living Standards Outlook 2018, Resolution Foundation, February 2018; A Corlett, The Living Standards Outlook 2019, Resolution Foundation, February 2019; M Brewer et al., The Living Standards Outlook 2021, Resolution Foundation, January 2021; A Corlett & L Try, The Living Standards Outlook 2022, Resolution Foundation, March 2022. We also published a shorter update of the Living Standards Outlook 2022 later in the year, to account for the deepening of the cost of living crisis: A Corlett & L Try, In at the deep end: The living standards crisis facing the new Prime Minister, Resolution Foundation, September 2022.
2 E Fry, S Hale & J Smith, Macroeconomic Policy Outlook: Q4 2022, Resolution Foundation, December 2022.
3 ONS, Inflation and cost of living for household groups, UK: October 2022.

when prices are higher, whereas higher-income households are able to cut back more, as a higher proportion of their spending is devoted to luxuries.

FIGURE 1: **High inflation is being driven by significant increases in energy and food prices**

Contributions to the rise in CPI inflation since April 2021: UK

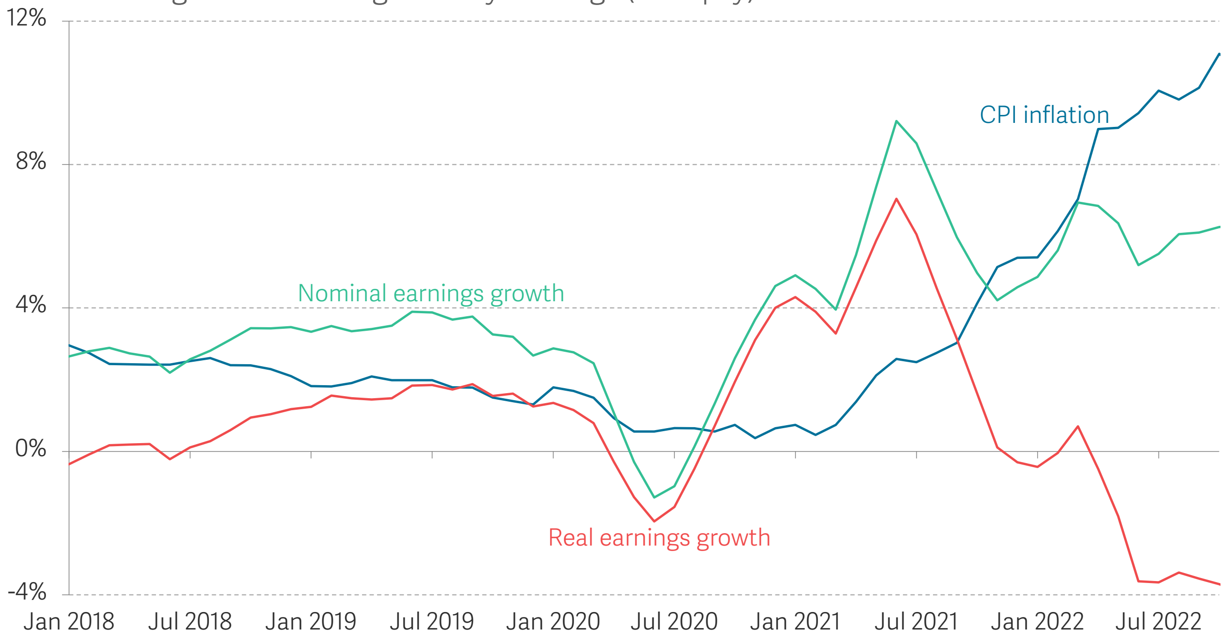


SOURCE: RF Analysis of Bank of England, Monetary Policy Report November 2022, ONS, Consumer Price Inflation.

As we discuss more in Section 3, the labour market context over the past year has been one of low unemployment, and some of the fastest nominal growth in earnings for some years. In 2022, nominal wage growth will have averaged 6.1 per cent, the highest rate since 1991. By comparison, nominal wage growth over the 2000s averaged around 4 per cent, and over the 2010s it only averaged 2 per cent. However, despite this high nominal wage growth, wages this year have failed to keep up with prices, which have grown even faster, with CPI inflation averaging around 9 per cent in 2022. This means that workers in the UK have faced a fall in their real wages over the course of this year.

FIGURE 2: **Despite strong growth in nominal wages, they have not kept up with rising prices**

Annual growth in average weekly earnings (total pay) and CPI inflation: UK



NOTES: Nominal and real earnings growth is three month on three month annual growth, with data being for the three months ending in the month shown. Average Weekly Earnings data is GB only.
SOURCE: ONS, CPI; ONS, Labour Market Statistics.

2022 also saw the Government provide several rounds of financial support to help households with high energy bills, some of which were for 2022-23 and others for 2023-24; we summarise the impact of those taking effect in 2023-24 in Section 3, and we have analysed those for 2022-23, which are estimated to cost £58bn, in other reports.[4]

This report combines forecasts of living standards, based on official projections, with new survey data on the impact of the crisis this winter

This Living Standards Outlook provides an assessment of what government policy and economic forecasts mean for household incomes across the income distribution, poverty rates and inequality. We take the 2019-20 edition of the DWP's Family Resources Survey dataset as the base, and combine this with more up-to-date data on core economic aggregates to create nowcasts from 2020-21 to the current year, and then

4 HM Treasury, Autumn Statement 2022 Policy Costings, November 2022; T Bell et al., Help today, squeeze tomorrow: Putting the Autumn Statement 2022 in context, Resolution Foundation, November 2022. Our analysis of the various forms of cost of living support can be found in: A Corlett et al., The price is right? The April 2022 energy price rise and the government's response, Resolution Foundation, February 2022; T Bell et al., Inflation Nation: Putting Spring Statement 2022 in context, Resolution Foundation, March 2022; T Bell et al., Back on target: Analysis of the Government's additional cost of living support; Resolution Foundation, May 2022; T Bell et al., Blowing the budget: Assessing the implications of the September 2022 fiscal statement, Resolution Foundation, September 2022.

create forecasts until 2027-28, using the OBR's forecasts of those same aggregates.[5] We also consider tax and benefit policy changes in our nowcasts and forecasts. There is, of course, a great deal of uncertainty associated with economic forecasts: for example, the OBR and the Bank of England's latest forecasts – which were released in the same month – show quite different outcomes in areas such as inflation and unemployment.[6] Indeed, our forecasts should be interpreted as a likely path for household incomes, poverty and inequality rates given current (namely, the OBR's) economic forecasts, and government policy. Of course, if policy changes, and economic factors do not follow current forecasts, then the path household incomes follow will look different to what is shown here.

Our forecasts for income growth, poverty rates, and inequality allow us to determine the effect of economic factors such as inflation, earnings growth and interest rates during the cost of living crisis, and on incomes following the crisis. However, our forecasts can only show the effect of the cost of living crisis on household incomes, not how people are affected by the crisis in a more practical sense. We therefore combine these forecasts with results from an online YouGov survey of more than 10,000 adults aged 18+. The survey was conducted in late November (23 to 30 November), after the 2022 Autumn Statement (17 November), in which the Chancellor announced details of the Energy Price Guarantee for 2023-24, confirmed that benefits and the state pension will rise in April 2023 in line with inflation (in the usual way), and announced a new round of Cost of Living Payments in 2023-24.

The rest of this report is set out as follows:

- Section 2 focuses on how different families are experiencing the cost of living crisis this winter, using results from our recent survey.
- Section 3 sets out the drivers that will determine household incomes going forward, including inflation, earnings, benefits, employment, housing costs, and taxes.
- Section 4 sets out what the trends set out in Section 3 would mean for household incomes across the distribution, absolute and relative poverty, and overall inequality. Our forecasts look at the cost of living crisis period (2022-23 and 2023-24), and the recovery from the crisis (2024-25 to 2027-28).
- Section 5 concludes, and provides recommendations on how the Government can best support people during the cost of living crisis.

5 The 2020-21 Family Resources Survey dataset has been released, but it was heavily affected by the Covid-19 pandemic. See: Department for Work and Pensions, Technical report: assessment of the impact of COVID-19 on the HBAI statistics for FYE2021, May 2022.
6 OBR, Economic and Fiscal Outlook, November 2022; Bank of England, Monetary Policy Report, November 2022.

- Annex 1 sets out the methodology for our forecasts and the assumptions underlying our projections.
- Annex 2 presents some of the key inputs into our forecast, and some of our main findings.

Section 2

How are people currently experiencing the cost of living crisis?

Results from an online survey of 10,470 UK adults in the field in late November confirm that the cost of living crisis is affecting almost everyone, but some are being much more deeply impacted than others, with poorer and prime-age (25-55) adults in the front line. Just over three-quarters of UK adults (76 per cent) reported in November that they tried to cut back on overall spending, with slightly more saying that they are trying to cut back on energy. This pattern of some belt-tightening varies only a little by income, but working adults in lower-income households were much more likely to report that they had tried to cut back a lot, and more likely to say that their financial situation was worse than a year ago. 42 per cent of workers in the bottom income quintile reported that they tried to cut back a lot on overall spending, twice as many as in the top income quintile, and 63 per cent of workers in the bottom income quintile reported being worse off than the beginning of 2022, compared to 50 per cent of workers in the top income quintile. There is also an age gradient: those aged 65 and above are relatively insulated, trying to cut back at similar levels on average to workers in the highest income quintile. Indeed, they are half as likely to have tried to cut back a lot on overall spending compared with those aged 35-44.

While cutting back is widespread, the sharper end of the cost of living crisis is biting for a worryingly large minority of families struggling with more acute struggles. Compared to before the pandemic, there are large increases in people unable to afford essentials: the proportion of adults unable to replace electrical goods when they need to has rocketed from 8 per cent to 23 per cent (or 12 million adults), and the proportion unable to save regularly has risen from 6 per cent to 27 per cent (or 14 million adults). The 70 per cent rise in the cost of energy by 2022-23 since 2019-20 has led the proportion of adults reporting being unable to adequately heat their home to rise from 5 per cent to 27 per cent (or 14 million adults). Instances of food insecurity have more than tripled from pre-pandemic levels, and now cover almost a third of adults; in November 2022, 28 per cent (up from 9 per cent pre-pandemic) of adults say that they could not afford to eat balanced meals, and 11 per cent (up from 5 per cent pre-pandemic), or six million adults, reported being hungry in the past month because they lacked enough money to buy food.

These more-alarming outcomes are more common among groups known to experience disadvantage. 23 per cent of those receiving means-tested or disability benefits are severely food insecure this winter, up from 4 per cent pre-pandemic. Rates of food insecurity are much higher among families with three or more children, single parent families, and among certain non-white ethnic groups. Social renters were almost twice as likely to say that they could not afford to keep their homes warm (45 per cent, compared with 19 per cent for those who own their house outright).

While some of these impacts may be short lived, there are signs that the cost of living crisis will leave its mark on people's longer-term finances and health. Unsurprisingly, rises in the price of essentials are making some families' budgets unsustainable, and debts are starting to accumulate, particularly among low-income households. People are twice as likely to be increasing their debts now compared with the pandemic. This winter, 11 per cent of respondents said that their debts had increased moderately or substantially in the past three months, rising to 20 per cent amongst workers in low-income families. This compares with 7 per cent of adults, and 12 per cent of low-income adults, during the pandemic (comparing February 2020 to May 2021).

As well as increasing their debts, people are increasingly falling behind on bills. 10 per cent of people – and a quarter of workers in poorer households – have missed at least one payment of a priority bill over the past three months (with 40 per cent of those blaming higher costs of energy or price rises of other essentials).

Even for those not going into debt, families are taking actions to cope with higher costs today which will worsen their future financial resilience. Just over a quarter of adults (27 per cent) report using their savings for daily living expenses in the past four weeks, up from one-in-five (20 per cent) in June. Among workers in the lowest income quintile, 12 per cent report selling or pawning possessions they would have preferred to keep, 7 per cent have cancelled or not renewed their insurance, and 7 per cent say they have stopped or reduced pension contributions to save money.

The rising cost of living is not just having harmful financial consequences; it is causing difficulties for people's mental and physical health. Our survey suggests that mental health has worsened since the pandemic, with the percentage of people facing emotional distress increasing from 40 per cent in October 2021 to 47 per cent in November 2022. The mental health of Black and Mixed-race people has worsened by more than other groups, with their emotional distress rising from 35 and 40 per cent to 50 and 58 per cent respectively. ONS survey evidence shows that the proportion of adults reporting high levels of anxiety in October to December 2022 were at their highest levels (35.2 per cent) since December to February 2021 (35.7 per cent) when strict lockdowns were implemented during the festive period. And there is a clear link between lower financial resilience and emotional distress. Those receiving state benefits (excluding Child Benefit or the state pension) are increasingly in emotional distress, with 64 per cent affected compared to 42 per cent for those who do not receive any benefits. 41 per cent of people who are not behind on any bills feel that they are constantly under strain, but 72 per cent of those who are behind on two or more bills feel that they are constantly under strain. More generally, 21 per cent of people say that their health has been negatively affected by the rising cost of living, rising to a third amongst poorer households.

Even if the crisis ended now, the way that the crisis is affecting financial resilience and health means that its adverse, and unequal, impacts will persist.

The cost of living crisis is having widespread effects across the UK

While the pandemic was the pre-amble, a huge shock to people's finances has taken place in 2022

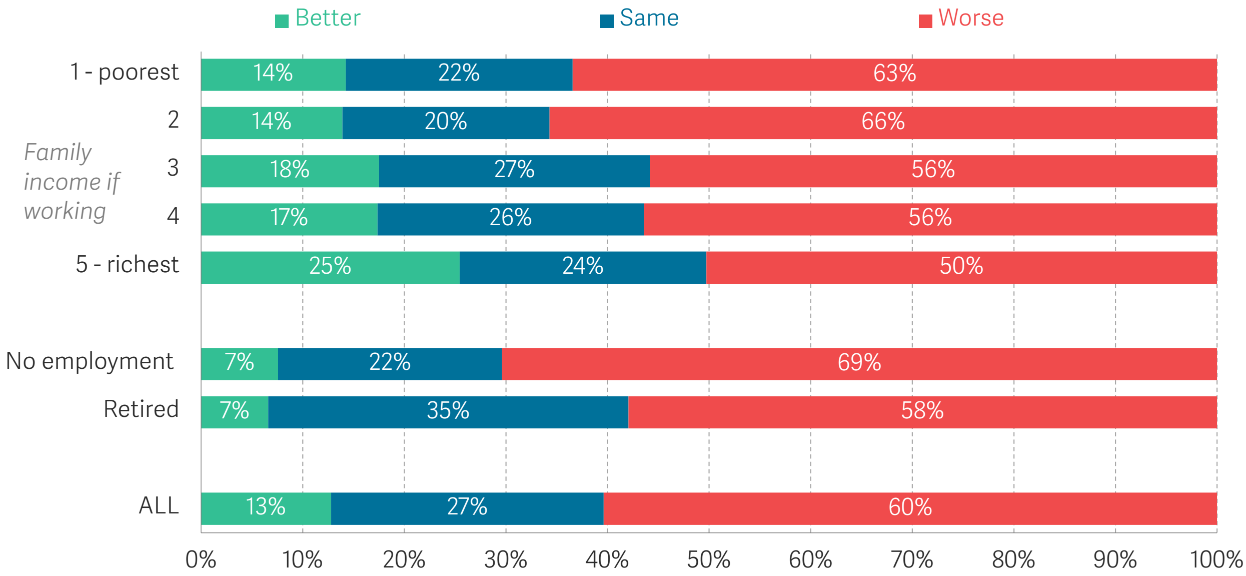
This Section reports results from an online YouGov survey of more than 10,000 adults; the survey was conducted in late November (23 to 30 November), and is the first of three that we will commission to study the impact of the cost of living crisis. It shows that the cost of living crisis is having extremely widespread impacts. This winter, 60 per cent of adults (equivalent to 32 million adults) said that their financial situation is worse compared with the beginning of 2022, four times as many as who said that their situation is better (Figure 3).[7] This pattern broadly holds across the income distribution, with 63 per cent of workers in the bottom quintile of the income distribution and 50 per cent of workers in the top quintile saying that they are worse off this winter than the beginning of 2022. Similarly (and not shown in the figure), there was little variation between those who do and do not receive benefits: 66 per cent of benefit recipients and 59 per cent of non-recipients say that their financial situation is worse.

However, those who are retired were more likely than other groups to say that their situation will be unchanged compared with the start of 2022, with 34 per cent saying this.

7 ONS, Estimates of the population for the UK, England, Wales, Scotland and Northern Ireland, 53.2 million adults aged 18+ in 2021.

FIGURE 3: **People are over four times as likely to report being worse off compared to the start of 2022 than better off**

Percentage of respondents reporting a change in their financial circumstances compared to the start of 2022: UK, 23-30 November 2022



NOTES: Income is equivalised and bracketed using uprated HBAI data from 2019-20. 'Unknown' answers are all below 6 per cent and have been excluded. Better includes both 'is now a lot better' and 'is now a little better'. Worse includes both 'is now a little bit worse' and 'is now a lot worse' All (n=10,470), lowest income quintile (n=988), q2 (n=740), q3 (n=897), q4 (n=703) and highest income quintile (n=1128). No employment (n=1631), Retired (n=2,824). Unknowns have been excluded. These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave.

BOX 1: **More details on the survey, and on creating income quintiles.**

Throughout this report, survey results are broken down by quintiles of equivalised family income for respondents who were in work. This was done by asking working respondents to give details of the overall family income (in bands); by adjusting this to take account of family composition, we created estimates of equivalised family income. We then used a projection of the income distribution in 2022-23 to put survey respondents into population-level income quintiles. All results for specific quintiles should be understood as being for working respondents only, but using whole-population quintiles (rather than quintiles only of working families).

We also show results for those not in employment: 32 per cent of these is people who are not working due to long-term sickness, 21 per cent are students without paid work, 18 per cent are caregivers and 16 per cent are people who are unemployed (n=1,631). Finally, we show results for those who are retired, 87 per cent of whom are aged 65+ (n=2,751).

But the effects of the crisis are worse for some

As families feel the effects of squeezed earnings combined with higher prices, just over three-quarter of households (76 per cent) report that they are trying to cut back on their overall spending (Figure 4). There is little variation here by income – 85 per cent of workers in the bottom quintile and 76 per cent of those in the top quintile are trying to cut back back – or between workers and non-workers. This matches recent retail sales data which shows that, while the value of sales is up 4 per cent compared with the same time last year, the volume has fallen by 6 per cent (November 2021 compared with November 2022).[8]

But there is a stronger gradient in who reports they are trying to cut back a lot, with more than twice as many workers in the bottom income quintile reporting that they are doing this compared to the top income quintile (42 per cent vs 18 per cent). This should not come as a surprise – as we discussed in Section 1, those goods and services seeing the fastest price rises make up a higher fraction of the budget of low-income households, meaning they have less slack; energy and food are essential, meaning it's harder to cut back; and low-income families tend to have fewer savings to draw down.

Across different age groups, it seems that younger adults (but not those aged under 25) are more likely to be trying to cut back than older adults. 82 per cent of those aged 35-to-44 are trying to cut back on their overall spending, but just 70 per cent of those aged 65 or over are trying to cut back.[9] In addition, those aged 65 and above are half as likely to have tried to cut back a lot (rather than a little) on overall spending (52 per cent as likely) compared with those aged 35-44. Those aged 18-24 appear to be the least likely to be trying to cut back, but they are also the most likely not to have given an answer to the question. On the other hand, 44 per cent of this group live in a house owned or rented by others, and so they may not face the same cost pressures as other groups.

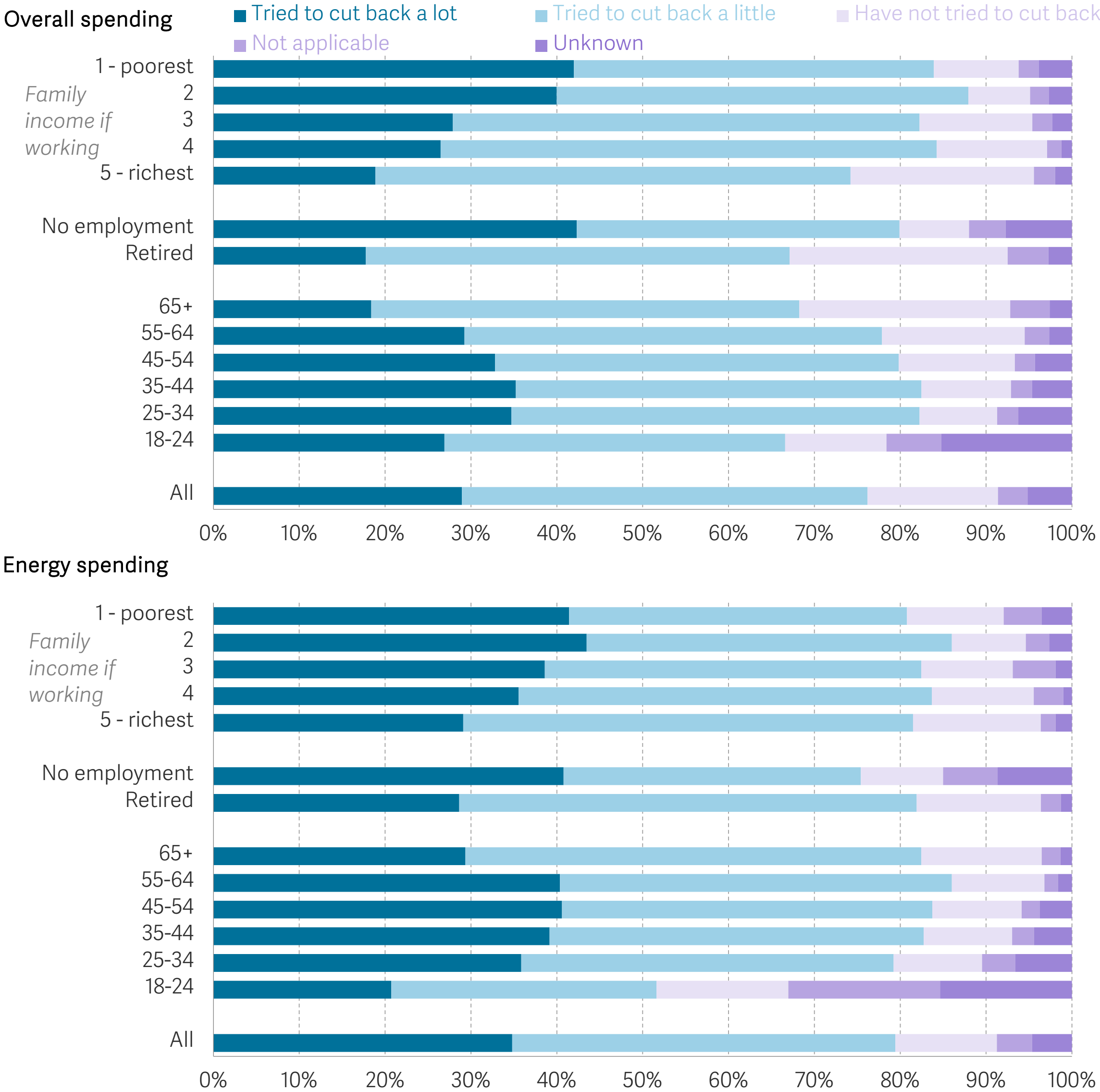
High global energy prices have had an extremely detrimental effect on energy bills at home. Annual household expenditure on gas and electricity has increased sharply in 2022-23 to £2,000 – a 70 per cent rise in the cost of energy since 2019-20. Bills will continue to rise, and a typical bill is set to increase by £850 in 2023-24 to reach £2,850 for the typical household as the government scales back support under the Energy Price Guarantee.[10] It is unsurprising, therefore, that the vast majority of households said that they were trying to cut back on their energy consumption in November. Almost four-in-five people are trying to cut back on energy consumption either a little or a lot, with more than 80 per cent of people in each income bracket trying to cut back. There is little

8 ONS, Retail Sales, GB, Seasonally Adjusted: All Retailers ex fuel: All Business Index.
9 Of those aged 18-24, 44 per cent live in a house owned or rented by others, and therefore they don't have the same outgoings as other age groups (18-24 n=865), (Living in home owned/rented by someone else n= 373).
10 Typical energy bills include the £400 discount which is split over 2022 and 2023.

difference here between those with and without a pre-payment meter (PPM): 76 per cent of those with PPMs report trying to cut back on energy (of which 39 per cent are trying to cut back a lot), compared with 80 per cent of those paying via Direct Debit (of which 34 per cent are trying to cut back a lot), but we show later that worry about future energy bills varies markedly by whether a household uses a PPM.[11]

FIGURE 4: **Almost 80 per cent of people are trying to cut back on energy and overall spending**

Percentage of respondents reporting trying to cut back on different areas of spending in the past 3 months: UK, 23-30 November 2022



NOTES: Income is equivalised and bracketed using uprated HBAI data from 2019-20. All (n=10,470), 18-24 (n=865), 25-34 (n=1,480), 35-44 (n=1,999), 45-54 (n=1,625), 55-64 (n=1,750), and 65+ (n= 2,751). Lowest income quintile (n=988), q2 (n=740), q3 (n=897), q4 (n=703) and highest income quintile (n=1128). No employment (n=1631), Retired (n=2,824). PPM (n=1366), Direct Debit (n=7540). These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave.

11 Those on PPMs will be facing much larger rises in the cost of energy this winter compared to this summer, given that they are unable to smooth spending across the year. See: T Bell et al, Help today, squeeze tomorrow, The Resolution Foundation, November 2022

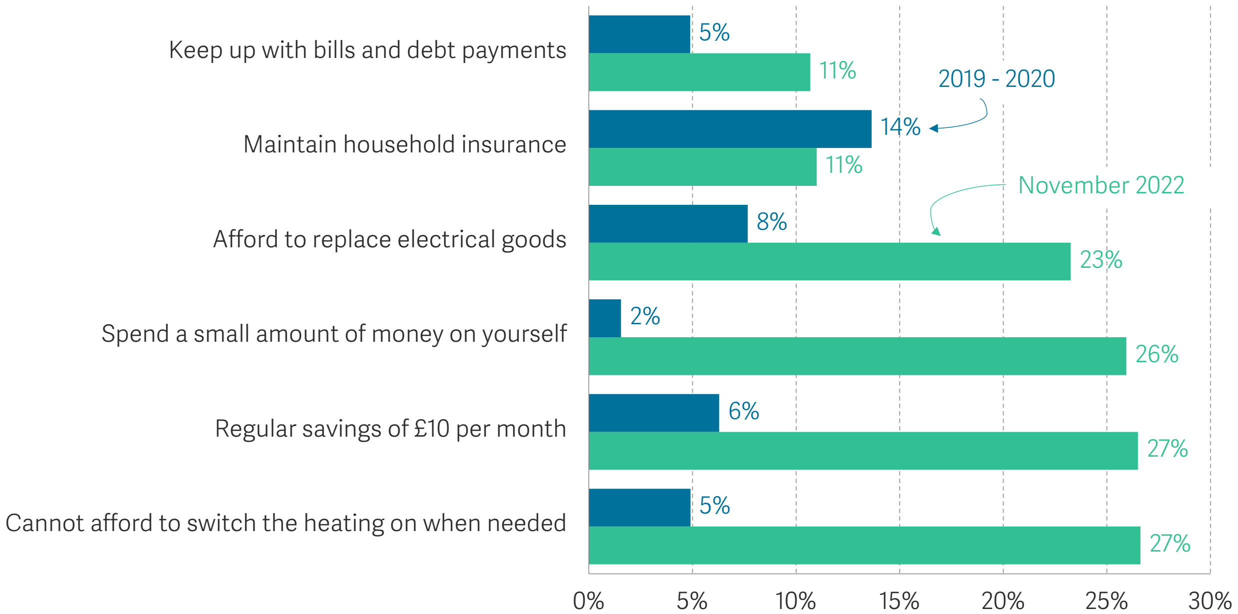
It should be noted, though, that National Grid data suggests that gas consumption in the September to November period had fallen just 0.3 per cent for all end users excluding power stations, having adjusted for the warm weather, suggesting that these behaviour changes might only be very small to date.[12]

The choice to heat or eat has become far more pervasive this winter than even during the pandemic

While trying to cut back is widespread, some families are far more likely to be experiencing the sharp end of the cost of living crisis. Figure 5 looks at the percentage of respondents saying in November 2022 that they could not afford certain key essentials alongside a comparison with 2019-20 (using the Family Resources Survey). There are large increases in, for example, the proportion of people who are unable to replace electrical goods when they need to, rising from 8 per cent of people before the pandemic to 23 per cent now (or 12 million people). With prices rising, and money squeezed, people are also far less likely to report that they are unable to make regular savings of £10 per month, growing from 6 per cent to 27 per cent of people (or 14 million people).

FIGURE 5: **Families are less able to afford items than before the pandemic**

Percentage of respondents reporting being unable to afford certain essentials: UK, 2019-20 and 23-30 November 2022



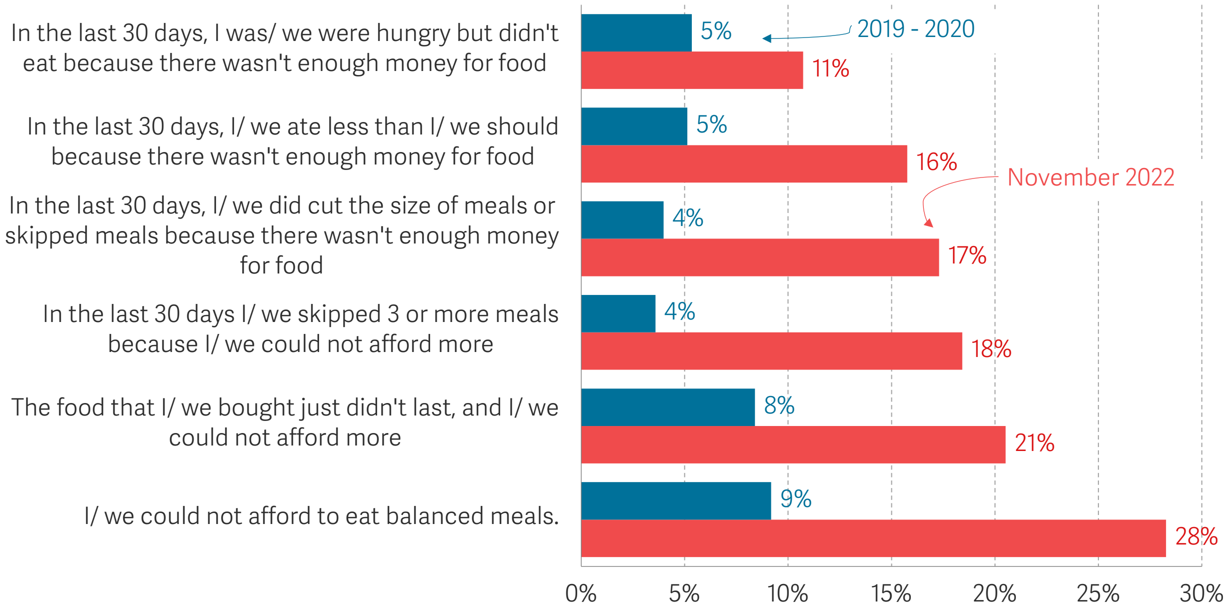
NOTES: Responses shown for all adults aged 18+. Base (n=10,470). Respondants responded to statements with 'We/I would like to have this but cannot afford this at the moment'. These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave; DWP, Households Below Average Income, HBAI, 2019-20, DWP, Family Resources Survey, FRS, 2019-20.

12 I Staffell et al, Q3 2022: No Sign Of Britain's Gas Demand Falling, Imperial College, Q3 2022.

We can also compare our survey respondents' ability to afford food to the same set of questions fielded in 2019-20: this is shown in Figure 6. In November 2022, 28 per cent of adults say that they could not afford to eat balanced meals within the last 30 days (up from 9 per cent pre-pandemic), and 11 per cent (equivalent to more than six million people) said that they were hungry but didn't eat because there wasn't enough money for food in the past month (compared with 5 per cent pre-pandemic).

FIGURE 6: **Families are increasingly going hungry**

Percentage of respondents reporting being unable to afford sufficient food: UK, 2019-20 and 23-30 November 2022



NOTES: Responses shown for all adults aged 18+. Base (n=10,470). Respondents to those who said 'often true' (10 per cent) and 'sometimes true' (18 per cent) These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave; DWP, Households Below Average Income, HBAI, 2019-20, DWP, Family Resources Survey, FRS, 2019-20.

As discussed in Box 2, we can combine the six items shown in Figure 6 into a single indicator of food insecurity, and we plot that in Figure 7. Our survey suggests that food insecurity stands at 31 per cent of adults, as food inflation reached 16.4 per cent in November 2022, compared with 8 per cent in 2019-20. These findings are in line with the rapid rises in food insecurity observed over 2022, with the Food Foundation finding that total insecurity was already 18.4 per cent in September, more than double the levels in January 2022 (8.8 per cent), and higher even than the first two weeks of lockdown in 2020.[13]

13 For example, see: Food insecurity tracking, The Food Foundation, September 2022 which uses three of the six questions from Box 2 (questions 3, 4 & 5), and asks whether they have experienced these in the past 30 days and past 6 months; and, R Earwaker, Going under and without: JRF's cost of living tracker, winter 2022/23, JRF, December 2022.

BOX 2: **Measuring food insecurity**

In this report, we assess food insecurity using six standardised questions which are internationally aligned with questions asked by the United States Department of Agriculture (USDA) and with the DWP's Family Resources Survey (FRS). These six questions or statements are as follows:

- The food that [I/we] bought just didn't last, and [I/we] didn't have money to get more.
- [I/we] could not afford to eat balanced meals.
- In the last 30 days, did you ever eat less than you felt you should because there wasn't enough money for food?
- In the last 30 days, were you every hungry but didn't eat because there wasn't enough money for food?
- In the last 30 days, since last (name of current month), did (you/you or other adults in your household) ever cut the size of your meals or skip meals because there wasn't enough money for food?
- How many days during the past 30 days did you cut the size of your meals or skip meals because there wasn't enough money for food

Each question is scored as 0 or 1 with the total of 2 to 6 is considered 'food insecure', a score of 2 to 4 'moderately food insecure', and a score of 5 or 6 considered to be 'severely food insecure'. The FRS assesses food insecurity using a total of 10 questions, although the outcomes of these 6 questions are aligned with the food insecurity measure found in the FRS. The Food Foundation uses a subset of three questions. [14]

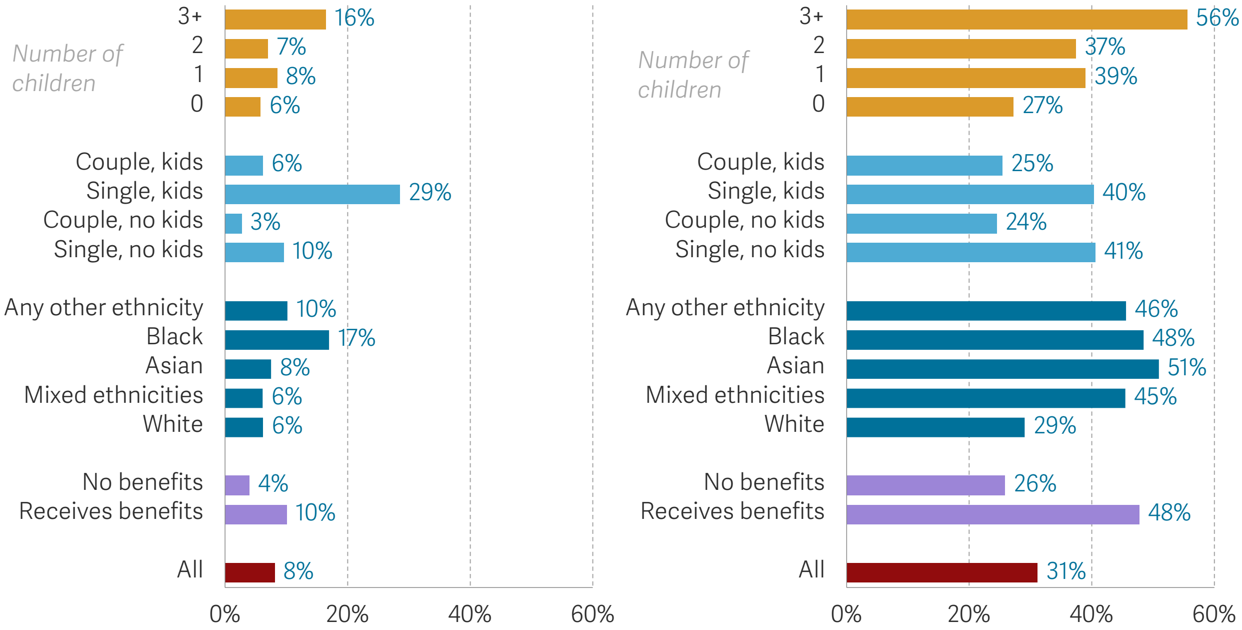
Before the pandemic, moderate or severe food insecurity was already higher for those with more children, and single parents. For example, 16 per cent of those with three or more children were food insecure, which has tripled to 56 per cent of families with three or more children this winter. 29 per cent of single parent families were food insecure before the pandemic which has risen to 40 per cent of single parent families.

Ethnic minorities are also likely to be experiencing higher levels of food insecurity, for example 51 per cent Asian and 48 per cent of Black adults reported that they were experiencing food insecurity compared with 29 per cent of White adults.

14 Food insecurity tracking, The Food Foundation, September 2022.

FIGURE 7: **Severe and moderate food insecurity is rising sharply**

Percentage of respondents in moderate food insecurity: UK, 2019-20 (left) and 23-30 November 2022 (right)



NOTES: Full description of food insecurity included in Box 2. Responses shown for all adults aged 18+. Base, All (n=10,470); No children (n= 7,846) one child (n=1,132) two children (n= 1,003) three or more children (n=421); Couple with children (n= 4,430) single with children (n= 1,408) couple with no children (n= 2,082) single with no children (n= 2,550); White (n= 9,359) Mixed or multiple ethnicities (n= 179) Asian (n= 344) Black (n= 93) Any other ethnicity (n=53); Receives benefits (n= 2,507) No benefits (n= 7,963). Benefits includes carers allowance, DLA/PIP, ESA, Housing Benefit, Income Support, JSA, Council Tax Support, UC, working tax credit and pension credit. These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave; DWP, Households Below Average Income, HBAI, 2019-20, DWP, Family Resources Survey, 2019-20.

It is particularly concerning that severe food insecurity, where people more regularly run out of food, or have gone for multiple days in the month without eating sufficiently because they cannot afford food, has risen from 3 per cent of people to 11 per cent of people. 9 per cent of single parent families were already severely food insecure pre-pandemic, but this has doubled to 18 per cent. Before the pandemic, 4 per cent of families with three or more children had severe food insecurity compared with 2 per cent of families of no children. But this winter, this has risen almost five times to 21 per cent of families with three or more children, compared with 10 per cent of families with no children under 18. Finally, 23 per cent of those receiving benefits are now severely food insecure this winter, up from 8 per cent pre-pandemic. Box 3 summarises findings from a companion report that explored how people with disabilities are faring in the current crisis.

BOX 3: **Adults with disabilities and the cost of living crisis**

A companion report to this report shows how working-age adults with disabilities are being affected by the cost of living crisis.[15] They went into the current crisis with already very weak living standards, financially vulnerable to fast rising prices of essentials. It shows that people with a disability have been stung by fast-rising energy and food prices. Almost half (48 per cent) of disabled adults say they have had to cut back on energy use this winter, compared to almost one-third (32 per cent) of people without a disability. Around two-fifths of people with a disability (41 per cent) said they could not afford to keep their homes warm, compared to under one-fifth (23 per cent) of the non-disabled population. Almost one-in-three (31 per cent) people with a disability say they have had to reduce their expenditures on food, compared to 18 per cent of the non-disabled population.

It's welcome that the Government is repeating the £150 Disability Cost of Living Payment in 2023 that help millions of people with disabilities in the short term. But much more work will be needed to close the stark living standards gap between disabled people and the rest of the population. This should include support for both those who wish to work, and those who cannot.

Lasting financial consequences of this winter are affecting low-income families the most

Accumulating debts and falling behind on bills are becoming more common

While some of these impacts may be short-lived, rises in the price of essentials are making some families' budgets unsustainable, and debts are starting to accumulate, particularly among low-income households.

In Figure 8, we compare the results from our survey in November 2022 to a similar survey that we commissioned in June 2021. During the pandemic, there were broadly similar numbers of people reporting debt rising as falling (and, on aggregate, savings rose and debt fell in the pandemic)[16]. But it is clear the cost of living crisis is putting more pressure on debts: 11 per cent of respondents say their debts have increased by more than 10 per cent over the past 3 months, compared with 7 per cent of people who reported higher debts over the February 2020 to May 2021 period. It is workers in low-income families

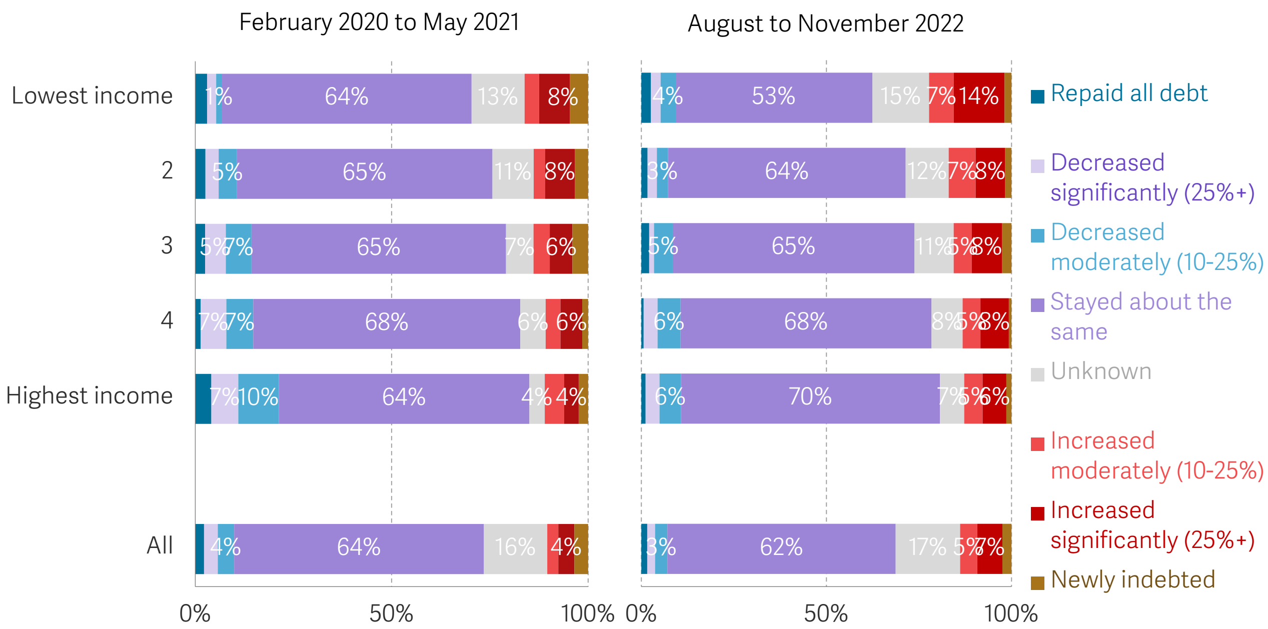
15 O El Dessouky & C McCurdy, Costly differences, The Resolution Foundation, January 2023.
16 J Leslie & K Shah, (Wealth) gap year, The Resolution Foundation, July 2021.

who are most likely to be going into debt, with 20 per cent of those in the bottom quintile saying their debts have increased moderately or significantly over the past three months compared with 12 per cent during the pandemic.

Workers in low-income families who have debts are also more likely than those in higher-income quintiles to feel that their debt is a burden. 71 per cent of workers in the bottom family income quintile with a debt say that this debt is either a heavy burden or somewhat of a burden (and 30 per cent say it is a heavy burden). This is compared to 60 per cent of all adults (of which 18 per cent say it is a heavy burden).

FIGURE 8: **Low-income families' non-housing debt has risen substantially over the past three months**

Percentage of employed respondents reporting changes in amount owed on loans or credit agreement: UK, February 2020 to May 2021 (left) and August to November 2022 (right)



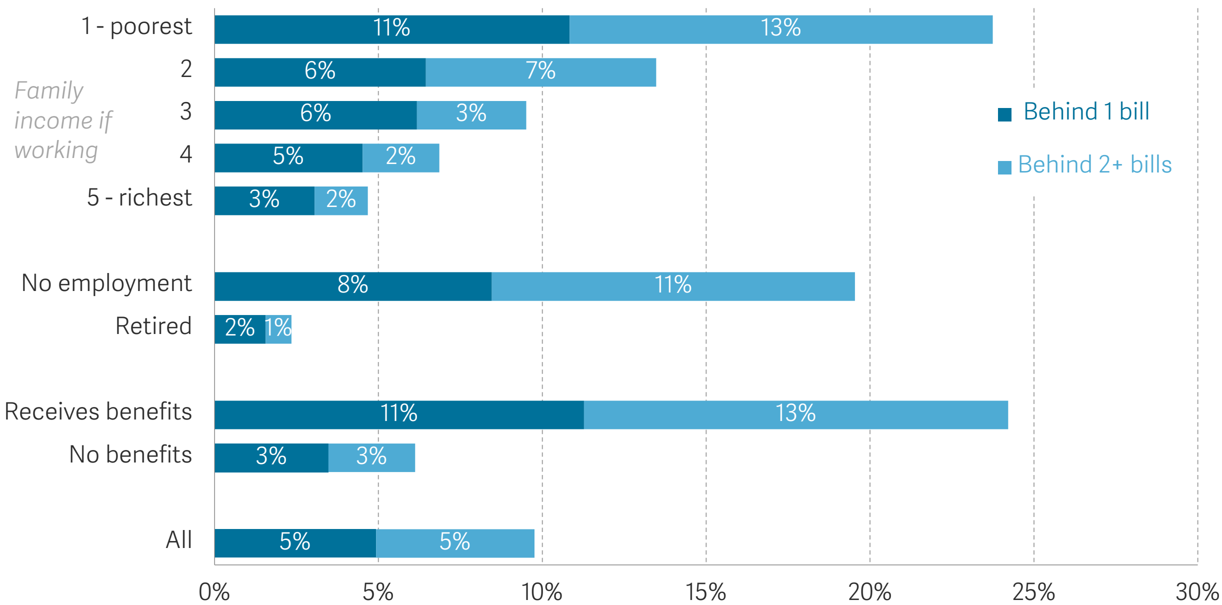
NOTES: Charts shows adults aged 18+. Debt includes non-housing debt. Debts stayed about the same includes those who say that they have stayed the same and those that say their debts have increased or decreased by up to 10%. For the left chart, the base is n=2,680: non-retired aged 18+ with valid income data for March 2020. Quintiles were calculated using mid-points of 20 banded responses from £0 to £5,000. The All bar base is 8,030 and includes the retired and unemployed who are working age. For the right chart the base is (n=4,456) with equivalised family income, lowest income quintile (n=988), q2 (n=740), q3 (n=897), q4 (n=703) and highest income quintile (n=1128). The All bar base is 10,470 and includes the retired and unemployed who are working age. Family income distribution based on equivalised, disposable benefit unit incomes, excluding families containing retired adults or nonworking adult students. These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave (right chart); YouGov, adults age 18+ and the Coronavirus (COVID-19), June 2021 wave (left chart)

In addition, people are increasingly falling behind on 'priority' bills. 10 per cent of respondents (5 million adults) report falling behind on at least one important bill payment over the past three months, including 5 per cent who have fallen behind on two or more payments.[17] Almost a quarter of workers in the bottom income quintile (24 per cent) have fallen behind on at least one bill, and 13 per cent were behind on two or more bills (Figure 9). Before the beginning of 2022, 95 per cent of survey respondents said that they paid their bills always or often in full or on time.

The most common types of bills that people were behind on this winter are council tax payments (with 3.6 per cent of people falling behind). Energy bills are also common to be behind on, with 3.2 per cent behind on their electricity payments and 2.9 per cent behind on gas payments; according to Ofgem, the number behind on electricity bills reached its highest level in Q2 2022 since at least 2006, and has remained above these historic levels in Q3 2022.[18] Finally, 2.2 per cent of people reported being behind on their mortgage or rent payments, comparable to the levels of arrears found in other surveys during the 2022-23 winter period.[19]

FIGURE 9: **10 per cent of people, but a quarter of workers in low-income families, are behind on at least one priority bill payment**

Percentage of respondents reporting missing one or more payments of priority debt: UK, 23-30 November 2022



NOTES: All adults aged 18+. Base is (n=10,470). Receives benefits (n= 2,507) No benefits (n= 7,963). Lowest income quintile (n=988), q2 (n=740), q3 (n=897), q4 (n=703) and highest income quintile (n=1128). No employment (n=1631), Retired (n=2,824). These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave.

17 Priority bills includes: Electricity, Gas, Water, Council Tax, TV Licence, Child maintenance, Income Tax, National Insurance or VAT, any loan other than a mortgage secured against your home, Mortgage or rent, and/or court fines.
18 Ofgem, Number of accounts with a consumer repaying an energy debt: Q1 2006 and Q3 2022.
19 For example, see: M Brignall, Nearly 2m UK households behind on bill payments as Christmas approaches, The Guardian, December 2022.

The most common reasons that people gave for being behind on bills are directly linked to the pressures of the cost of living crisis, with the increased costs of essentials and high energy bills being the main reasons given (40 per cent and 39 per cent of people who had fallen behind respectively). Those who receive benefits are more likely to say that the rising costs of essentials and energy bills is making them fall behind on their bill payments (45 per cent of those on benefits say this, compared to 35 per cent not on benefits), but are less likely to blame increased housing costs (17 per cent of those receiving benefits and behind on bills say this, compared with 22 per cent of those not on benefits).

Some actions taken by families to cope with today's costs are reducing future financial resilience

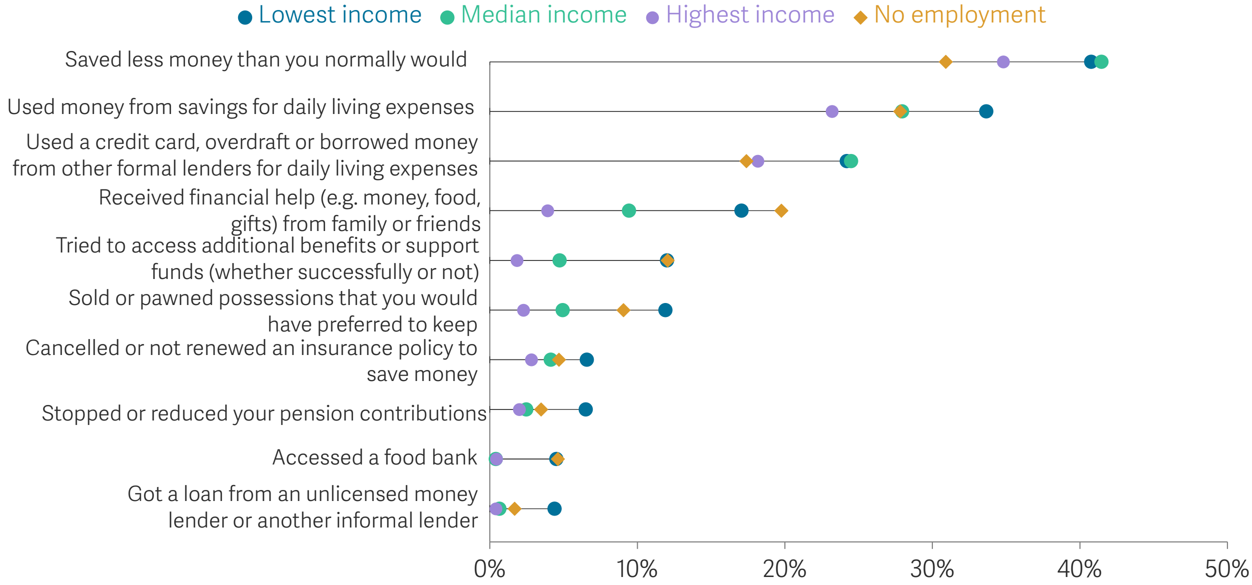
Even for people not taking on more debt, families are taking actions to cope with costs today which will worsen their future financial resilience. As many as 27 per cent of adults (14 million people) report that they are using money from savings for their daily living expenses over the past four weeks. This is more pronounced for workers in lower-income families: 34 per cent of those in the bottom income quintile report using savings for daily living expenses compared with 23 per cent of those in the top income quintile (Figure 10). Overall, these levels have increased by one third since June this year, from 20 per cent of adults.[20]

Another action that people are taking, in order to afford increasing prices, is to cut back on pension savings or paying for insurance, both measures that also reduce future financial resilience. This is particularly pertinent for workers in the bottom income quintile, 7 per cent of whom say that they are cancelling insurance and 7 per cent saying they have reduced pension contributions to save money; 4 per cent and 2 per cent (respectively) of workers in middle-income families are doing the same (Figure 10).

20 J Evans & S Collard, Prices rising, temperatures falling, Financial Fairness Trust, December 2022.

FIGURE 10: **Families are relying on savings where possible to cope with the cost of living crisis**

Percentage of working-age respondents reporting taking actions to cope with rising cost of living over the past four weeks: UK, 23-30 November 2022



NOTES: income is equivalised and in quintiles. Income only shown for those in employment. Lowest income quintile (n=988), middle income (n=897), and highest income quintile (n=1128). No employment (n=1631). These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave.

Alarmingly, workers in the lowest-income families are four times as likely as the highest income families to report that they are selling or pawning possessions (with 12 per cent of the lowest income doing this compared with 2 per cent of the highest income), or getting a loan from an unlicensed money lender to cope with rising costs (with 4 per cent of the lowest income doing this compared with none of the highest income). At the sharp end, food bank use continues to rise with 5 per cent of the lowest income families and those not in employment reporting that they have used a food bank in the past 4 weeks, while those on middle or higher incomes have not done this (Figure 10).

As one way of measuring families' financial resilience, we asked survey respondents a (commonly-used) question about how they would cope with an unexpected expense; we discuss the responses in Box 4.

BOX 4: A family's financial situation as they entered the cost of living crisis, including the level savings, matters more than ever this winter

The options a family has to respond to unexpected income or price shocks varies depending on their financial situation, in particular their level of savings, which clearly provide a buffer when costs rise.[21]

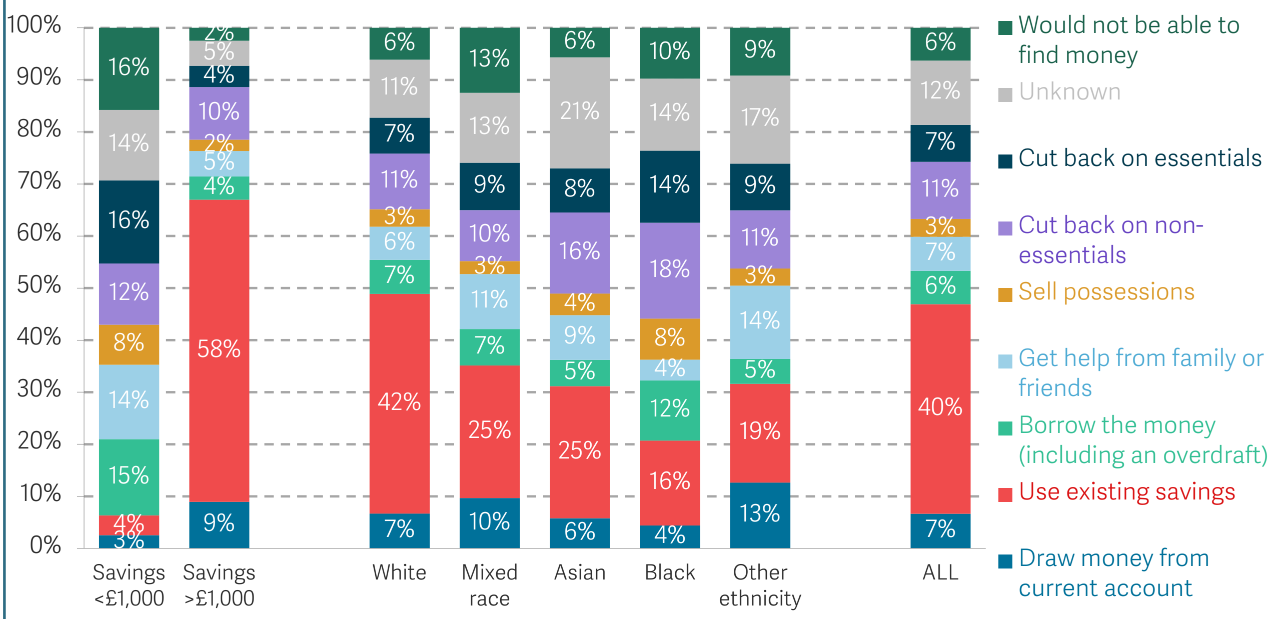
Our survey suggests that as many as 21 per cent of people do not have any savings at all, and 36 per cent of people have savings of less than £1,000 this winter. The levels of savings, and therefore financial resilience, vary substantially by age, income and ethnicity. First, 85 per cent of those who are 65 and above report having savings of £1,000 or more, compared with 60 per cent of those aged 34-44. Second, workers in lower-income families also less likely to have savings, with 24 per cent of workers in the bottom income quintile having no savings at all, and 46 per cent having savings of £1,000 or less. Third, it is well documented that Black and Mixed-race people in the UK have far less household wealth than White and Indian families.[22] In our survey, more than 52 per cent of Black people have savings of less than £1,000, about double that of White people (28 per cent).

And we can see the importance of savings in the responses to a question about how people would deal with an unexpected expense. 58 per cent of those with savings of £1,000 or more are able to use existing savings, compared with just 4 per cent of those with less than £1,000 of savings (Figure 11). Of those with savings less than £1,000, 14 per cent would rely on friends and family for help, and 16 per cent would cut back on essentials. Concerningly, 16 per cent would not be able to find the money at all, forced to rely on a threadbare state. There are very striking differences between ethnic groups. Just 16 per cent of Black people say that they would use existing savings to pay for an unexpected expense; they are more likely to say that they will cut back on non-essentials (18 per cent) and cut back on essentials (14 per cent). This compares to 42 per cent of White people who would use existing savings for an unexpected major expense.

21 M Broome & J Leslie, Arrears Fears, The Resolution Foundation, July 2022.
22 K Shah, Wealth on the eve of a crisis, The Resolution Foundation, January 2022.

FIGURE 11: **Those with savings can rely on them during the cost of living crisis**

Percentage of respondents reporting how they would cope with an unexpected expense, by ethnicity and level of savings: UK, 23-30 November 2022



NOTES: Base is all adults 18+. Respondents could only choose one of these options from a list. All (n=10,470), savings <1k (n=2,369); savings > 1k (n=5,445). White (n= 9,359) Mixed or multiple ethnicities (n= 179) Asian (n= 344) Black (n= 93) Any other ethnicity (n=53). These figures have been analysed independently by the Resolution Foundation.

SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave.

The cost of living crisis is harming mental and physical health

There are not just financial consequences of the cost of living crisis: it is also causing difficulties for people's mental and physical health. Our survey suggests that mental health is getting worse even compared to autumn last year when the UK was only just emerging from ongoing lockdowns, with the percentage of people facing emotional distress increasing from 40 per cent in October 2021 to 47 per cent in November 2022 (Figure 12). This matches evidence from the ONS, which shows that the proportion of adults reporting high levels of anxiety in October to December 2022 was at its highest levels (35.2 per cent) since December to February 2021 (35.7 per cent), at a time when the UK was in lockdown.[23] Similarly, adults reporting low levels of life satisfaction were at their highest levels in October to December 2022 (11.3 per cent) since February to April 2021 (11.4 per cent).

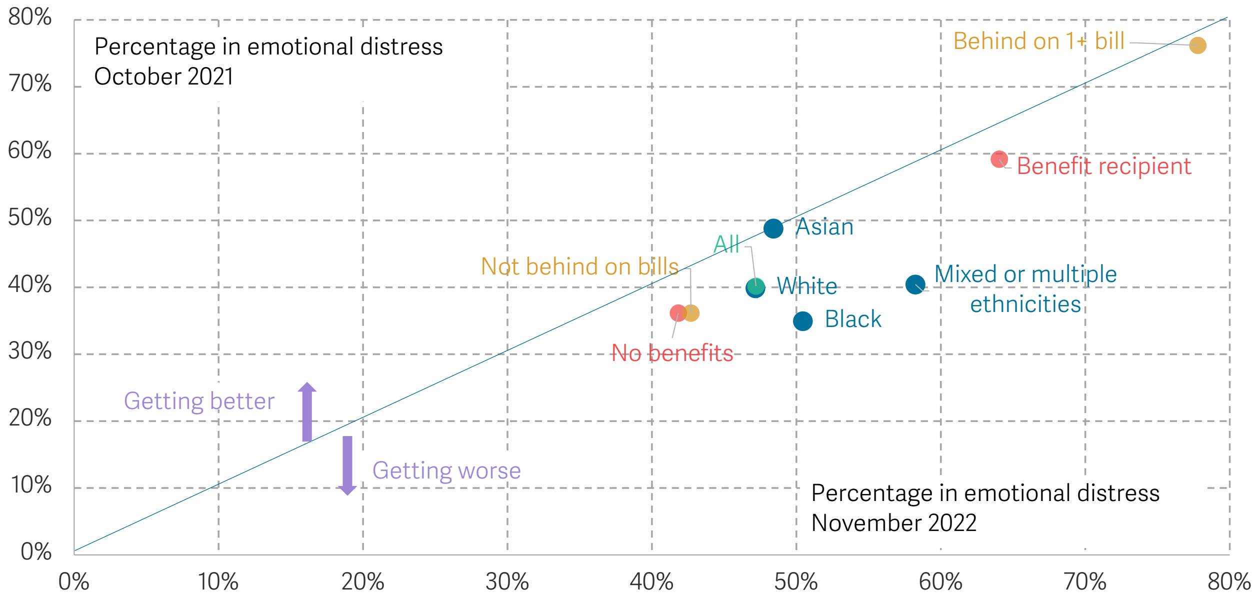
Those with lower financial resilience are also more likely to be experiencing emotional distress. For example, those receiving benefits are increasingly in emotional distress,

23 RF analysis of ONS, Public opinions and social trends, Great Britain: personal well-being and loneliness, December 2022. Figures show a rolling 3-month average, data collected at different intervals, so some periods have more data points than others.

with the fraction now standing at 64 per cent (up from 59 per cent at the same time in 2021), compared to 42 per cent for those who do not receive any benefits. Splits by ethnic groups suggest that the mental health of Black and Mixed-race people is worsening at faster rates than other groups, with emotional distress of Black people rising from 35 per cent to 50 per cent, and that of Mixed-race groups from 40 per cent to 58 per cent between October 2021 and November 2022.

FIGURE 12: **Emotional distress has worsened since the pandemic, on average, but particularly for Black and Mixed-race people**

Percentage of working-age respondents reporting being in emotional distress, by ethnic group, arrears, and benefits status: UK, October 2021 and November 2022



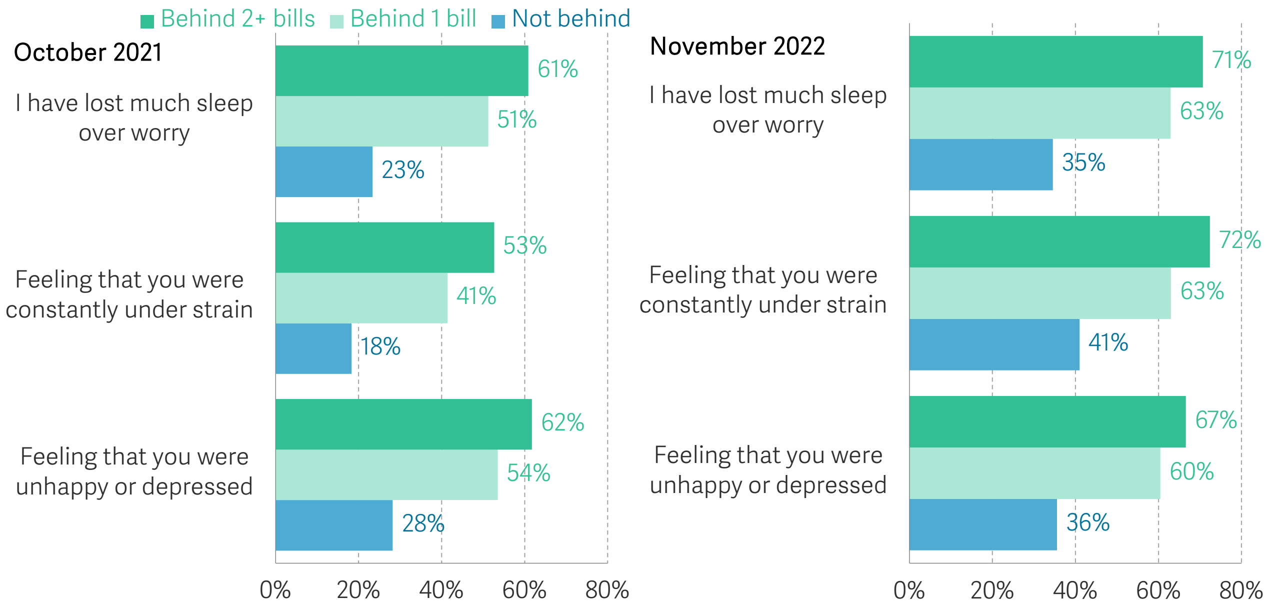
NOTES: Working-age adults shown only to enable comparison between 2021 and 2022 Survey data. The proportion of people in emotional distress is defined as those scoring 4+ on the 12-point General Health Questionnaire. For November 2022: All (n=7,474), White (n= 6,732), Mixed or multiple ethnicities (n= 170), Asian (n= 320), Black (n= 90), Behind on 1+ bill (n =1002), Not behind on any bills (n = 9448). For October 2021: All (n=6,100), White (n= 5,416), Mixed or multiple ethnicities (n= 133), Asian (n= 232), Black (n= 55), Behind on 1+ bill (n =603), Not behind on any bills (n = 5,497), Benefit (n= 5,009), No benefits (n=1,091). These figures have been analysed independently by the Resolution Foundation. The 'Any other ethnicity' category is not shown as working-age sample size < 50 people.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave, and YouGov, adults aged 18-64 Covid-19 October 2021 Wave.

Those who are behind on bills are particularly likely to face emotional distress rising from 76 per cent to 78 per cent from the pandemic to this winter. While 41 per cent of people who are not behind on any bills currently feel that they are constantly under strain, 72 per cent of those who are behind on two or more bills feel this way (Figure 13).[24] The way that these accumulating arrears are treated during the cost of living crisis will be very important to how people's health will evolve.

24 See also: T Clark & A Wenham, Anxiety nation? Economic insecurity and mental distress in 2020s Britain, Joseph Rowntree Foundation, November 2022.

FIGURE 13: **Those behind on bills are susceptible to feeling anxious, unhappy and depressed**

Percentage of respondents feeling the following situations are occurring rather more or much more than usual, by the number of bills the respondent has fallen behind on: UK, October 2021 (left) and November 2022 (right)



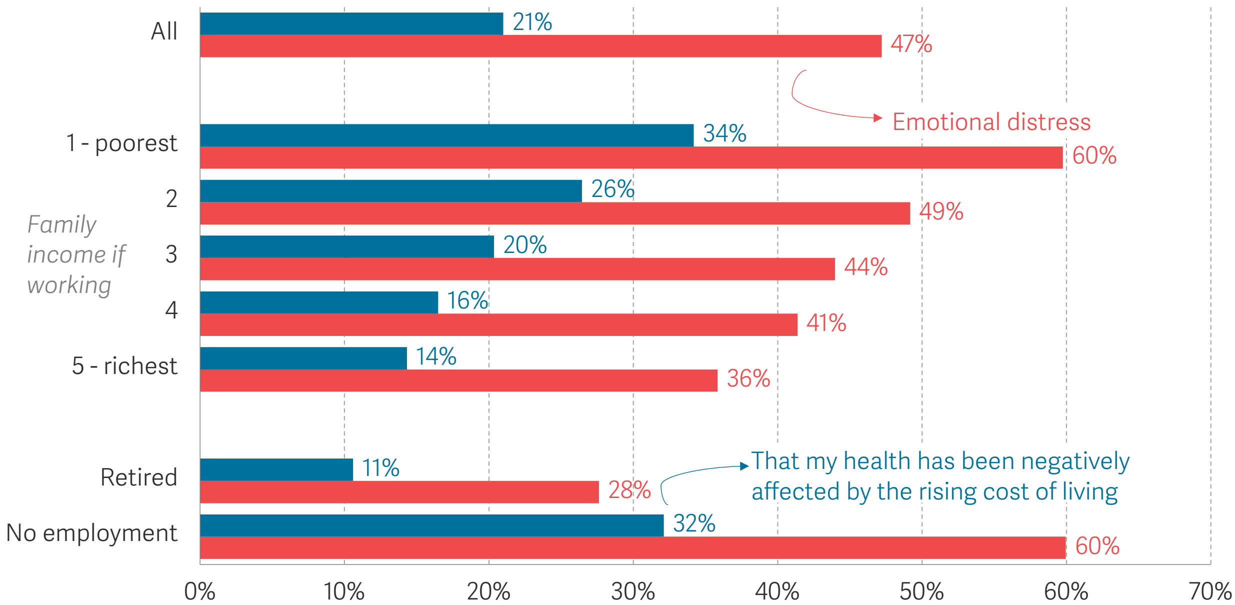
NOTES: Working-age adults only shown. November 2022: Behind on no bills (n=6,767), Behind on 1 bill (n=468), Behind on 2+ bills (n=484). October 2021: Not behind on any bills (n = 5,497), Behind on 1 bill (n=304), Behind on 2+ bills (n=299). These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave, and YouGov, working age adults and the Coronavirus (COVID-19), October 2021 wave.

Confirmation that the cost of living crisis is driving this decline in mental health comes from our finding that 21 per cent of people say that their health has been negatively affected by the rising cost of living, rising to 34 per cent of workers in the bottom income quintile, and 32 per cent of those not in employment. Furthermore, 60 per cent of workers in the bottom income quintile report that they are in emotional distress, almost double the levels of those in the top income quintile. This matches other research that has shown that experiences of material deprivation and food insecurity during the cost of living crisis, as well as increasing debt and arrears, are all associated with worsening mental health.[25]

25 For example, see: SRC Centre for Society and Mental Health, On the edge: What the cost-of-living crisis could mean for UK mental health, King's College London, November 2022; S Williams & K Dienes Cost of living crisis having significant impact on mental health, study shows, Swansea University, October 2022.

FIGURE 14: **The cost of living crisis is harming health, particularly that of low-income families**

Percentage of respondents reporting health consequences of the cost of living crisis: UK, 23-30 November 2022



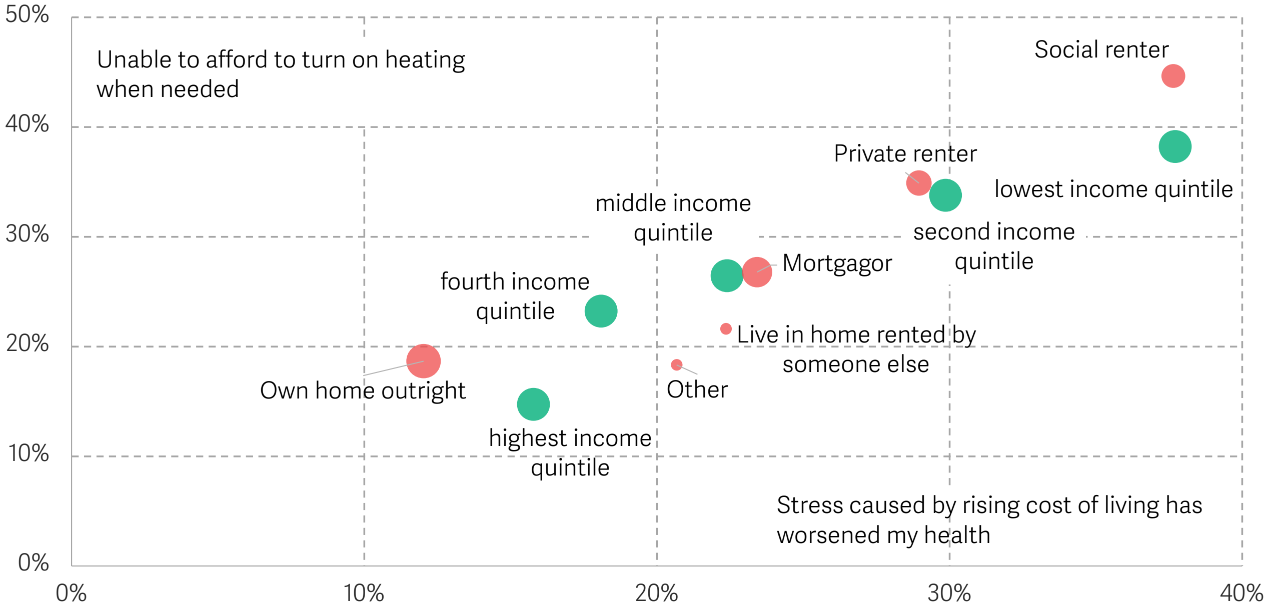
NOTES: The red bars show the proportion of people scoring 4+ on the 12-point General Health Questionnaire, considered to be the respondent showing signs of emotional distress. The blue bars show those responding that a doctor or health professional has confirmed that their health has been negatively affected by the rising cost of living. All (n=10,470), Lowest income quintile (n=988), q2 (n=740), q3 (n=897), q4 (n=703), highest income quintile (n=1,128), No employment (n=1,631), Retired (n=2,824). These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave.

There are also consequences for people's physical health this winter, as people report being unable to afford to turn on their heating even when they need to. Figure 15 shows that workers in the bottom income quintile are far more likely to say that the stress caused by the rising cost of living has made their overall health worse and that they are unable to turn on the heating when needed (38 per cent in both cases).

These effects on physical and mental health also vary by housing tenure. For example, 45 per cent of social renters are unable to turn on the heating when they need to, more than double the rate among those who own their home outright. In addition, 38 per cent of social renters are experiencing stress related to the rising cost of living, three times as high as those who own their home outright.

FIGURE 15: **Those unable to afford to turn on heating are also having negative health outcomes from stress from the rising cost of living**

Proportion of respondents who report that they are unable to afford to turn on heating when needed and that stress caused by the rising cost of living has worsened their health, by income quintile and tenure: UK, 23-30 November 2022



NOTES: Income deciles only show those employed, housing tenure shown for all adults aged 18+. Own home outright (n= 3,624), Mortgagor (n = 3,116), Rent from LA (n= 1,151), Privately rent (n = 1,486), Live in home rented by someone else (n= 881), Other (n = 212), Lowest income quintile (n=988), q2 (n=740), q3 (n=897), q4 (n=703), highest income quintile (n=1128). Bubbles sized by number of households in each category. These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave; DWP, Households Below Average Income, HBAI, 2019-20.

Our findings on physical and mental health are particularly relevant in the context of the current debate about the rise in labour market inactivity since the onset of the Covid-19 pandemic, the majority of which is due to long-term sickness.[26] As mental and physical health continue to suffer during the cost of living crisis, this could have ongoing impacts on labour force inactivity rates. Previous Resolution Foundation work has shown, for example, that having a mental health condition increases young adults' risk of worklessness, both by holding them back from entering work or study and by increasing the odds that they will leave employment.[27]

This Section has shown that while the cost of living crisis is affecting the overwhelming majority of households, it is predominately lower-income families that are making major cut backs, being unable to afford essentials, experiencing food insecurity and hunger, increasing arrears and debts, and suffering poor health. Although the Covid-19 pandemic interacted with pre-existing inequalities in complex ways, the cost of living crisis is more

26 G Thwaites, Low unemployment belies a labour market in poor health, The Resolution Foundation, October 2022.
27 L Murphy, Not working: Exploring changing trends in youth worklessness in the UK, from the 1990s to the Covid-19 pandemic, Resolution Foundation, June 2022.

straightforward, with low-income families more affected than average by higher costs of essentials, and with fewer coping mechanisms. Our results also show that some of the ways that low- and middle-income families have to use to cope will have longer-term consequences for both their financial resilience and their mental health.

The following Section will explore how the cost of living crisis is likely to evolve over 2023, before we look at the implications for incomes and living standards in the coming years.

Section 3

Determinants of household incomes to 2027-28

Section 2 showed that families are already struggling with arrears and debt due to the cost of living crisis, and are seeing their health deteriorate as a result. Although policy makers might hope that 2023 will bring better economic news, household living standards are set to get worse before they get better. Inflation may have peaked in late 2022, but that does not mean that the pain caused by the cost of living crisis will be over soon. Food price inflation will continue to pose a problem for living standards, and the combination of a higher cap on energy prices and the fact that the £400 rebate paid this winter was a one-off means that the energy bill for a typical household in 2023-24 will be 43 per cent higher than in 2022-23. More fundamentally, falling inflation in 2023 does not mean that the level of prices will fall.

Nominal wage growth in 2022 was strong, and hit a 31-year high, but inflation was higher, meaning wages have been falling in real terms. Real wages are expected to keep falling into 2023, with growth in average earnings outstripping growth in prices only from Q3 2023.

The Government has confirmed that benefits will rise in April 2023 in line with last September's inflation rate, delivering a very welcome 10.1 per cent rise, and another round of Cost of Living Payments to those receiving social security benefits or the state pension will help protect incomes towards the bottom of the distribution. But personal tax changes will be holding back income growth: from April, a typical middle-income household will see their personal tax bills rise by around £700 compared to a world where the Government had indexed all thresholds with prices as usual.

Bank rate is currently 3.5 per cent, and current yield curves imply that it will peak in October 2023, at 4.6 per cent. This will turn into living standards pain for the roughly 2 million fixed-rate mortgages that are set to be renewed in 2023-24, as well as at least 1 million floating-rate mortgages that are facing the impact of continued rises in the Bank of England's policy rate.

These factors suggest that the cost of living crisis is definitely not over, and that

2023 will be harder than 2022. This helps explain why almost one-in-five (19 per cent) of people in our survey are not confident about their finances as a whole over the next three months. This rises to 32 per cent among those in work and in the bottom income quintile, and to 43 per cent for those not working and receiving benefits. A fifth (21 per cent) of low-income families expect that their non-housing debt will increase by more than 10 per cent over the next three months.

If policy makers want some good news, then they may need to wait for 2024. By then, projected falls in international gas prices may mean that the cost of living may fall slightly in 2024 or 2025, with the OBR predicting negative inflation in those years. Wage growth should return to normal by 2024, although average real earnings will grow a lot more slowly than they shrank: real wages won't reach their Q1 2022 rate until the end of 2027 – nearly six years later. On top of this, the labour market will weaken in the short term, with unemployment forecast to rise until late 2024, peaking at 4.9 per cent.

The fall in the rate of inflation will create a rollercoaster for the real value of benefits (and, to a lesser extent, social rents). Under the usual rules for their annual uprating, benefits are due to rise in April 2024 by the rate of inflation in September 2023, which is forecast to be 6.9 per cent. Given that inflation in 2024-25 is set to be close to zero, this will deliver a large real-terms increase in the value of benefits. But this rise is needed to undo the real-terms cut that happened in the 2021-2022 period of rising inflation, and simply returns the real value of benefits to their pre-pandemic levels.

The period of higher interest rates is good news for savers: the Office for Budget Responsibility projects that aggregate income from savings will rise by £20bn between 2021-22 and 2023-24, taking interest receipts as a proportion of income from around 1 per cent in 2021 to 6 per cent in 2024. This boost to household incomes will, though, be heavily skewed towards the top of the distribution, as high-income households are much more likely to have money in savings or other financial investments.

Our survey results show that, even before the coldest months of the winter, some families were struggling with arrears, debt and seeing their health deteriorate as a result. In this Section, we look at the key economic factors affecting living standards over the next five years. This look-ahead can be split into three periods:

- another year of incomes falling, as cost of living increases outpace earnings growth;
- a period of very low or even negative inflation; and,
- a return to more normal circumstances from 2024.

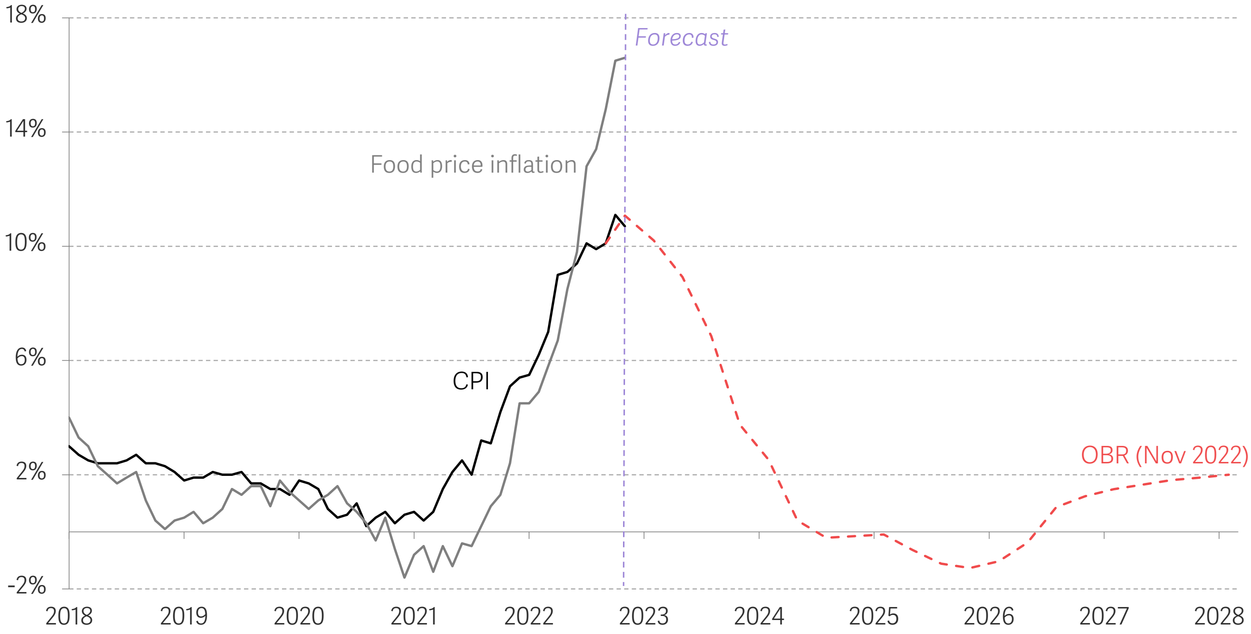
A relatively novel phenomenon affecting household finances will be high interest rates: this will boost income for savers, but put up housing costs for mortgagors. We set all these out below.

Inflation is set to fall rapidly in 2023, and may turn negative in 2025 and 2026

As we discussed in Section 1, the overwhelming factor responsible for the grim outlook for household incomes at present is inflation. As shown in Figure 16, CPI inflation was 10.7 per cent in November 2022, the latest data available at the time of writing. It is possible that inflation has already peaked – inflation the month before was 11.1 per cent, the highest rate in 40 years – and the OBR forecasts that inflation will fall through 2023 and the first half of 2024. (Indeed, the OBR projects that the UK will then experience eight successive quarters of (technical) deflation, from Q3 2024 to Q2 2026; we discuss what this might mean for benefit and social rent uprating later.) But where inflation ends up will depend to a large extent, as it does now, on international energy prices, and so any forecast will be especially uncertain; the key point is that it seems likely that, from 2024, we can expect rates to be much closer to the Bank's 2 per cent target than we have seen since 2020.

FIGURE 16: **Inflation will fall quickly in 2023, and may turn negative in 2025 and 2026**

Annual CPI inflation: UK



SOURCE: OBR, Economic and Fiscal Outlook, November 2022; ONS, Consumer Price Inflation.

However, the pain caused by high inflation will not be over soon. Price levels will be persistently higher (even the deflation forecast by the OBR between 2024 and 2026 would bring prices down by only 2 per cent) and these persistently higher prices will likely continue to weigh on household budgets. Furthermore, food price inflation will continue to pose a problem for living standards: the latest data shows food price inflation at 16.6 per cent, the highest level on record.

But changes to the Energy Price Guarantee mean that energy bills will rise in April 2023, and are set to be 43 per cent higher in winter 2023 than now

Although inflation may fall in 2023-24, energy prices are still rising rapidly. Figure 17 shows the monthly energy bill cost for a typical household between April 2022 and March 2024, for households on both pre-payment meters and direct debits. The combination of the £400 energy bill rebate and the £2,500 Energy Price Guarantee (EPG) this winter prevented direct debit customers' bills from rising much in October 2022 compared to their Summer 2022 rate.[28] Despite this, average energy bills this winter will still be the highest rate they have ever been, at £175 per month for direct debit customers.

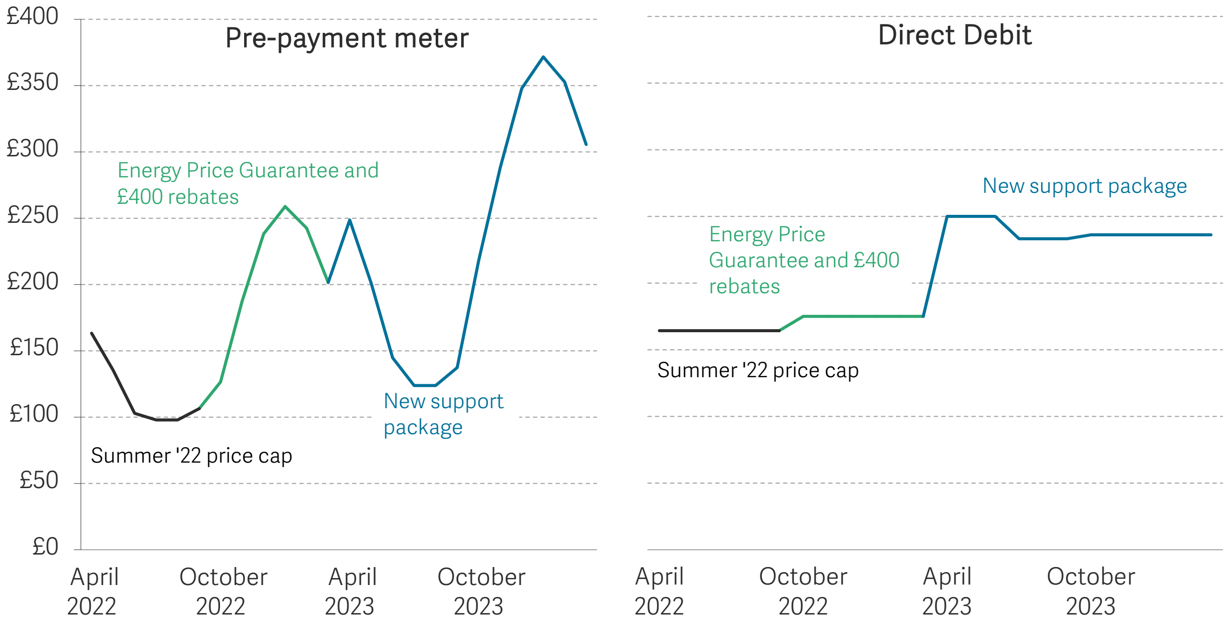
But they are set to rise further, mostly because of a reduction in government support: a higher price cap under the Energy Price Guarantee of £3,000 for the typical household will be implemented from April 2023 to March 2024.

However, given the recent falls in wholesale gas prices across Europe, forecasts published just as we were finalising this report suggest that the EPG would in fact only bite for the first three months of 2023-24, and a typical bill in 2023-24 would be £2,850.[29] But even with these falls, the combination of a higher cap and the fact that the £400 rebate is not being repeated means that an energy bill for a typical household in 2023-24 will be 43 per cent higher than in 2022-23. Pre-payment meter customers are particularly exposed to higher monthly energy costs, though, and are forecast to be in line to pay £370 in January 2024 alone under this new support package.

28 For more analysis of the effect of the 2022-23 EPG, see: A Corlett et al., A blank cheque: an analysis of the new cap on energy prices, Resolution Foundation, September 2022.
29 RF analysis of Ofgem price cap methodology, Government Energy Price Guarantee, Cornwall Insight, UCL SERL data.

FIGURE 17: **The less generous Energy Price Guarantee means energy bills in 2023-24 will be around 40 per cent higher than in 2022-23**

Historical and forecast monthly energy bills for a typical household paying via a pre-payment meter (left-hand panel) and direct debit (right-hand panel): GB, April 2022-March 2024



NOTES: Figures net of £400 Energy Bills Support Scheme rebates but no other cost of living payments such as those delivered through the benefits or council tax system. Costs are based on January 2023 forecasts for Cornwall Insight resulting in a typical energy bill of £2,850 in 2023-24, below the £3,000 EPG.
SOURCE: RF analysis of Ofgem price cap methodology, Government Energy Price Guarantee, Cornwall Insight, UCL SERL data.

As well as the reduction in energy bills the EPG will provide in 2023-24 (the effects of which are shown in Figure 17), the Government has committed to providing further support to help with high energy bills through Cost of Living Payments (worth £900 to those on means-tested benefits, £300 to pensioners and £150 to those on disability benefits).[30] In earlier analysis, we showed that energy support next year will be lower, but more progressive, than this year's (although the very recent reduction in the forecasts for energy prices next year would mean that the EPG provides even less support in 2023-24 than we forecasted at the time of the Autumn Statement).[31]

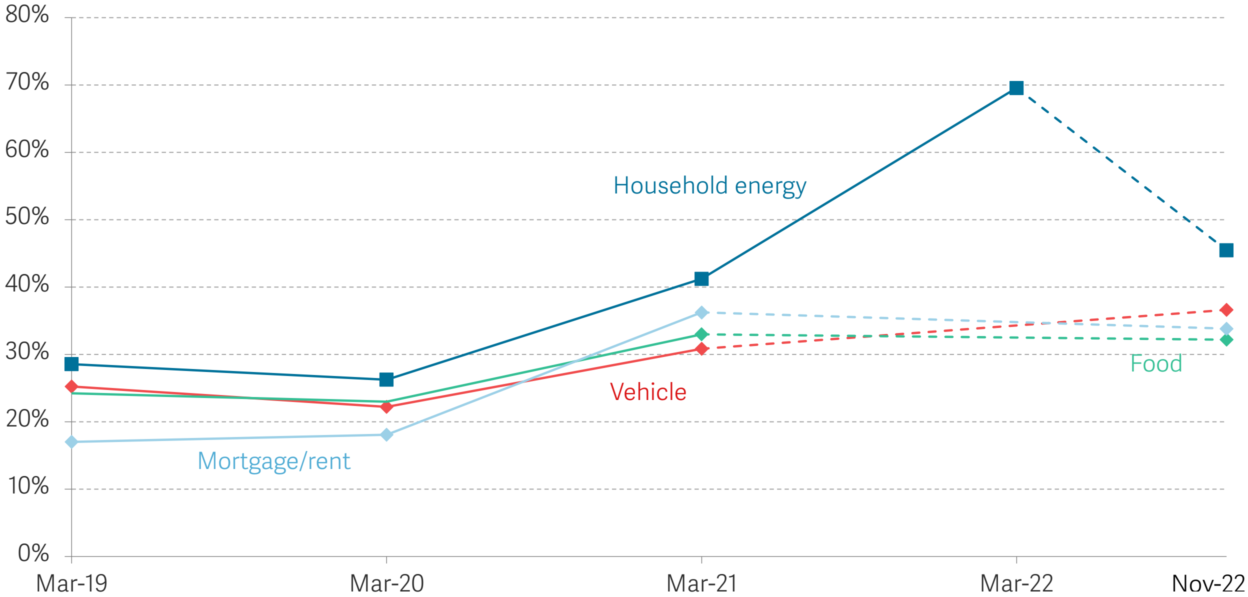
The significant policy interventions announced since May 2022 may help explain why worry about paying energy bills over the winter months has fallen from 70 per cent of people in March 2022 to 47 per cent of people in November 2022 (Figure 18), although it remains well above pre-pandemic levels. For other essentials such as mortgages and rent, food and vehicles, worry about the ability to pay for these over the winter months

30 For analysis of the 2022-23 Cost of Living Payments, see: T Bell et al., Back on target: Analysis of the Government's additional cost of living support, Resolution Foundation, May 2022.
31 T Bell et al., Help today, squeeze tomorrow: Putting the Autumn Statement 2022 in context, Resolution Foundation, November 2022.

remains as high as it was during the pandemic, with worry about paying for vehicles rising in the rankings, likely reflecting high fuel prices in November. Worry about the ability to pay mortgage and rent has doubled compared to pre-pandemic levels, from 17 per cent in March 2019 to 34 per cent in November 2022 (Figure 18).

FIGURE 18: **Worry about paying energy bills is higher than during the pandemic, but policy certainty means this has fallen from earlier this year**

Percentage of respondents reporting they are worried about paying for certain bills over the winter months: UK



NOTES: Values before November 2022 are from the BEIS Public Attitudes tracker which asked how worried the respondent had been about paying these costs over the winter that had just ended. Values for November 2022 are derived from a question about how worried the respondent is about ability to pay over the forthcoming winter period. Base of n=10,470. Unknown responses have been excluded. These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave, BEIS Public Attitudes Tracker.

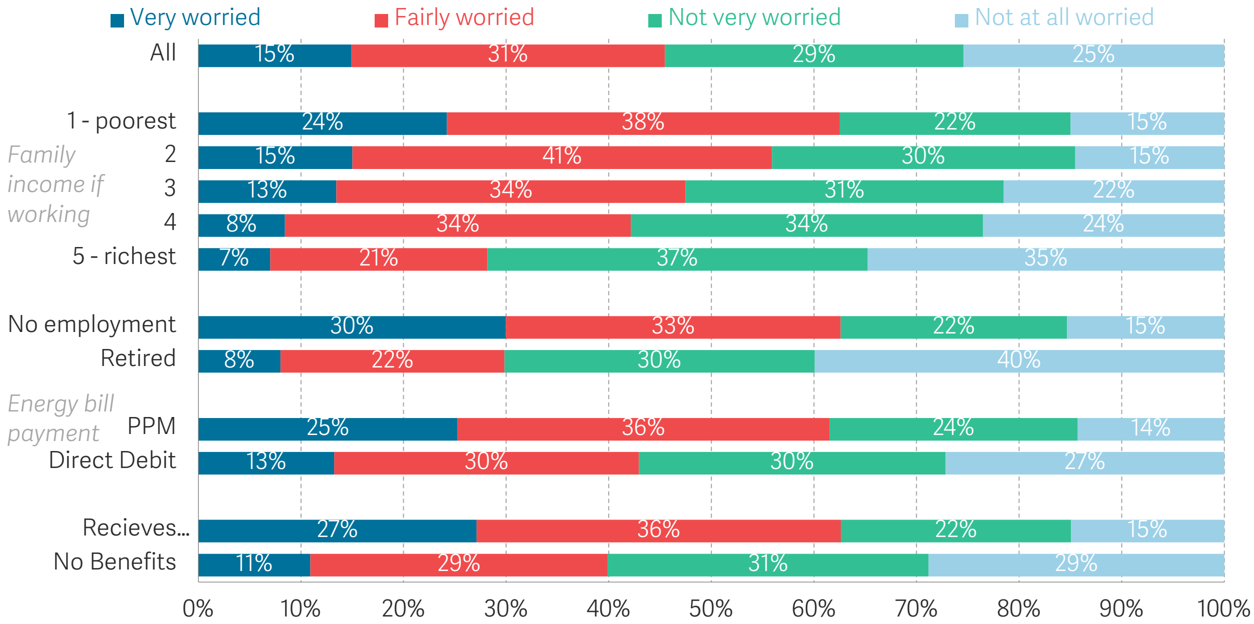
However, there remains considerable variation between different types of households in their confidence in coping with future bills. Lower-income families are more worried than average about their ability to afford their energy bills, with 63 per cent of workers in the bottom quintile saying that they are very or quite worried about paying their bills this winter, compared to 28 per cent of those in the top quintile (Figure 19). Larger families are also more likely to be worried about their energy bills, with 63 per cent of families with three or more children saying that they are worried about their bills this winter, compared with 42 per cent of families without children.

There are also important differences between those with and without a pre-payment meter (PPM). A typical household with a PPM will face costs of £250 this January alone to keep their heating and lights on. Reflecting these sharp increases in costs during the coldest months of the year, 62 per cent of those paying their energy bills using a PPM are worried about paying their energy bills over the winter, compared with 43 per cent of people who pay their energy bills by direct debit (Figure 19). People using a PPM are also more likely to be benefit recipients: 26 per cent of benefit recipients use a PPM for their gas and/or electricity bills, compared with 10 per cent of people who do not receive benefits.

These high levels of worry might be due to a perceived lack of support from key institutions during the cost of living crisis. Research has found that people feel that they are receiving less support during the cost of living crisis than during the pandemic. This is true both of general support and of support from lenders, by landlords, and for household bill providers.[32]

FIGURE 19: **Lower-income families, those using PPMs and those receiving benefits are worried about paying their energy bills**

Percentage of respondents reporting they are worried about energy bills over the winter months: UK, 23-30 November 2022



NOTES: Income is equivalised and bracketed using uprated HBAI data from 2019-20. All (n=10,470), Lowest income quintile (n=988), q2 (n=740), q3 (n=897), q4 (n=703), highest income quintile (n=1128), No employment (n=1631), Retired (n=2,824), PPM (n=1366), Direct Debit (n=7540), Receives benefits (n=2,507), No benefits (n=7,963). Unknown responses have been excluded. These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave.

32 J Evans & S Collard, Prices rising, temperatures falling, Financial Fairness Trust, December 2022.

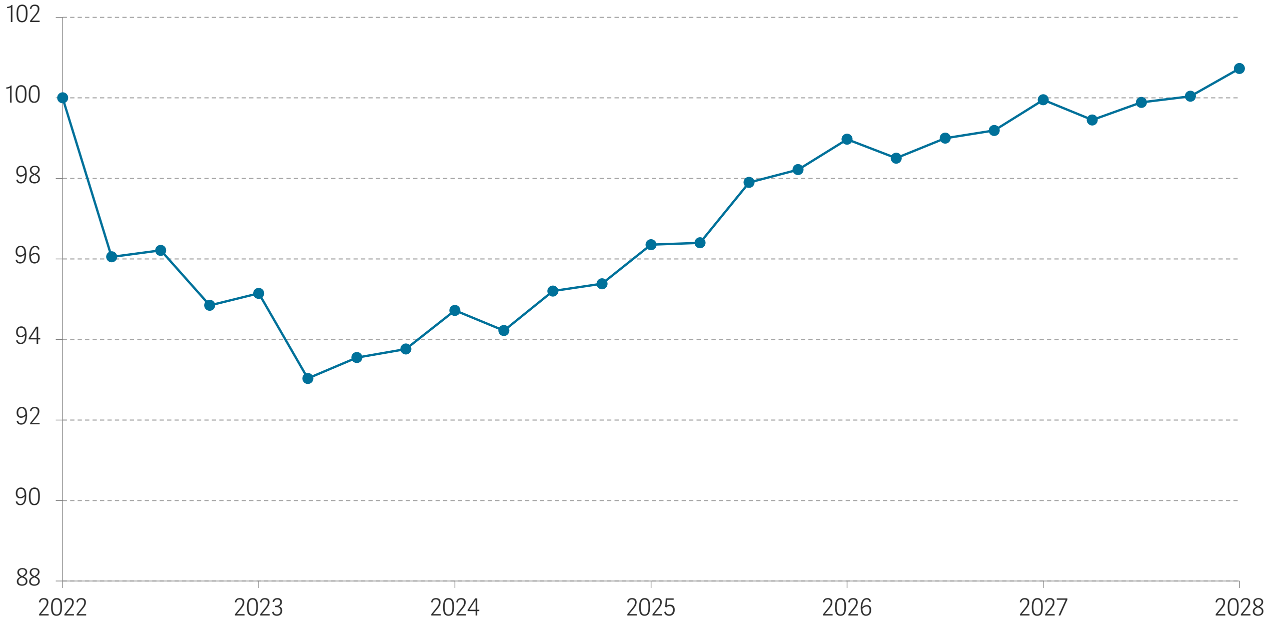
Wages will continue to grow strongly in nominal terms, but won't outpace the rising cost of living until the second half of 2023

As mentioned in Section 1, nominal wage growth is currently at a 31-year high, but inflation is higher, meaning wages are currently falling in real terms. Real wages are expected to keep falling into 2023, with growth in average earnings outstripping growth in the price level only from Q3 2023 (see Figure 20). From that low point, average real earnings are expected to rise a lot more slowly than they fell: indeed, real wages won't reach their Q1 2022 rate until the end of 2027, nearly six years later. This follows a long period of poor wage growth: wages are at present approximately at the same level they were pre-financial crisis.[33]

What isn't shown in the OBR's headline wage rate forecasts in Figure 20 is the gulf between public and private sector pay rises. This has come under increased scrutiny in recent weeks and months, due to a rise in strikes by public sector workers (private sector wages have risen by higher rates than public sector wages for much of the 2010s).[34] Indeed, since February 2020, public sector pay has only grown by 3.8 per cent, compared to 5.2 per cent pay growth in the private sector.[35]

FIGURE 20: **Real wages are not set to reach the level they were at the start of the cost of living crisis until the end of 2027**

Index of average earnings in real terms (Q1 2022=100): UK



SOURCE: OBR, Economic and Fiscal Outlook November 2022.

33 Resolution Foundation & Centre for Economic Performance, LSE, Stagnation nation: Navigating a route to a fairer and more prosperous Britain, Resolution Foundation, July 2022.
34 T Bell, Strikes are an inevitability not an aberration, Financial Times, December 2022.
35 L Murphy, Understanding the labour market context behind the current strikes, Resolution Foundation, December 2022.

In addition to wages falling, the labour market is expected to cool in another way, in the form of unemployment, which is set to rise.

The UK's labour market emerged from the Covid-19 pandemic with low unemployment (just 3.5 per cent in August 2022, the lowest since 1973), and a record low of just 0.9 unemployed people per vacancy.[36] Since then, the labour market has shown some signs of cooling: the latest data has unemployment at 3.7 per cent and there was one unemployed person for every vacancy in October 2022. This turn in the labour market is likely to be due to the cost of living crisis affecting consumer spending and employers' profit margins.

The OBR forecasts that unemployment will peak at 4.9 per cent in Q3 of 2024, after which it will fall gradually to 4.1 per cent at the end of the forecast period.[37] This is more optimistic than the Bank of England forecasts from November, which show unemployment rising to 6.4 per cent in Q4 of 2025.[38] (We use the figures from the OBR in our projections in Section 4).

A potentially more significant labour market development since the end of the pandemic has been the decline in labour market participation. In September 2022, this stood at 62.9 per cent, its lowest level since 2002. Since then, it has risen slightly to 63.0 per cent, which is where the OBR thinks it will remain for the next few years. The Bank of England's forecast looks different, with participation falling to 62.5 per cent in 2024, and rising to 62.75 per cent in 2025.[39]

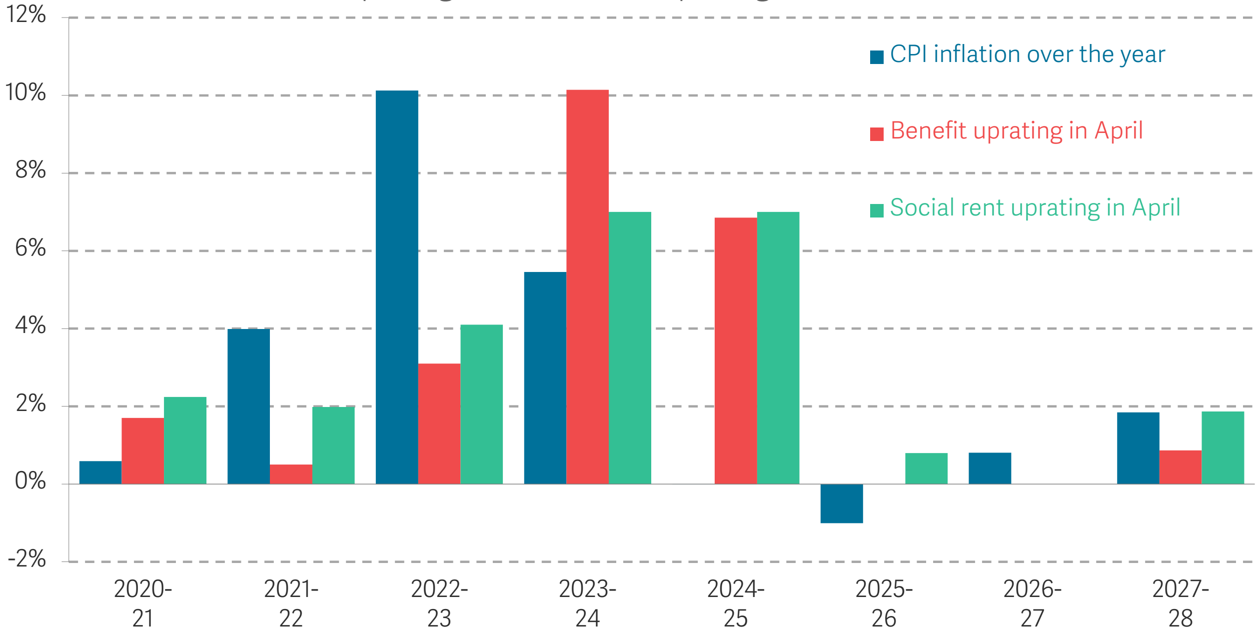
The imminent abrupt fall in the rate of inflation will create a rollercoaster for the real value of benefits and social rents

Typically, benefits and social rents rise every April in line with the previous September's CPI inflation rate. During times when inflation is steady and sitting close to the Bank of England's 2 per cent target, this rule ensures that benefits preserve their real-terms value, as inflation in April (and over the financial year as a whole) is similar to that in the previous September. However, rapidly rising inflation has disrupted this arrangement: as Figure 21 shows, benefits rose by 3.1 per cent in April 2022, but the OBR expects inflation to average 10.1 per cent in 2022-23. When inflation is rising, using inflation rates that are seven months out of date means benefits fall behind in real terms (as can be seen in Figure 23).

36 ONS, Labour Market Statistics, December 2022.
37 OBR, Economic and Fiscal Outlook, November 2022.
38 Bank of England, Monetary Policy Report, November 2022.
39 Bank of England participation figures are rounded to the nearest 0.25 percentage points.

FIGURE 21: **High inflation followed by deflation means fluctuating levels of benefit and social rent uprating**

CPI inflation, benefit uprating and social rent uprating: UK



NOTES: 0 per cent benefit uprating assumed in 2025-26 and 2026-27, due to projected inflation in Q3 2024 and Q3 2025 being negative. Social rent uprating settlement of CPI plus 1 per cent applies to England only; other countries having their own settlements. The social rent uprating settlement in England lasts until April 2025; we have assumed that it continues beyond the whole forecast period. 0 per cent social uprating assumed in 2026 due to projected Q3 2025 inflation being under -1 per cent. 0 per cent social uprating assumed in 2026 due to projected Q3 2025 inflation being under -1 per cent.
SOURCE: ONS, CPI; OBR, Economic and Fiscal Outlook November 2022.

Sensibly, the Government committed in the Autumn Statement to uprate benefits in April 2023 by the usual value of CPI inflation in September (10.1 per cent), despite suggestions over the summer that they were considering an uprating using earnings (5.5 per cent) instead.[40] Indeed, the Chancellor also announced that the 10.1 per cent rise in April 2023 would apply to some parts of the benefit system that are not normally indexed to price inflation – these being the benefit cap and Pension Credit, which are discussed in Box 5.

BOX 5: **Benefit cap and Pension Credit uprating in April 2023**

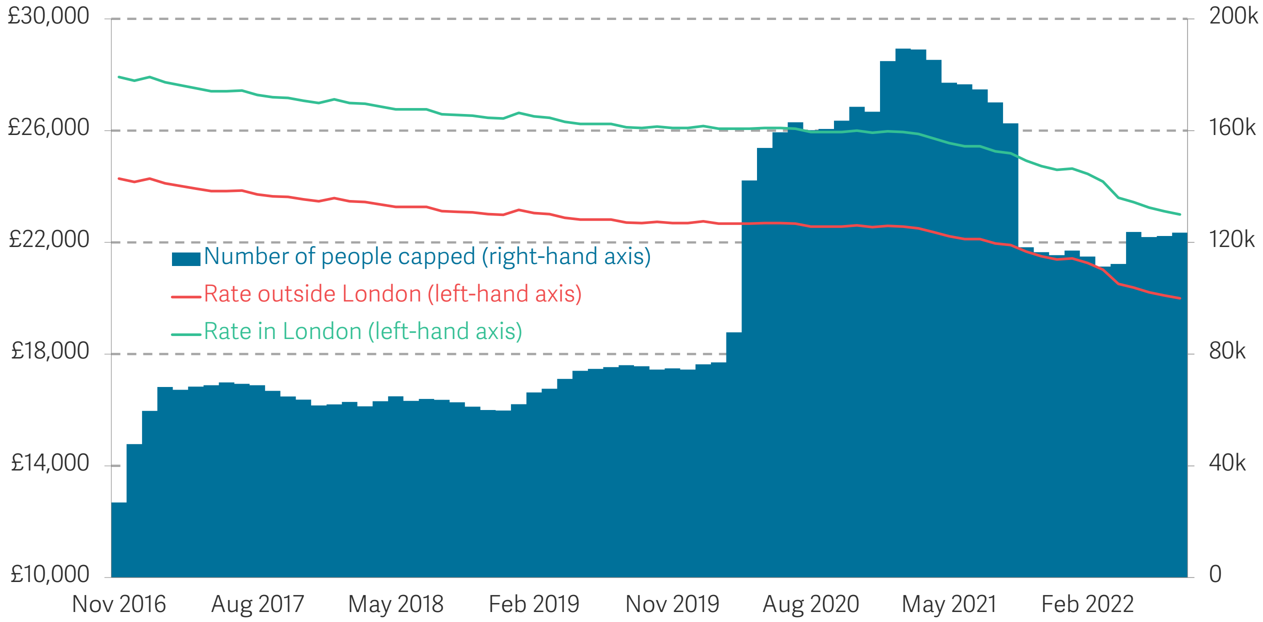
Introduced in 2013, the benefit cap limits the total amount of income from benefits that a family can receive. At its introduction, the benefit cap was £26,000, but it was reduced in November 2016 to £23,000 in London and £20,000 elsewhere.[41] Since then, the cap has been frozen in nominal

40 A Corlett & L Try, The Long Squeeze: Benefit uprating policy for April 2023, Resolution Foundation, October 2022.
41 House of Commons Library, Benefit Cap, 24 June 2020.

terms, meaning that the cap has been falling in real terms. As Figure 22 shows, the value of the benefit cap has fallen by a significant 17.6 per cent in real terms since November 2016. Because of this, increasing numbers of households have become subject to the benefit cap, with 123,500 households being capped in August 2022 (the most recent data), compared to 26,900 in Nov 2016.[42] (The number of people being capped has fallen since its February 2021 high of 189,300, due to the withdrawal of the £20 a week Universal Credit uplift, which pushed more claimants into being capped.)

FIGURE 22: **The longer the benefit cap has been frozen in real terms, the more people have become subject to it**

Level of benefit cap in August 2022 prices, and number of people on Universal Credit or Housing Benefit being capped: GB



NOTES: Benefit cap level is for a couple or lone parent.
SOURCE: DWP, Stat-Xplore; ONS, CPI.

In the Autumn Statement, the Chancellor announced that the benefit cap will be uprated by CPI in April 2023, bringing it to £25,323 in London and £22,020 outside of London.[43] This is a welcome commitment, especially given that the high uprating of the other parts of the benefit system in April 2023 would otherwise have brought thousands more over the threshold for being capped.

In addition to the benefit cap uprating, the Chancellor also committed to uprating the Pension Credit Standard

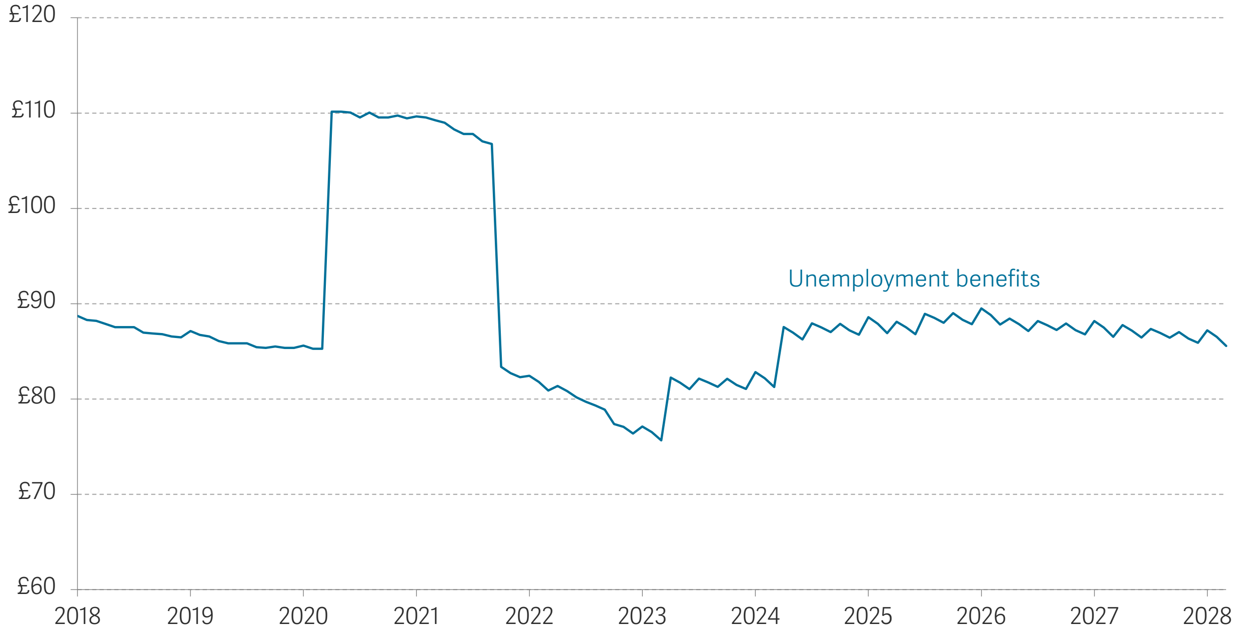
42 The mean amount lost because of the cap is £51 a week. DWP, Benefit cap: number of households capped to August 2022, 13 December 2022.
43 HM Treasury, Autumn Statement 2022 Policy Costings, November 2022.

Minimum Guarantee in April 2023 by the previous September's CPI inflation, bringing the single rate to £201.05 and the couple rate to £306.85; these rates are normally indexed in line with growth in average earnings, which in 2022 was considerably lower.[44]

In April 2024, benefits are due to be increased by the rate of inflation in September 2023, which is forecast by the OBR to be 6.9 per cent. However, inflation in 2024-25 is very likely to be less than that (and the OBR forecasts it will be 0 per cent). But this large real-terms increase in the value of benefits is needed to undo the real-terms cut that happened in the period of rising inflation. As Figure 23 shows, the 6.9 per cent rise in benefits in April 2024 will merely return the real value of benefits to the level they were in March 2020, before the start of the pandemic.

FIGURE 23: **Uprating benefits by inflation in 2023 and 2024 brings them back to pre-pandemic levels**

Value of selected benefits in real terms (November 2022 prices): UK



NOTES: Unemployment benefit is assumed to be frozen in nominal terms in 2025 and 2026 instead of uprated, as Q3 2024 and 2025 inflation projections are negative.
SOURCE: RF analysis of DWP, Abstract of Benefit Statistics; ONS, Average Weekly Earnings; OBR, Economic and Fiscal Outlook November 2022.

In our modelling, we have assumed that benefits will be frozen in April 2025 and April 2026, given that the OBR's projections for inflation in Q3 of 2024 and 2025 are both negative. If the OBR's forecasts are correct – and these forecasts will be much more

44 Department for Work and Pensions, Benefit and pension rates 2023 to 2024, November 2022.

uncertain than in normal times, given the continuing close link between the cost of living and the international price of gas – then this would deliver a real-terms boost to benefit levels (0.2 per cent between 2024-25 and 2026-27). However, the OBR's forecasts differ from the Bank of England's, which show inflation reaching around 1 per cent in 2024-25, and falling to 0 per cent in Q4 2025.[45]

Personal tax changes will bear down on incomes

In the 2022 Autumn Statement, the Government doubled down on using threshold freezes and fiscal drag – continuing a strategy begun in the Spring 2021 Budget – as a way to increase tax revenues.[46] Figure 24 shows the distributional impact of those personal tax changes coming into effect in April 2023, compared to the business-as-usual baseline where tax thresholds are indexed with inflation. On average, these changes will increase tax payments of the typical household by £700. The overwhelming majority of this is driven by the decision to freeze almost every threshold in our tax system at a time of high inflation. Indeed, Chancellor Sunak and Hunt's decisions to freeze thresholds have increased personal tax bills from April 2023 by almost £1,000 for a middle-income household, rising to £1,500 by 2027-28.[47]

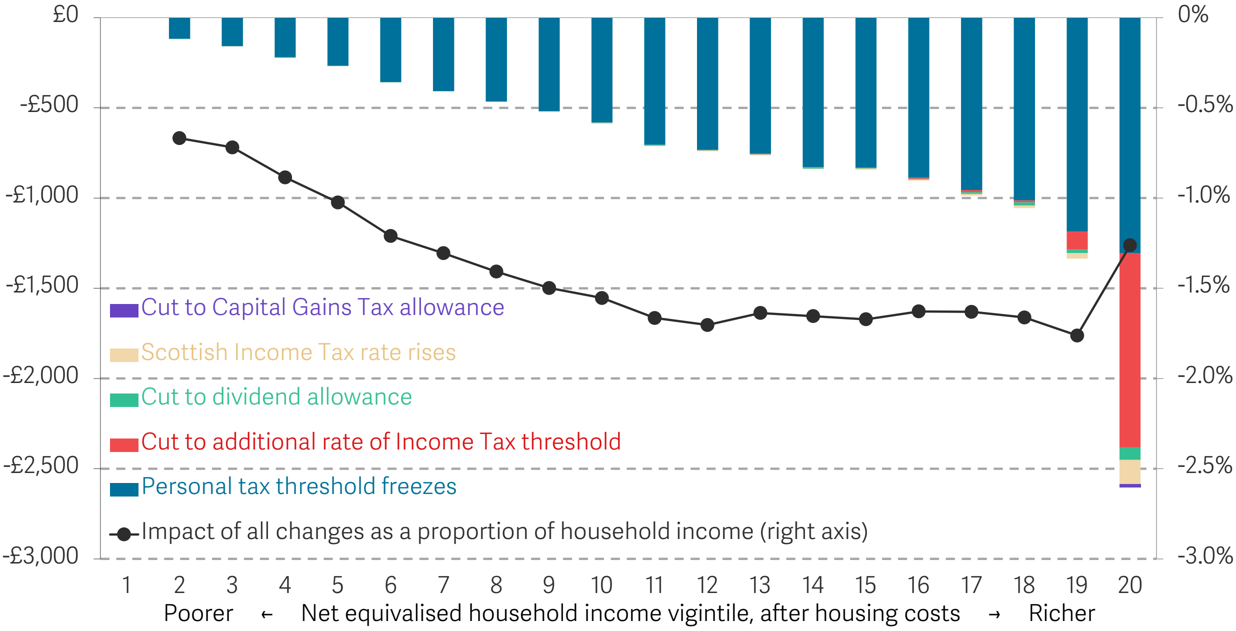
The losses vary enormously with income, with the biggest impact in cash terms being among the richest households, who are also affected by the reduction of the threshold of the additional rate of Income Tax, and reductions in the dividend tax threshold and the Capital Gains Tax threshold. However, when looking at losses as a proportion of household income, it is middle-income households that suffer the most: households in the middle-income quintile will see their incomes fall by 1.6 per cent as a result of tax rises, whereas the top 5 per cent will only see their incomes fall by 1.3 per cent.

The Autumn Statement confirmed that many tax thresholds will be frozen through to 2027, but the impact of future freezes to tax thresholds will be small or non-existent when inflation is due to be very low, or even turn negative. If we consider all personal tax changes introduced so far this Parliament coming in until 2027-28, middle-income households will remain harder-hit than higher-income households (when considered as a fraction of income), with the middle quintile of households facing income falls of 3.7 per cent in 2027-28 compared to 2.8 per cent for the top 5 per cent.[48]

45 Bank of England, Monetary Policy Report, November 2022.
46 T Bell et al., Help today, squeeze tomorrow: putting the Autumn Statement 2022 in context, Resolution Foundation, November 2022.
47 The 2027-28 fact comes from Figure 32 of T Bell et al., Help today, squeeze tomorrow: putting the Autumn Statement 2022 in context, Resolution Foundation, November 2022.
48 For more information on the effect of tax and benefit policy on household incomes in 2027-28, see T Bell et al., Help today, squeeze tomorrow: putting the Autumn Statement 2022 in context, Resolution Foundation, November 2022.

FIGURE 24: **Tax rises coming into effect in April 2023 mean a £700 hit to a typical household**

Average impact of tax changes taking effect in April 2023 by income vigintile, in 2023-24 prices: UK



NOTES: Capital Gains Tax change reduces the annual exempt amount from £12,300 to £6,000 from 2023-24, then to £3,000 in 2024-25. We assume Capital Gains Tax changes affect the top vigintile only. Dividend allowance change reduces the threshold from £2,000 to £1,000 in 2023-24, and £500 in 2024-25. Additional rate of Income Tax threshold reduced from £150,000 to £125,140 in 2023-24. Personal Tax Threshold Freeze refers to Income Tax and National Insurance thresholds freeze (excluding employer NI). Scottish Income Tax rates are rising by 1p for higher and additional rate payers. We do not include changes in Council Tax.
SOURCE: RF analysis of DWP, Family Resources Survey using IPPR tax-benefit model; DWP, Households Below Average Income.

High and rising interest rates will increase unearned income, especially at the top of the income distribution

Rising interest rates will have a significant direct effect on incomes after housing costs in two ways: they will increase unearned income, but also increase mortgage payments. We consider these separately below.

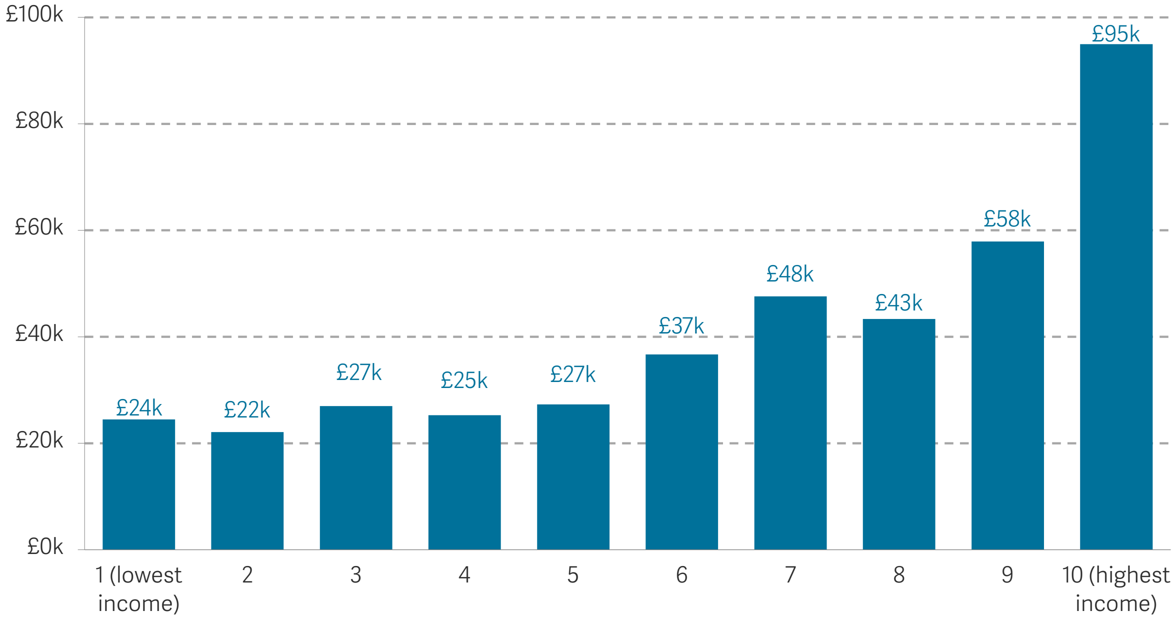
After over 13 years where interest rates remained below 1 per cent, sharp rises in interest rates this year have had a significant effect on investment income. Bank rate is currently 3.5 per cent (having risen from 0.25 per cent in January 2022), and current yield curves imply that it will peak in October 2023, at 4.6 per cent.[49] The OBR projects that aggregate savings income, excluding ISAs, will rise by £20 billion between 2021-22 and 2023-24.[50] Overall, the OBR expects a rise of around £65 billion in gross household interest receipts between 2021-22 and 2023-24.[51] As a proportion of household disposable income, interest

49 Bank of England, Yield Curves, 4 January 2022.
50 OBR, Economic and Fiscal Outlook – Income streams subject to self-assessment income tax, December 2022.
51 OBR, Economic and Fiscal Outlook, November 2022.

receipts will rise from 1.5 per cent in 2021-22 to 5.4 per cent in 2023-24, and 6.0 per cent in 2024-25.[52] This boost to household income will, though, be heavily skewed towards the top of the distribution, as high-income households are more likely to have more money in savings or other financial investments, as Figure 25 shows.[53]

FIGURE 25: **The top income decile hold far more financial wealth than the rest of the income distribution**

Average family net financial wealth per adult, by income decile: GB, 2018-20



NOTES: Data is adjusted using CPIH into 2021/22 prices.
SOURCE: RF analysis of ONS, Wealth and Assets Survey.

The substantial boost from higher interest rates is reflected in our income modelling and the results set out in Section 4 of this report, although there is considerable uncertainty about this income source, as we discuss in Box 6.

52 OBR, Economic and Fiscal Outlook, November 2022.
53 Higher interest rates will also mean households spend more servicing their debts, but the HBAI method does not deduct money spent on loan repayments (other than on mortgages) from measures of disposable income.

BOX 6: Increases in investment income during the forecast period

To project future investment income, we have used the OBR's forecasts of aggregate growth in different types of investment income: dividend income, income from property, and savings income.[54] These figures include strong growth in dividend and property income, partly due to assumed rebounds following the pandemic. But there is a dramatic rise in savings income: this income (excluding tax-free income within ISAs) is projected to increase by 167 per cent in 2022-23 and another 88 per cent in 2023-24. This is largely the result of increases in Bank rate, although the rise in the stock of savings since the arrival of Covid-19 is also a source of savings income growth.

These projected changes are not minor. The £20 billion rise in non-ISA savings income between 2021-22 and 2023-24 equates to over £700 per household. An illustrative increase in rates from 0.5 per cent to 3.5 per cent would be worth £3,000 a year to a household with £100,000 in the bank or ISAs – and many families have substantially more than this. The scale and distribution of this income boost have a noticeable effect on overall income changes for the highest income households in our projections – see, for example, Figure 31 – particularly driven by the very richest.

These projected changes are, of course, dependent on forecasts for interest rates, which are uncertain. But our income projections also depend on inevitably-imperfect data and rough assumptions that make this element particularly uncertain. Survey-based income data may underestimate investment income, for example;[55] while administrative data tends to ignore the non-taxable income within ISAs.[56] Stocks of savings are also very unequally distributed, leading to big differences between typical and mean results – with small numbers of observations having a large impact on survey-based averages. We also have to make assumptions about how an increase in Bank rate would translate into higher returns on different households' savings, and we assume for simplicity that all households see the same proportional increase in their income from savings, even though there will be a range of portfolios and experiences in terms of actual interest rates received.

54 OBR, Economic and Fiscal Outlook – Income streams subject to self-assessment income tax, December 2022. In our analysis we adjust these growth figures to remove population growth.
55 A Aitken & M Weale, Imputation of Pension Accruals and Investment Income in Survey Data, ESCoE, March 2018.
56 A Corlett, A Advani & A Summers, Who gains? The importance of accounting for capital gains, Resolution Foundation, May 2020.

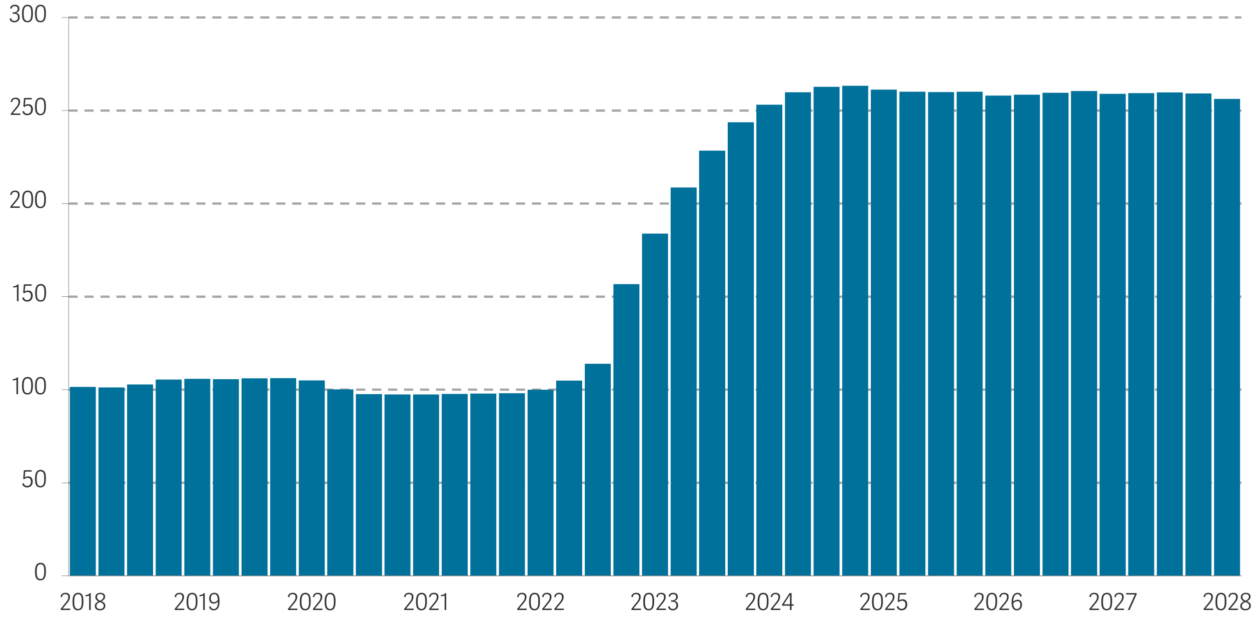
Mortgagors will experience the highest increase in housing costs

Households of all tenures will see housing costs rising in real terms over the coming years, as Table 1 summarises.

For mortgagors, higher interest rates have already begun to push up housing costs for mortgagors, and will continue to do so throughout the forecast period. As Figure 26 shows, mortgage interest payments in 2024 will be two and a half times higher than they were in Q1 of 2022. Indeed, the average mortgagor household renewing their mortgage will face a £3,000 annual increase in their mortgage costs in 2023.[57] The biggest cohort of households will face the mortgage bill shock of being newly affected by the new higher rate regime in 2023-24, with around 1.8 million fixed-rate mortgages set to be renewed, and over 1 million more floating-rate mortgages facing the impact of (likely) continued rises in the Bank of England's policy rate.[58]

FIGURE 26: **Mortgage interest payments are projected to be persistently a lot higher than they have been in recent years, due to higher interest rates**

Indexed average mortgage interest payments (Q1 2022=100): UK



SOURCE: OBR, Economic and Fiscal Outlook November 2022.

To protect social renters from significant rent rises in England, the Government has said it will cap social rent rises in April 2023 at 7 per cent – without this cap, social rents could have risen by 11.1 per cent, as the current social rent uprating settlement in England allows landlords to increase rents by up to the previous September's CPI inflation plus 1

57 Bank of England, Financial Stability Report, December 2022.
58 RF analysis of ONS, Wealth and Assets Survey; Bank of England, Bankstats.

per cent.[59] We have also assumed that the 7 per cent cap on social rent rises will apply in 2024 too, as Q3 2023 inflation is projected to be 6.9 per cent by the OBR. Deflation will also have an effect on the social rent uprating settlement: in 2026, we have assumed that social rents will be frozen, as Q3 2025 inflation is currently forecast by the OBR to be negative.

TABLE 1: **Housing costs will rise in 2023 for all types of tenure**

Annual growth in housing costs: UK

	Mortgage interest payments	Private rents	Social rents	House prices	Average earnings
2020-21	-7.2%	1.4%	2.2%	4.5%	0.0%
2021-22	0.3%	1.6%	1.9%	9.6%	6.5%
2022-23	42.1%	3.1%	4.1%	9.2%	5.4%
2023-24	66.9%	3.5%	7.0%	-4.2%	3.5%
2024-25	12.1%	1.6%	7.0%	-4.0%	1.6%
2025-26	-0.8%	1.7%	0.8%	2.1%	1.7%
2026-27	-0.1%	2.1%	0.0%	3.2%	2.1%
2027-28	-0.3%	2.7%	1.9%	3.6%	2.7%

NOTES: From 2023-24 onwards, we assume rents grow with average earnings growth.
SOURCE: RF analysis of DWP, Abstract of Benefit Statistics; ONS, Average Weekly Earnings; OBR, Economic and Fiscal Outlook November 2022.

The cost of living crisis will continue to be challenging over the next couple of years

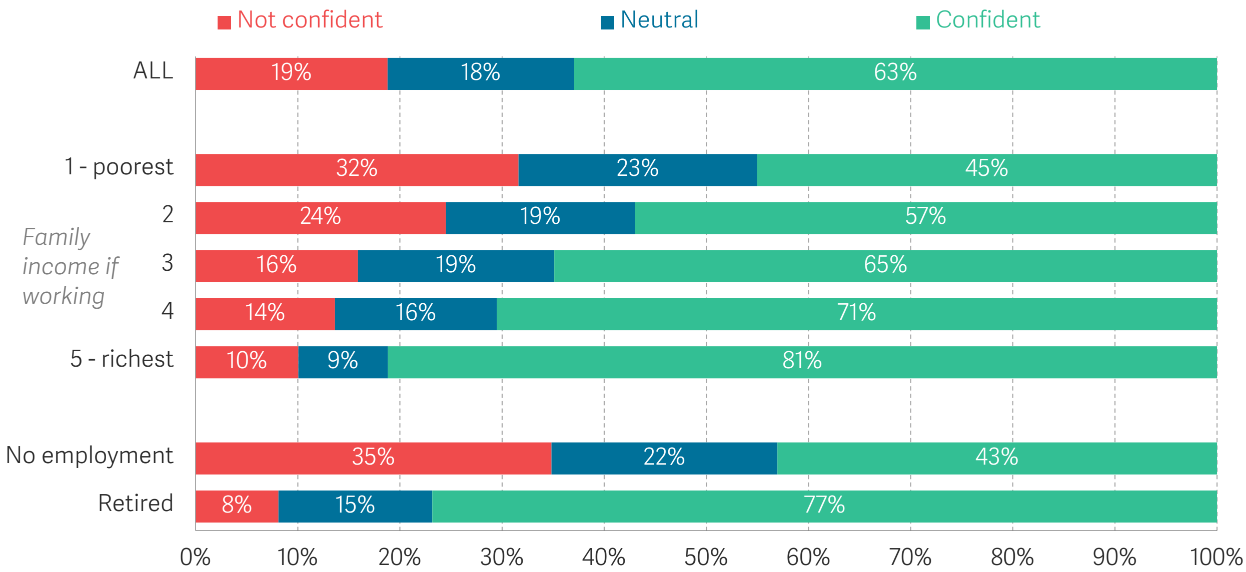
This Section has shown that the cost of living crisis and the resulting rise in interest rates will continue to bear down on household incomes through at least 2023. This is reflected in the results from our survey. 19 per cent of adults (or 10 million people) are

59 The Scottish government have announced a below-inflation rent increase for 2023-24. In Wales, social rents can be uprated by a maximum of CPI plus 1 per cent as long as CPI stays within a prescribed range. Source: Scottish Government, Agreement on social rents for 2023-24, December 2022; Welsh Government, New social rent policy balances tenant affordability with ambitions to build more homes – Julie James, Welsh Government, December 2019.

not confident about their finances as a whole over the next three months (Figure 27).[60] Those in lower-income families and those without employment are also less confident, with 32 per cent of workers in the bottom income quintile and 35 per cent of those not in employment not feeling confident about their finances, more than three times as many as workers in the top income quintile. This rises further to 43 per cent for those not working and on benefits.

FIGURE 27: **Overall, low-income workers and unemployed people on benefits are least confident about their finances over the next three months**

Respondent's confidence about their financial situation as a whole over the next three months: UK, 23-30 November 2022



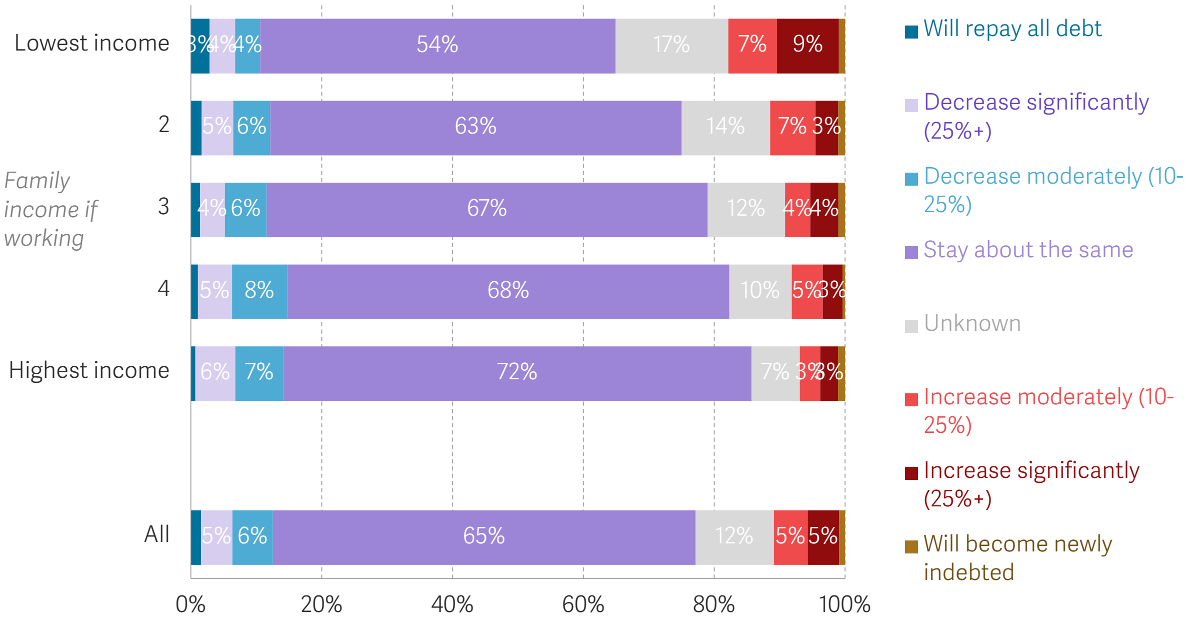
NOTES: All (n=10,470). Lowest income quintile (n=988), q2 (n=740), q3 (n=897), q4 (n=703) and highest income quintile (n=1128). No employment (n=1631), Retired (n=2,824). Unknowns have been excluded. These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave.

Survey respondents also expect their non-housing debt to increase further in the coming months. 17 per cent of workers in low-income families expect that their non-housing debt will increase by more than 10 per cent over the next three months, while 8 per cent of median-income families and 6 per cent of the highest-income families expect their debts to increase either a little or a lot. Of course, this increased debt will also likely be subject to higher interest rates, as discussed earlier in this Section.

60 Levels of financial confidence are higher than the Financial Fairness Trust who found that 35 per cent of respondents in October 2022 were not confident about their finances over the next three months, compared with 42 per cent who were confident about their finances over the next three months.

FIGURE 28: **Lower-income families expect debts to continue to rise in 2023**

Respondent's expectations on how their levels of non-household debt will change over the next three months: UK, 23-30 November 2022



NOTES: All (n=4456). Lowest income quintile (n=988), q2 (n=740), q3 (n=897), q4 (n=703) and highest income quintile (n=1128). Debt excludes housing debt, student loans, and car finance. These figures have been analysed independently by the Resolution Foundation.
SOURCE: RF analysis of YouGov, adults age 18+ Cost of Living Crisis November 2022 wave.

Overall, this section has set out the reasons to think that, for household living standards, the worst is not yet behind us. Although inflation could fall this year, food inflation (which affects low-to-middle income families the most) is continuing to climb, and even when inflation does start to fall, that does not mean a fall in the price level. There are also headwinds in 2023-24 from declining support for energy bills, personal tax rises, and higher mortgage payments. Over the longer term, inflation should be much less of a concern from 2024, and earnings should grow in real terms, but real wages won't reach their Q1 2022 rate until the end of 2027, nearly 6 years later. The next section shows how these forecasts for inflation, the labour market and housing costs combine into prospects for household incomes.

Section 4

Future prospects for living standards

This Section takes the economic forecasts and policy announcements outlined in Section 3, and projects what they mean for household living standards. Typical incomes among non-pensioners are set to fall by 3 per cent in 2022-23, and will fall by an even larger 4 per cent in 2023-24, driven by the slimming-down of government support for households, personal tax rises, and rising costs for mortgagors. The fall in 2023-24 is set to be largest single-year fall since 1975, and the two-year fall of 7 per cent (or £2,100 for a typical household) is bigger than in the Financial Crisis, where there was a two-year decline of 5 per cent. This precipitous decline will take typical incomes in 2023-24 to where they were in 2018-19 – and lower than they were in 2016-17 – and would mean that this becomes the worst Parliament on record for living standards for almost all parts of the income distribution. Although incomes should start growing in 2024-25, typical incomes are set to still be below their pre-pandemic (2019-20) level in 2027-28.

Almost all parts of the income distribution see incomes fall in 2022-23 and 2023-24 (except the top 5 per cent, where higher interest rates boost investment and unearned income), and, in both years, the falls in income are smaller at the bottom of the distribution. This partly reflects that the Cost of Living Payments in both years are worth the most (in proportional terms) to low-income households, and that benefits will be uprated in April 2023 by 10.1 per cent in a year where inflation is set to average 5.5 per cent. But it is also a statistical artefact of following the usual assumption that all households face the same inflation rate. This is clearly untrue, with rapidly increasing prices for energy and food meaning that inflation for the richest 10 per cent of households is about 1.5 per cent lower than the poorest 10 per cent in November 2022. Adjusting income changes for these different inflation rates means that the fall in household incomes this year and next is shared more evenly.

From 2024-25, income growth returns for most of the distribution, except where the loss of the £900 Cost of Living Payments outweighs the high benefit uprating of nearly 7 per cent in a year where inflation is set to average 0 per cent. From 2025-26, income growth is stronger at high incomes than at low incomes, chiefly reflecting that earnings are expected to be growing in real terms, but that income from benefits is (at best) staying constant in real terms. Should inflation turn negative – as is forecast by the OBR – then the real value of some benefits will rise slightly, but the continued roll-out of the two-child limit, the benefit cap and frozen LHA rates will bear down on incomes of low-income households.

Absolute poverty is set to rise in the short run, from 17.2 per cent in 2021-22 to 18.3 per cent in 2023-24 (or an additional 800,000 people in absolute poverty); this reflects that incomes are set to fall in real terms in the short term, and the absolute poverty threshold is fixed in real terms. Absolute child poverty is set to rise by 2.9 percentage points between 2021-22 and 2023-24. Absolute poverty among pensioners is set to fall between 2022-23 and the end of the forecast period in 2027-28: pensioners benefit from the State Pension triple lock, and are less likely than working-age adults to be hit by rising housing costs.

The outlook for relative poverty appears more promising than for absolute poverty because the threshold for the relative poverty measure is set to fall considerably in 2022-23 and 2023-24, as typical income falls. However, relative child poverty returns to its upward trend when the cost of living crisis ends, as the two-child limit, benefit cap and frozen LHA rates continue to drag down income growth at the bottom of the distribution. The rate that we forecast for 2027-28 would be the highest relative child poverty rate since 1998-99, and the rise is driven entirely by large families: relative child poverty for families with three or more children is set to hit 55 per cent in 2027-28, and 77 per cent of children in families with four or more children will be in relative child poverty by 2027-28.

Income inequality across the bulk of the distribution will fall during 2022-23 and 2023-24, but then return to the usual pattern of rising during times of growth. However, the rapid growth in investment income, driven by rising interest rates, will predominately benefit the top 5 per cent, and this means that the Gini coefficient will rise in each of the next five years, reaching a new record high of 40.8 per cent in 2027-28.

After setting out the outlook for inflation, energy bills and support, earnings, benefits, taxes, and housing costs in Section 3, this Section presents the results from our projections for incomes, poverty and inequality between 2021-21 and 2027-28. As discussed in Section 1, these are based on the 2019-20 Family Resources Survey dataset which we uprate and project using more timely data on economic factors such as inflation and earnings and OBR forecasts (we give more details in Annex 1 and 2).

As in previous Living Standards Outlooks, our aim is to present statistics and analysis that are compatible with the official Households Below Average Income (HBAI) statistics. Because of this, we use the standard Consumer Prices Index (CPI) to adjust incomes in different years for the impact of price changes. This is a particularly important point given the large changes (in both directions) in the price of energy in recent and future years; in our modelling methodology, the way that energy price changes affect household incomes is through their impact on the CPI. Using the same measure of inflation for all households is akin to assuming that all households spend the same fraction of their budget on energy (as well as on other goods driving changes in the price level), whereas in reality it forms a larger part of the budget of low-income households.[61] We discuss this more in Box 7.

Despite government support, household incomes across the distribution are due to fall significantly in 2022-23 and 2023-24

Figure 29 shows the annual growth in non-pensioner median household income. Median income is set to fall by a staggering 3 per cent in 2022-23 and 4 per cent in 2023-24, with the fall in 2023-24 being the largest fall since 1975.

It may seem surprising that median income is set to fall by more in 2023-24 than 2022-23, even though inflation will be lower in 2023-24. This reflects several of the factors that we discussed in Section 3, including that:

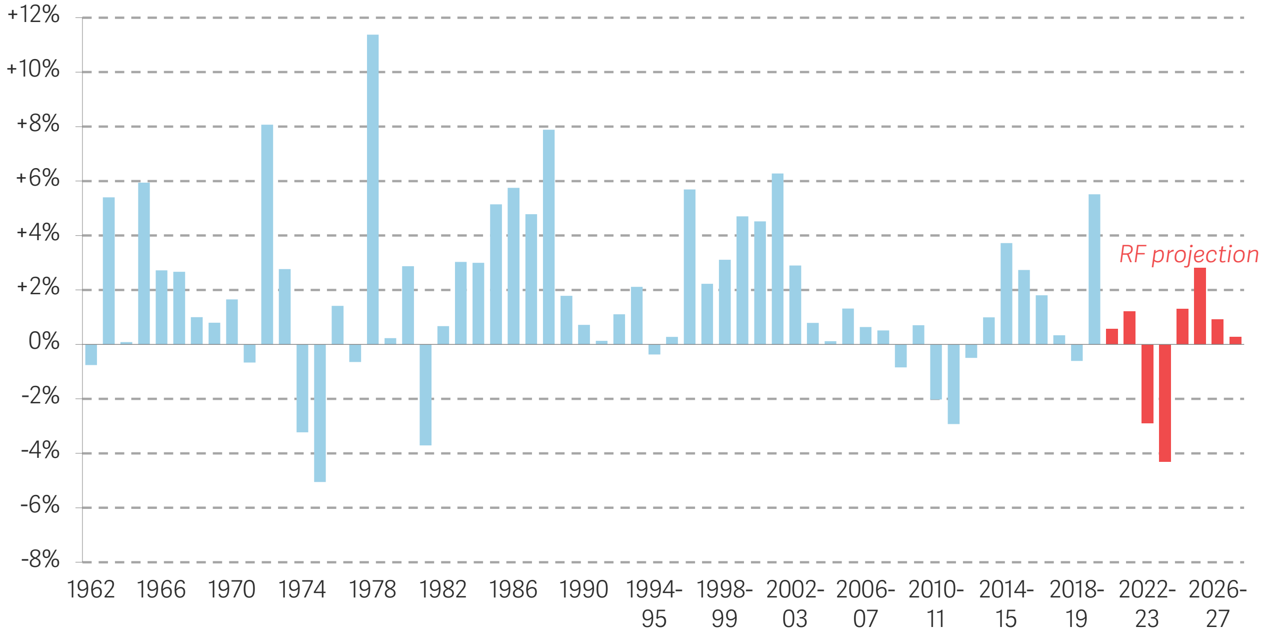
- government support through the Cost of Living Payments in 2023-24 will be less generous and more focused on low-income households than in 2022-23;
- rising interest rates will push up housing costs; and,
- personal taxes will be higher.

Therefore, although the economic situation may appear to be less bad in 2023-24 than 2022-23, a typical household will likely face a larger income fall.[62]

61 A Corlett & L Try, The Living Standards Outlook 2022, Resolution Foundation, March 2022.
62 T Bell, New Year's Outlook 2023: They think it's all over... it isn't now, Resolution Foundation, December 2022.

FIGURE 29: **Median incomes are set to fall by 3 per cent this year and 4 per cent next year, before growth returns in 2024-25**

Annual real growth in median equivalised household disposable income for non-pensioners, after housing costs: GB/UK



NOTES: Projections after 2019-20. Data source change in 1994-95. GB from 1994-95 to 2001-02.
SOURCE: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

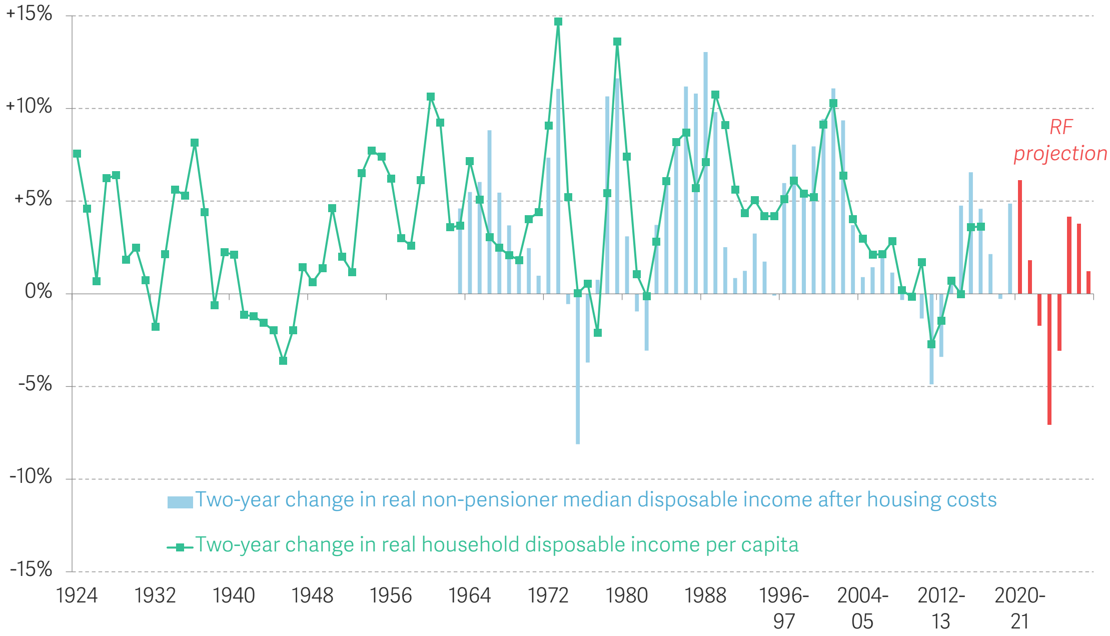
Income growth returns in 2024-25, but remains weak. As we discussed in Section 3, there are a range of factors driving this: mortgage costs are set to remain high, earnings won't reach their pre-cost of living crisis real-terms levels until Q4 of 2027, and unemployment will remain elevated.

When looking at two-year changes in median incomes, as we do in Figure 30, the early 2020s stand out. Median incomes are set to fall by 7 per cent between 2021-22 to 2023-24, or a fall of £2,100; this would be the biggest fall seen since mid-1970s (and larger than the depths of the Financial Crisis, where there was a 2-year decline of 5 per cent). This is similar to the OBR's forecast for Real Household Disposable Income, which shows RHDI per person falling by 7.1 per cent from 2021-22 to 2023-24 (4.3 per cent in 2022-23 and 2.8 per cent in 2023-24).[63]

63 OBR, Economic and Fiscal Outlook, November 2022.

FIGURE 30: **The cost of living crisis will lead to the largest median income fall since the 1970s**

Two-year real growth in median equivalised household disposable income for non-pensioners, after housing costs: GB/UK



NOTES: Projections after 2019-20. RHDI figures are means, and calendar years throughout. Non-pensioner median figures are GB from 1994-95 to 2001-02.
SOURCE: RF analysis of DWP & IFS, Households Below Average Income; RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts; and RF analysis of Bank of England, A millennium of macroeconomic data.

Middle- and higher-income households will face the largest income falls during the cost of living crisis

Figure 31 shows how incomes will change across the income distribution – but under the assumption that it is valid to use the same measure of price inflation at all parts of the income distribution (we discuss this assumption in Box 7).

Incomes fall across the distribution in 2022-23 and 2023-24, apart from in the top 5 per cent, where higher interest rates boost investment and unearned income enough to offset the decline in real earnings and extra tax payments, such that top incomes are projected to rise by 4 per cent between 2021-22 and 2023-24.

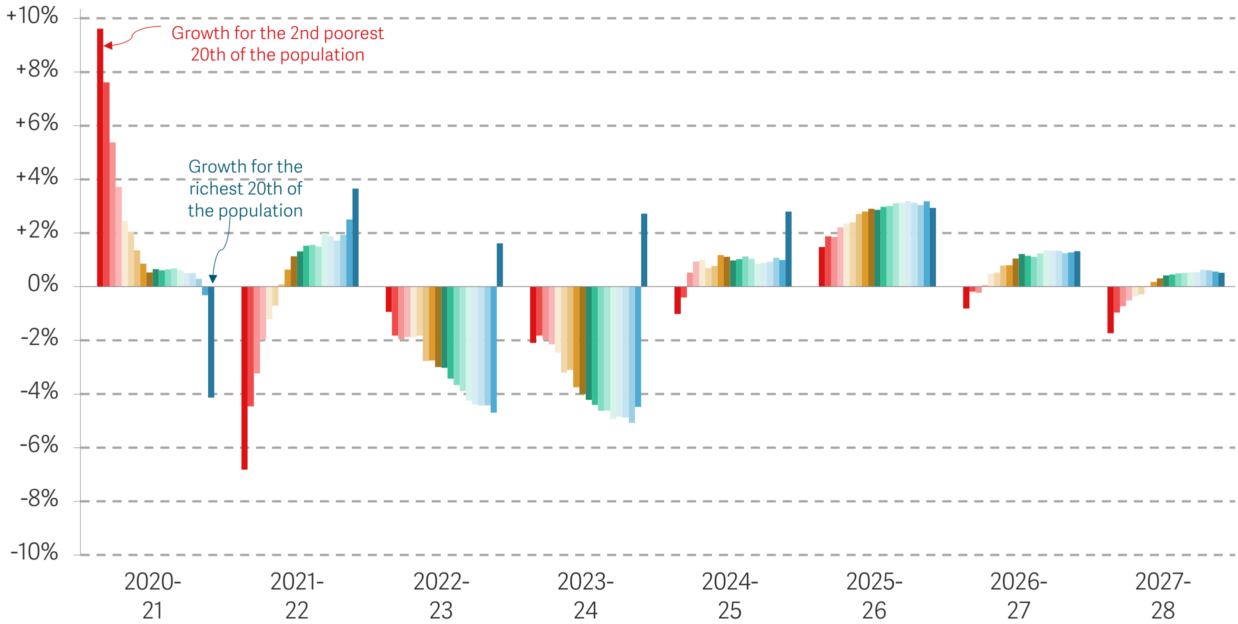
In both years, declines in income are smaller at the bottom of the distribution. This partly reflects that the Cost of Living Payments in both years are worth the most (in proportional terms) to households on benefits, but also that benefits will be uprated in April 2023 by 10.1 per cent in a year where inflation is set to average 5.5 per cent. Indeed, over the course of the two-year squeeze, real incomes among the poorest fifth of households will fall by 4 per cent, compared to 9 per cent for rich households (in the 19th vigintile of the distribution).

In 2024-25, income growth returns for most of the distribution, but the loss of the Cost of Living Payments drives income falls right at the bottom of the distribution where this loss exceeds the gain coming from the (expected) benefit uprating of 6.9 per cent in a year where inflation is predicted by the OBR to average 0 per cent. Rising interest rates continues to boost income at the very top of the distribution.

In 2025-26 and future years, there is a clear pattern for growth to be stronger at high incomes than at low incomes. This chiefly reflects our assumption that earnings will be growing in real terms in these years, whereas income from benefits is (at best) staying constant in real terms. If the two years of negative inflation forecast by the OBR come about, then this will (very slightly) push up the real value of some benefits, but other parts of the benefit system – such as the continued roll-out of the two-child limit, the freeze to the value of the benefit cap (from April 2024-25) and frozen LHA rates – bear down on incomes the further into the forecast period we get.

FIGURE 31: **Support for energy costs prevents large falls in income at the bottom of the income distribution in 2022-23 and 2023-24, and rising interest rates drives gains at the top**

Annual real growth in average equivalised household disposable income for non-pensioners, after housing costs, by income vigintile: UK



NOTES: We exclude the bottom 5 per cent, due to concerns about the reliability of data for this group.
SOURCE: RF analysis of DWP, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

As we flagged above, these statistics follow standard HBAI practice in assuming that the published CPI is applicable to all households. In Box 7, we show how allowing for differential inflation alters our impression of income changes in 2022-23 and 2023-24.

BOX 7: **The distributional variance of inflation**

The Consumer Prices Index (CPI) attempts to measure the change in prices of a basket of goods and services that is meant to represent the consumption patterns of an average household. However, different households will consume different goods and services in different quantities. In particular, low-income households spend a higher-than-average proportion of their incomes on essentials such as energy and food. This means that low-income households are currently facing higher rates of inflation then high-income households, as energy and food prices have increased significantly during the cost of living crisis.[64]

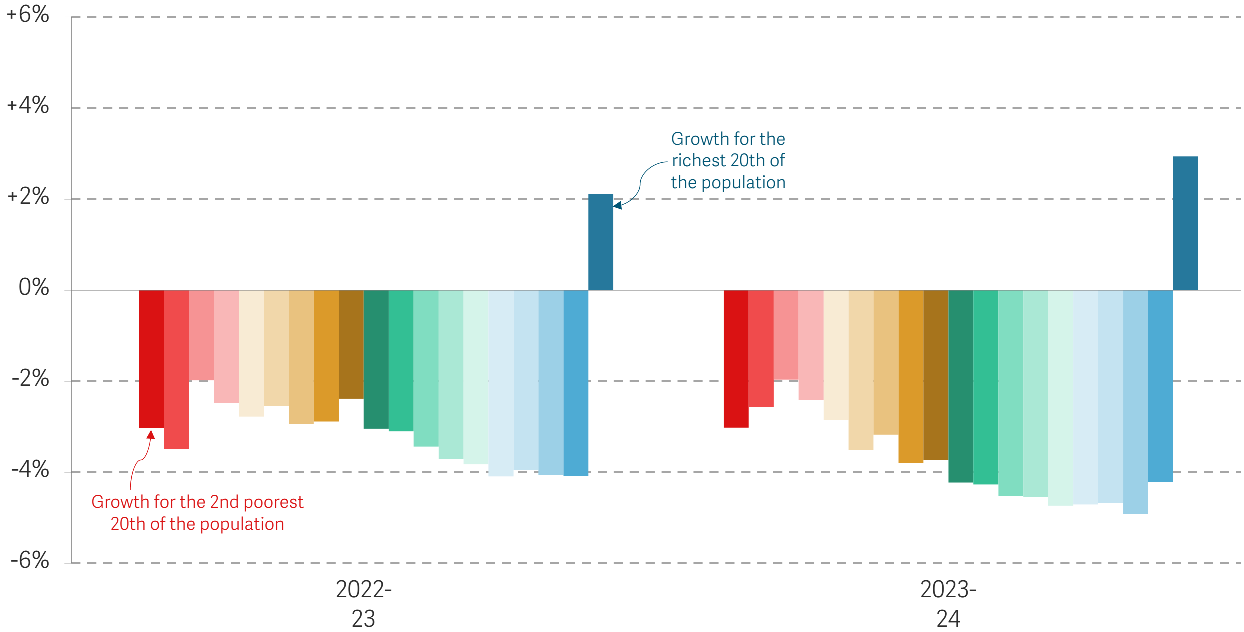
Because our aim in this Section is to present analysis that is compatible with the official Households Below Average Income (HBAI) statistics, we use the standard Consumer Prices Index (CPI) to adjust incomes in different years for the impact of price changes. Given that low-income households are currently facing higher-than-average inflation rates, then our analysis will understate the extent of income falls in 2022-23 for low-income households (and overstate it for high-income households). To see how important this effect is, Figure 32 repeats the analysis of Figure 31, but uses our estimates of the effective inflation rate in each vigintile to calculate the change in real incomes. We describe our methodology for creating these estimates in Annex 1.

The effect of allowing for differential inflation is to flatten the profile of the falls in income. The pattern is still broadly progressive, in that high-income households tend to face larger falls than low-income households, but the difference is much smaller than if we assume the same inflation rate affects all households. When differential inflation is taken into account, real incomes among the poorest fifth of households will fall by 5 per cent, compared to 8 per cent for rich households (in the 19th vigintile of the distribution).

64 ONS, Inflation and cost of living for household groups, UK: October 2022.

FIGURE 32: **Low-income households face larger income falls in 2022-23 and 2023-24 when differential inflation is accounted for**

Annual real growth in average equivalised household disposable income for non-pensioners using differential inflation rates, after housing costs, by income vigintile: UK



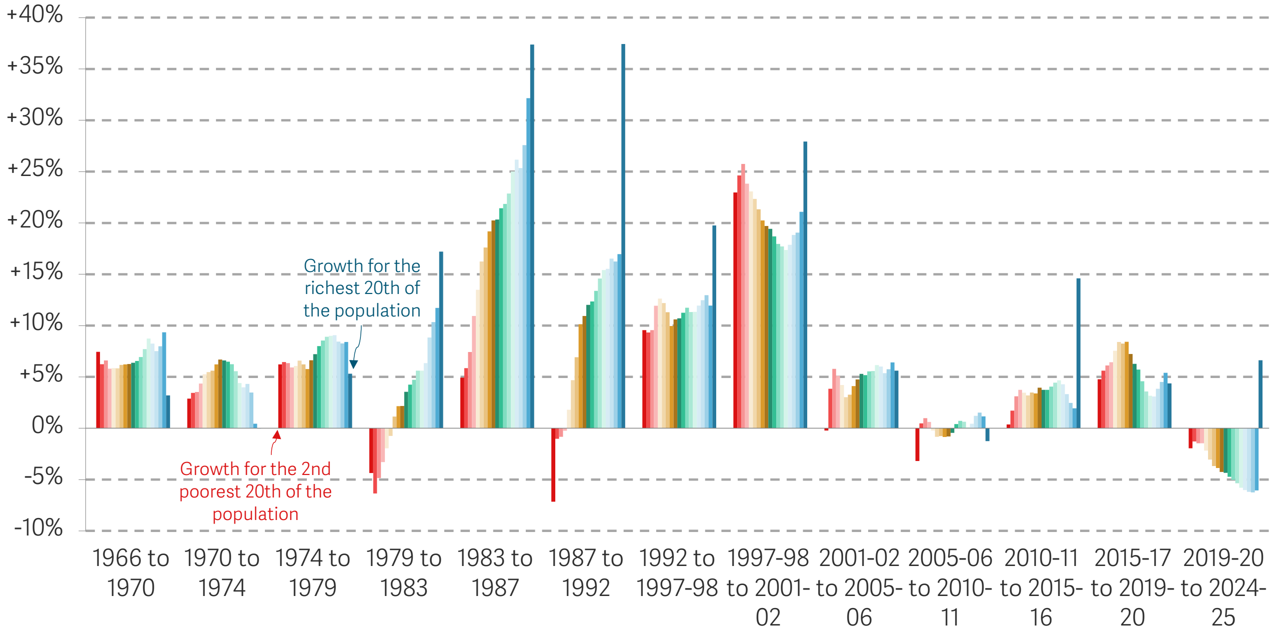
NOTES: We exclude the bottom 5 per cent, due to concerns about the reliability of data for this group.
SOURCE: RF analysis of DWP, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

However, if energy prices fall, as is predicted for 2024 and 2025 (at least by the OBR), then this pattern will reverse, and the effective inflation rate faced by low-income households should be lower (or more negative) than average, meaning that the pattern of income changes show in Figure 31 will understate income growth for low-income households (and similarly overstate it for high-income households). Due to the uncertainty of forecasts, though, we only have considered the impact of differential inflation for 2022-23 and 2023-24.

Looking at income changes over a longer time period shows that the cost of living crisis period is unique. As Figure 35 shows, this Parliament is set to be the worst on record for income growth across the majority of the income distribution. High inflation, weak earnings growth, and personal tax rises drag down on incomes across the distribution. The only part of the income distribution where incomes grow is in the top 5 per cent, where households benefit from higher interest rates.

FIGURE 33: **This will be the worst Parliament on record for income growth across most of the income distribution**

Total real growth in average equivalised household disposable income for non-pensioners by Parliament, after housing costs, by income vigintile: UK



NOTES: Some periods are four years long and others five years. The chosen time periods correspond to the years of past general elections (plus 2024), but we do not include a division for the 2017 election and nor do we try to estimate growth over the February to October parliament of 1974. We exclude the bottom 5 per cent, due to concerns about the reliability of data for this group.
SOURCE: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

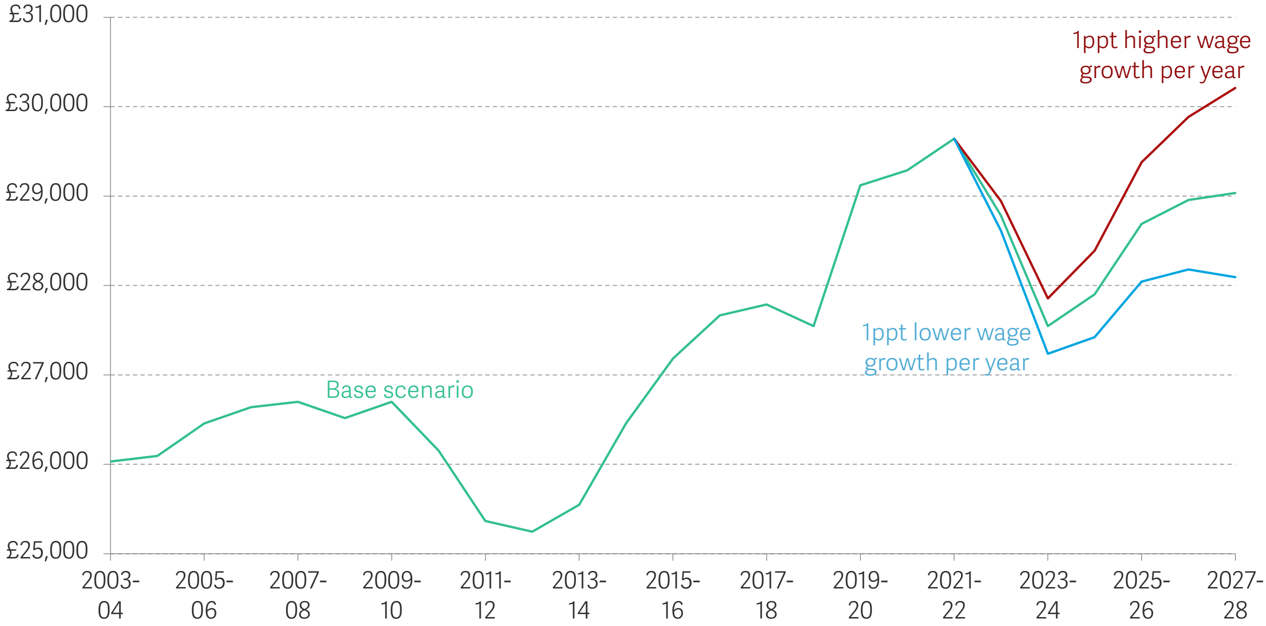
The outlook for income levels is bleak – but better wage growth would improve it

It is also worth considering the outlook for income levels, as well as income growth. Under our central scenario, median income will fall sharply in 2022-23 and 2023-24: in 2023-24, it is set to reach the same level as in 2018-19, and lower than it was in 2016-17. Indeed, median income won't have recovered to its pre-pandemic (2019-20) level by 2027-28 (see Figure 34).

But higher wage growth could improve this scenario. If nominal wages grew by 1 percentage point more per year, median incomes would reach their pre-pandemic level in 2025-26. However, if median incomes grew 1 percentage point less than forecast from 2022-23 onwards, in 2023-24 they would be at their lowest rate since 2015-16.

FIGURE 34: **Incomes will grow from 2024-25, but typical income will be below pre-pandemic levels even by 2027-28**

Real median non-pensioner equivalised household disposable income, after housing costs, 2022-23 terms: UK



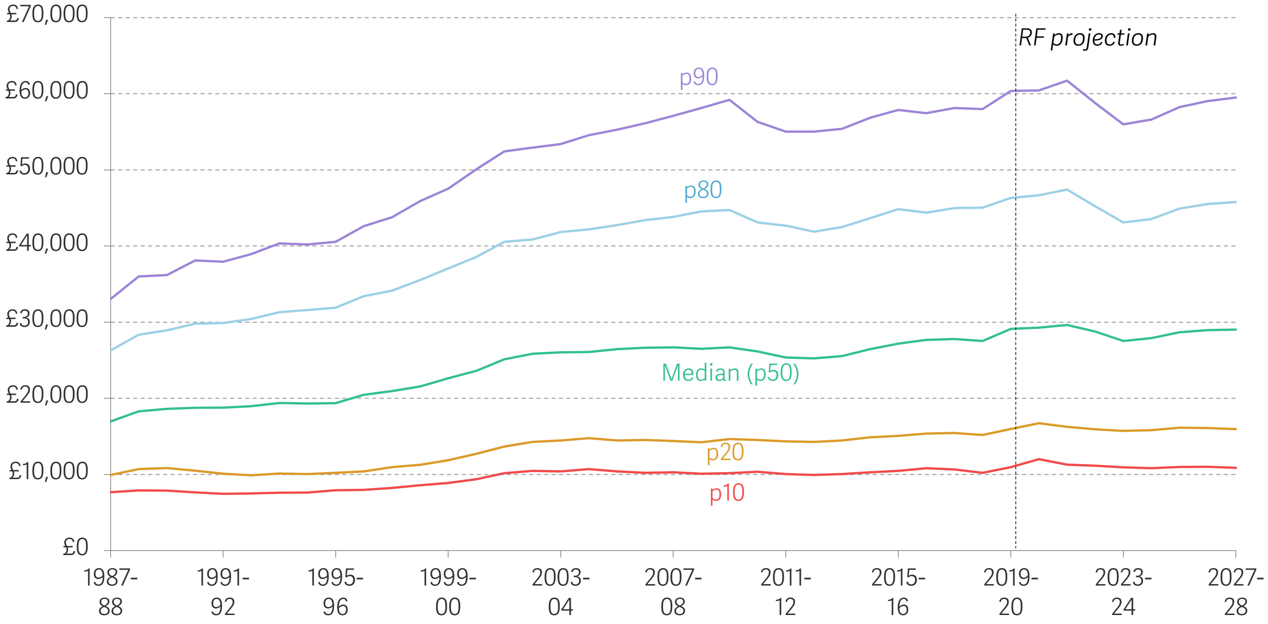
NOTES: Incomes are projected after 2019-20.
SOURCE: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

Figure 35 shows income levels across the distribution. This confirms what was shown in Figure 31: that high-income households look set to experience the largest income falls during the cost of living crisis (although Box 7 showed that the extent of this difference depends on whether we impose a constant inflation rate for all households). Like median income, the 80th and 90th percentile incomes do not reach their pre-pandemic level by the end of the forecast period, but incomes at the 10th and 20th percentile do.

If we instead use a different rate of inflation for every vigintile, then the income falls are smaller at the top and larger at the bottom during 2022-23 and 2023-24, which would push up the 90:10 ratio in 2023-24 from 4.5 to 4.7. As discussed in Box 7, it is likely that some of that would reverse in 2024-25 and after, but we have not attempted to produce vigintile-specific rates of inflation for those years.

FIGURE 35: **The cost of living crisis damages higher-income households' income levels in the long term**

Annual equivalised household disposable incomes for non-pensioners at various points of the distribution, after housing costs, 2022-23 terms: GB/UK



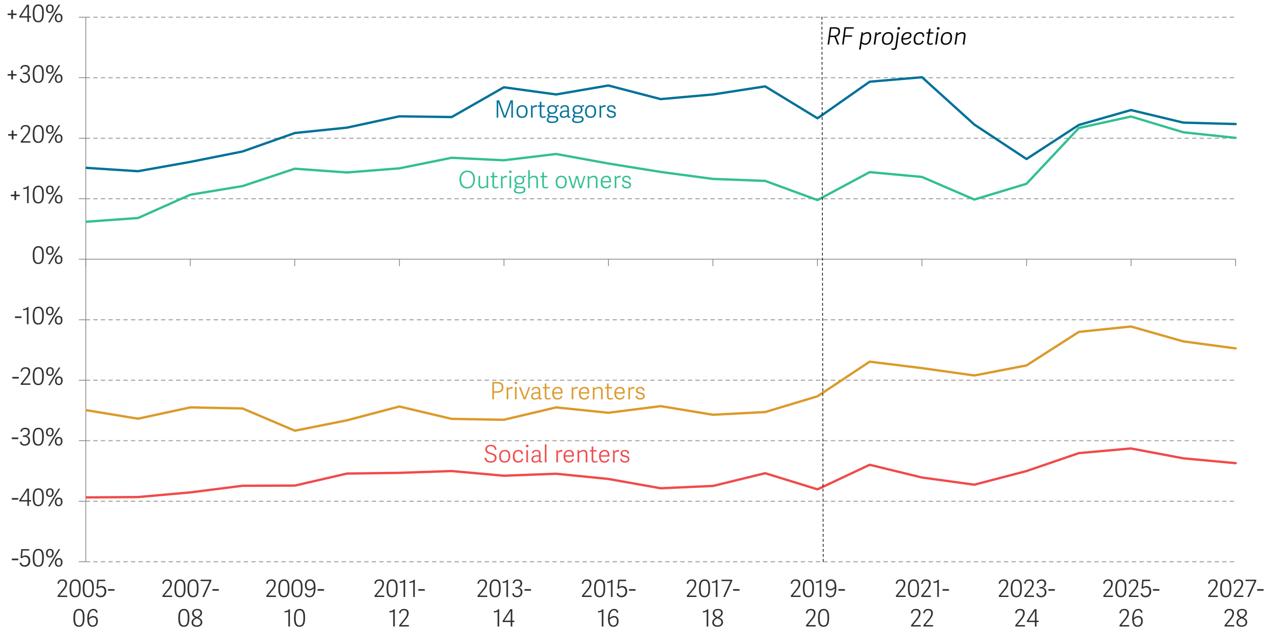
NOTES: Incomes are projected after 2019-20.
SOURCE: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

Figure 36 shows the ratio of typical income for people in different housing tenures as a proportion of the overall median non-pensioner household income in that year. The long-run trend is for the median income of mortgagors and outright owners to be consistently higher than the overall median, and median income among social and private renters to be lower.

Rising mortgage costs will, unsurprisingly, reduce typical incomes for mortgagors significantly: by 12 per cent between 2021-22 and 2023-24, or £4,400. This fall in income brings them closer to the incomes of outright owners, and reduces the relative advantage that mortgagors have had from the peak in 2021. However, the relative position of mortgagors has been on an upward trend since (at least) the mid-2000s, in part because of the very low mortgage rates that have applied since the financial crisis. The fall-back in the relative position of mortgagors during the cost of living crisis should really be seen as a partial reversal of the advantages that they accrued after over a decade of record-low interest rates. Although in 2024-25 mortgagor incomes will be 22 per cent higher than the typical working-age income, lower than the 30 per cent gap in 2021-22; this is still higher than the gap in 2007-08 when interest rates were over 5 per cent, of 16 per cent.

FIGURE 36: **Higher mortgage costs damage income growth for mortgagors, but do not completely wipe out their relative gains from the low-interest rate era**

Real median non-pensioner equivalised household disposable income by housing tenure, after housing costs, as a proportion of overall real median non-pensioner equivalised household disposable income: UK



SOURCE: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

Child poverty is set to worsen

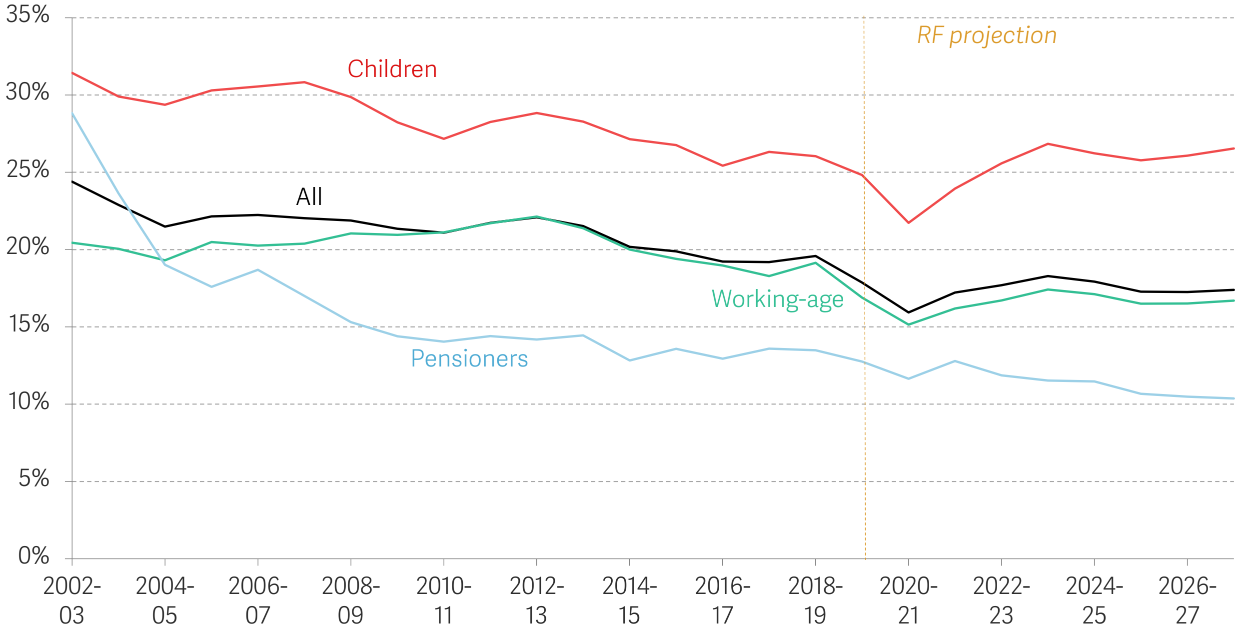
We turn now to rates of absolute and relative poverty.

Figure 37 shows rates of absolute poverty across the whole population (including pensioners) as well as rates for children, working-age people and pensioners.[65] Absolute poverty is set to rise overall in the short run, from 17.2 per cent in 2021-22 to 18.3 per cent in 2023-24 (or an increase of 800,000 people); this reflects that incomes are set to fall in real terms (as shown in Figure 31) and that the absolute poverty threshold is fixed in real terms.[66] Of the three different groups, child absolute poverty rises by the most – by 2.9 percentage points from 2021-22 to 2023-24, or 400,000 children. Absolute poverty among pensioners falls by around 60,000 from 2022-23 to the end of the forecast period: this reflects that they benefit from the State Pension triple lock, and are less likely to be hit by rising housing costs.

65 Absolute poverty is defined as below 60 per cent of the median income in 2010-11.
66 We have not attempted to calculate poverty rates allowing for different rates of inflation across the income distribution.

FIGURE 37: **Falling incomes mean absolute poverty is set to rise during the cost of living crisis**

Proportion of people living in absolute poverty, after housing costs: UK



NOTES: Outturn data is available for 2020-21 but the values shown here are our nowcasts, as we use 2019-20 rather than 2020-21 data as the starting point for our projections.
SOURCE: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

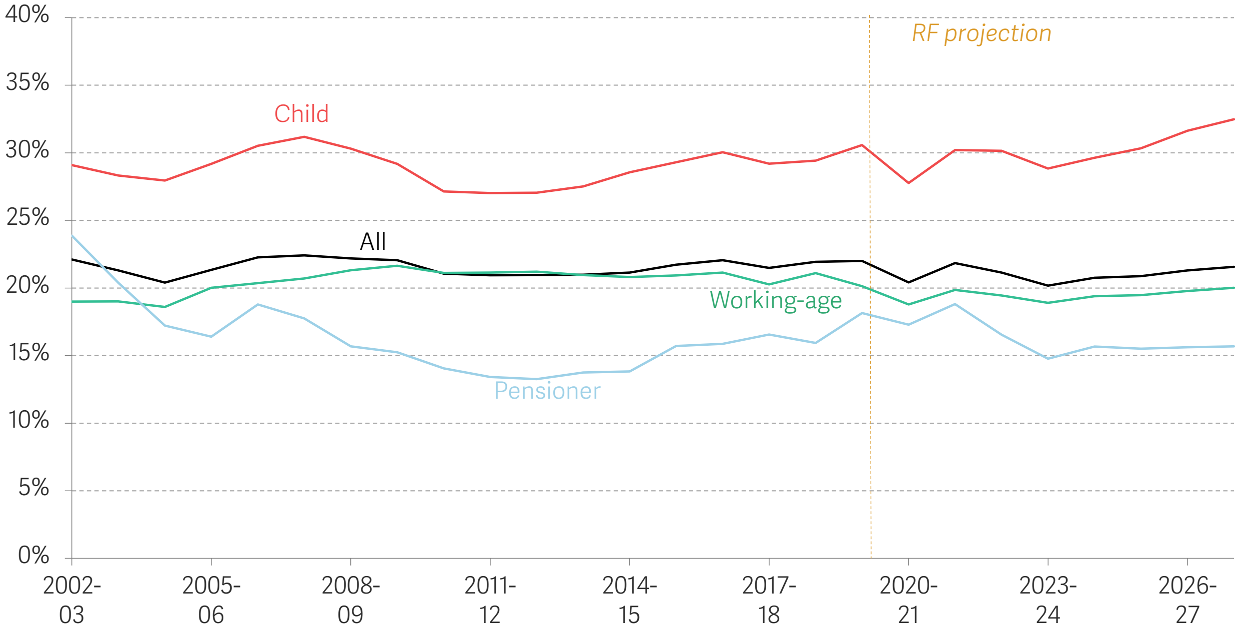
The outlook for relative poverty is shown in Figure 38; here, the prospects appear better than they do for absolute poverty. Indeed, relative poverty falls from 21.8 per cent in 2021-22 to 20.2 per cent in 2023-24, or by 1 million people. This is because the effective poverty threshold under a relative poverty measure is set to fall considerably in 2022-23 and 2023-24, as the median income falls (as Figure 31 shows).[67]

As with absolute poverty, relative pensioner poverty falls more than for the other groups, falling from 18.8 per cent in 2021-22 to 14.8 per cent in 2023-24, or by 400,000 people. Worryingly, relative child poverty continues to rise post-crisis, as the two-child limit, benefit cap and frozen LHA rates continue to drag down income growth at the bottom of the distribution. Indeed, by 2027-28, relative child poverty is set to have reached its highest rate since 1998-99, with 170,000 more children set to be in relative poverty than in 2021-22.

67 Relative poverty is defined as below 60 per cent of the median income of the given year.

FIGURE 38: **Financial support for low-income families means relative poverty rates are set to fall during the cost of living crisis**

Proportion of people living in relative poverty, after housing costs: GB/UK



NOTES: Outturn data is available for 2020-21 but the values shown here are our nowcasts, as we use 2019-20 rather than 2020-21 data as the starting point for our projections.
SOURCE: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

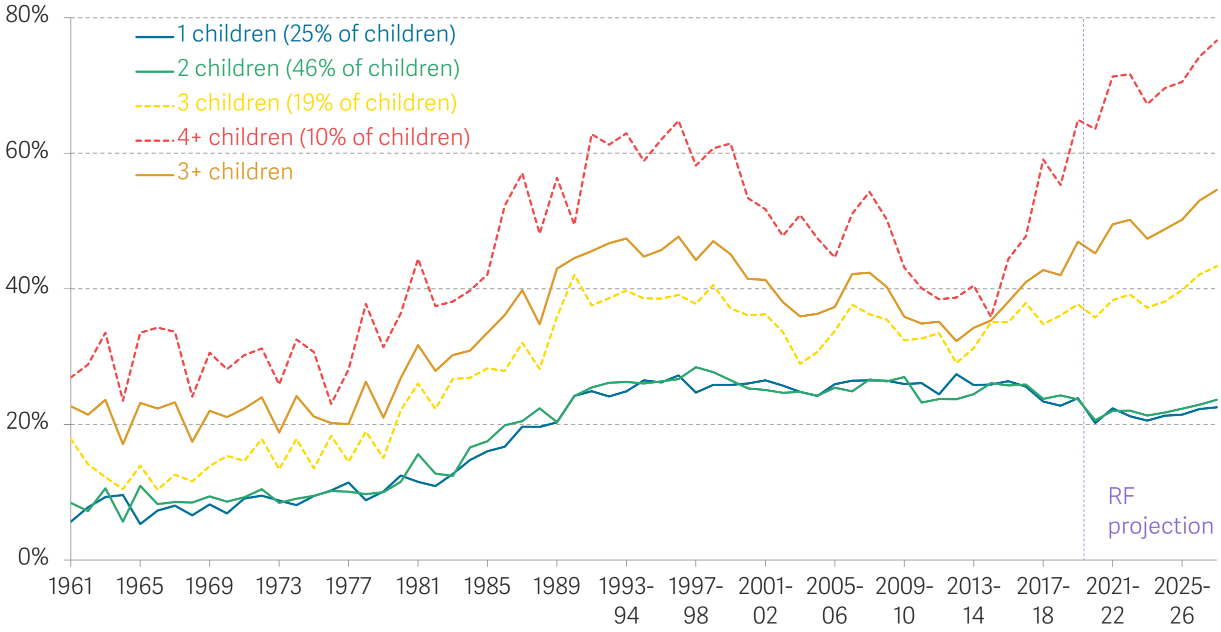
Figure 39 shows relative child poverty rates by the number of children in the household: rates for families with one or two children are very similar to each other, but rates for larger families are much higher – matching our findings on food insecurity, shown earlier in Figure 7. It also shows that the forecast rise in relative child poverty is driven entirely by larger families. Relative child poverty in families with three or more children is set to hit 50 per cent in 2025-26 and 55 per cent in 2027-28; 77 per cent of children in families with four or more children will be in relative child poverty by 2027-28.

It is incredibly striking that these rates of relative child poverty for different-size families converged during the 2000s and early 2010s and have diverged since. Key contributors to this are the two-child limit, which was explicitly designed to limit the amount of benefits large families could receive, and the benefit cap, which disproportionately affects families with children and high housing costs.[68]

68 120,000 households were subject to the benefit cap in August 2022, 87 per cent of which have children and 70 per cent of which are lone parents. The mean amount lost because of the cap is £51 a week. DWP, Benefit cap: number of households capped to August 2022, 13 December 2022.

FIGURE 39: **Larger families are disproportionately more likely to be in poverty**

Proportion of children living in relative poverty, after housing costs, by number of children in the household: GB/UK



NOTES: Data source changes in 1994-95. GB from 1994-95 to 2001-02.
SOURCE: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

Inequality is set to increase throughout the forecast period

Figure 40 shows the Gini coefficient for household income, a measure of inequality where 0 per cent corresponds to complete equality and 100 per cent complete inequality.

Our projections suggest that this measure of inequality is set to rise every year from 2021-22 onwards. This follows on from falls in the Gini coefficient in 2020-21, where the £20 uplift to Universal Credit and Working Tax Credits boosted incomes at the bottom of the distribution, and the furlough scheme provided incomes to people who would have otherwise become unemployed.

This rise in inequality is primarily driven by gains at the top of the distribution from growth in unearned income. After 2023-24, the pattern of income growth shown in Figure 31 is unambiguously inequality-increasing. Our forecast is that, by 2027-28, inequality could reach a record high of 40.8 per cent, higher than the previous peak just before the financial crisis.[69]

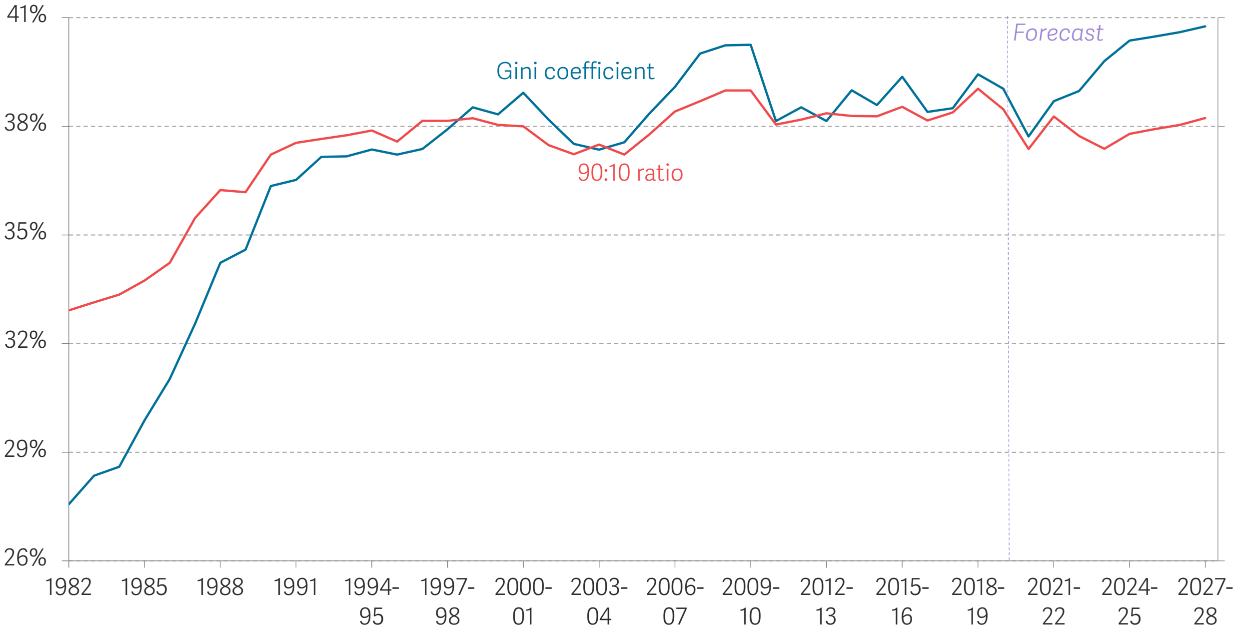
Figure 40 also shows the 90:10 ratio for household income, a measure of inequality that compares the 90th percentile of the distribution to the 10th percentile. The 90:10 ratio is

69 P Bourquin, M Brewer & T Wernham, Trends in income and wealth inequalities, The Deaton Review of Inequality, November 2022.

set to have reached a peak in 2022-23 of 5.09, following the abolition of the £20 a week boost to Universal Credit and Working Tax Credits, and due to government support with energy bills being (relatively) universal across the distribution.

FIGURE 40: **Inequality as measured by the Gini coefficient is set to reach a record high**

Gini coefficient (left axis) and 90:10 ratio (right axis) for equivalised household disposable income, after housing costs: GB/UK



NOTES: Data source changes in 1994-95. GB from 1994-95 to 2001-02. Our modelling produces lower inequality figures than the published data suggests – in part due to under-reporting of benefits in the published data. We adjust our projection levels to match the outturn data.
SOURCE: RF analysis of DWP & IFS, Households Below Average Income; and RF projection including use of the IPPR Tax Benefit Model, ONS data, and OBR forecasts.

Overall then, households across the income distribution are set to face another terrible year, as incomes fail to keep up with the rising cost of living. Real growth in incomes will return from 2024-25, but growth will be slow. Indeed, the combined impact of the pandemic and the cost of living crisis is a wasted eight years for household living standards: on our forecasts, median incomes in 2027-28 will still be £100 lower than their 2019-20 levels. Along with changes to the cost of living, the other key determinant of living standards over the next few years is the novel phenomenon of interest rates above 0.5 per cent; this may help home ownership become more realistic for some (if it lowers house prices), but the boost to investment income looks set to stretch out income inequality further.

With the Covid-19 pandemic coming after a fifteen-year period characterised by low growth and high inequality, there is a real risk that UK is becoming cemented as a stagnation nation. Measures that could help solve those fundamental weaknesses of the UK economy are the subject of our ongoing project with the Centre for Economic Performance at the London School of Economics; this work will conclude in late 2023.[70] In the next Section, though, we discuss what the Government should do in the short-run to protect household incomes for the remainder of the cost of living crisis.

70 Resolution Foundation & Centre for Economic Performance, LSE, Stagnation nation: Navigating a route to a fairer and more prosperous Britain, Resolution Foundation, July 2022.

Section 5

Conclusion and recommendations

This report has combined our usual projections on living standards, income and poverty with results from a survey we commissioned from YouGov of 10,000 adults in the UK, that was in the field in late November 2022, looking at how the UK is coping with the cost of living crisis.

2022 was a calamitous year for households, but there is more to come in 2023, and living standards may not reach their pre-pandemic levels until after 2027

Our survey has highlighted that almost everyone is feeling the impact of higher prices, leading around four-in-five adults to say that they are trying to cut back, but that the impact of higher prices is almost always worse for those on lower incomes. This should not come as a surprise – those goods and services seeing the fastest price rises make up a higher fraction of the budget of low-income households, meaning they have less slack; energy and food are essential, meaning it's harder to cut back; and low-income families tend to have fewer savings to draw down. But the weight of evidence is telling, with low-income families more likely than those on higher incomes to have to cut back severely, be unable to afford essentials, to not have enough money to buy food, and to miss paying key bills. And the choices made by families under pressure are, in some cases, reducing their future financial resilience (by increasing debt or reducing savings) or having impacts on their mental or physical health: even if the crisis ended today, the adverse impacts of the crisis, and the unequal impacts it has, would persist.

These survey findings show that 2022 was indeed a truly horrendous year for household living standards, with the OBR predicting that real disposable incomes fell by the biggest single-year fall in a century. 2023 should, though, see the back of double-digit inflation, as international energy and goods price pressures ease.[71] Given that inflation expectations seem not to be rising, and with the prospect of a cooling labour market domestically, this may make for an easier year ahead for policy makers in the Bank of England. But our

71 T Bell, New Year's Outlook 2023: They think it's all over... it isn't now, Resolution Foundation, December 2022.

forecasts show that for households, 2023-24 looks likely to be worse than 2022-23. Many low-income families and low-paid workers will be helped by most state benefits and the National Living Wage rising by around 10 per cent next April. But offsetting this will be a rise in energy bills – even if international gas prices fall, as predicted – as the price cap is lifted and government support is scaled back, shrinking pay packets with real wages remaining below current levels well into 2024, tax rises amounting to £700 for a typical household, and around 2 million households moving onto more expensive mortgages.

As a result, we forecast that typical incomes among non-pensioners are set to fall by 3 per cent in 2022-23, and 4 per cent in 2023-24, with this two-year fall of 7 per cent (or £2,100 for a typical household) being larger than in the Financial Crisis, where there was a 2-year decline of 5 per cent. The extensive government intervention in both years, combined with the 10 per cent rise in benefits and pensions in April 2023, mean that income falls are larger at the top of the distribution. But much of this relative protection of low-income households disappears when we consider that the items rising fastest in price make up more of the budgets of low-income households.

This precipitous decline will take typical incomes in 2023-24 to where they were in 2018-19 – and would mean that this becomes the worst Parliament on record for living standards for almost all parts of the income distribution. Although incomes should start growing in 2024-25, typical incomes are set to be below their pre-pandemic (2019-20) level in 2027-28.

Government should take action to help households through this winter and the next, but also work towards securing better long-term economic growth

Our findings point to several areas where Government action can make a difference in the short-term.

- The fact that wholesale gas prices have now fallen, while retail energy prices households face are set to rise, means there is likely to be a renewed debate about the level of the Energy Price Guarantee and whether it should rise above its current £2,500 level in April. Looking further ahead, the Government is currently considering how to support households with energy bills from April 2024, when the Energy Price Guarantee is due to end. [72] It is welcome this includes considering the practicalities of a social tariff, which offers the only route to being able to target support at a wider range of lower-income households than those claiming benefits and to recognise big differences in energy needs between households. [73] It goes without saying that in the medium-run, better insulation is key to reducing household

72 HM Treasury, Autumn Statement 2022, November 2022.
73 M Brewer et al, A chilling crisis: Policy options to deal with soaring energy prices, Resolution Foundation, August 2022.

energy bills and easing the transition to net zero. Both main political parties are now saying this is a key priority, with a recent report from the Resolution Foundation suggesting that turning that rhetoric into reality will require a greater focus on the most difficult part of the challenge: UK's homes inefficient walls.[74]

- For 2023-24, the Government has decided to focus its cost of living support for households on those receiving social security benefits. This makes it more important than ever that those entitled to those benefits claim them – there are 850,000 adults going without Pension Credit, for example – and the Government (and other organisations) should be doing what it can to boost awareness and encourage take-up of means-tested and disability benefits.[75]
- The social security system is good at identifying which families have low resources, but does not assess who has the greatest energy need. That is one reason why local discretionary schemes have an important role to play. But the fact that as many as one-in-four local authorities in England do not provide crisis support as part of their schemes is of real concern, leaving the most vulnerable individuals and families to fall back on charitable provision.[76] The UK Government should mandate a minimum provision of crisis and relocation support by local authorities, if necessary with ring-fenced funding. But the Government should avoid setting targets on (for example) what proportion of support should be allocated to a certain demographic group, as these reduce local authorities' ability to target help where it is needed (and, in some cases, just turn what is supposed to be discretionary support into a top-up to entitlement-based social security, but with greater administrative costs).
- A major driver of the cost of living pressure is coming from higher energy bills, and we are not yet through winter 2022. Outside of Scotland, there is already a programme that households do not need to claim, and that is automatically targeted to those on a low income and to areas that are experiencing cold winters: Cold Weather Payments.[77] These payments could play a more useful role in protecting households from the worse impacts of winter if the trigger temperature was raised so that they are paid more often (they are currently triggered automatically when the average temperature for a week is below 0 degrees, which is not a common occurrence), and if eligibility was widened to more working-age households that receive benefits.[78]

74 A Anis-Alavi et al, Hitting a brick wall: How the UK can upgrade its housing stock to reduce energy bills and cut carbon, Resolution Foundation, December 2022.
75 DWP, Income-related benefits: Estimates of take-up: financial year 2019 to 2020, 24 February 2022. There are no official estimates of how many people are not receiving UC despite being entitled.
76 K Handscomb, Sticking Plasters: An assessment of discretionary welfare support, Resolution Foundation, October 2022.
77 In Scotland, a payment of £50 is made automatically every February to all entitled families.
78 Eligibility is limited to those receiving Pension Credit (any kind), plus working-age families where no one is in work and that contain a child under five or someone in the family with a disability, or that contain a child with a disability (regardless of the parents' work status). See: https://www.gov.uk/cold-weather-payment/eligibility.

- Our survey shows that food insecurity is much worse for families with three or more children, and our forecasts show that rising relative child poverty from 2024 is driven entirely by families with three or more children. In the short-run, it is unfortunate that the same-sized Cost of Living Payments are being made to all recipients of Universal Credit (and other benefits) regardless of whether this is a single person or a family of five or more: varying the payments by family size would have allowed them to match energy need more closely.[79] In the medium-run, the diverging poverty rates of children in families with one or two children with those in families with three or more is in part down to the combined effect of the two-child limit, the benefit cap (this is being increased by inflation from April 2023, the first nominal increase since its introduction in 2013), and the post-pandemic freeze in LHA rates. All of these policies should be reviewed.
- Stepping back, it is clear that, since 2019-20, two major economic crises have combined with the UK's long-standing weakness in productivity to create eight wasted years for household living standards. With the Covid-19 pandemic and the current cost of living crisis coming after a fifteen-year period characterised by low growth and high inequality, there is a real risk that the UK is cemented as a stagnation nation. Measures that could help solve those fundamental weaknesses of the UK economy are the subject of our ongoing project with the Centre for Economic Performance at the London School of Economics; this work will conclude in late 2023.

79 M Brewer et al, A chilling crisis: Policy options to deal with soaring energy prices, Resolution Foundation, August 2022.

Annex 1

Nowcasting and forecasting methodology

As set out in this paper, there are many factors that influence household disposable incomes and therefore need to be modelled when 'casting forward' existing household income data (DWP's Family Resources Survey/Households Below Average Income, 2019-20) to the years from 2020-21 through to 2027-28. Our approach for projections is as follows.

Projecting underlying demographic change

Part of our forecasting relies on simply altering the composition of the population in the data, in line with actual or projected changes.[80]

- We reweight the population to match ONS forecasts for **demographic change** by age and gender.[81] This includes modelling changes in the numbers of **dependent children** of each age.
- We adjust the overall labour force **participation rate** using the OBR's November Economic and Fiscal Outlook.[82]
- The proportion of women aged 70+ who have **private pension income** is also adjusted each year, rising in line with past Family Resources Survey trends (note that there has been broadly no change among men).
- We do not account for changes in **migration patterns** (beyond overall demographics and participation), or **housing tenure** (which we hold constant over time), or any shifts in the number of people living with their parents –though all of these may have had important impacts on household incomes since the start of the Covid-19 pandemic.

Market incomes

Projecting wages and other forms of market income into the present and future is a key part of our modelling, and is done largely through the IPPR Tax Benefit Model.

80 We primarily do this using the 'reweight2' command in Stata: see J Browne, Reweight2: Stata module to reweight survey data to user-defined control totals, IFS, July 2012.
81 ONS, National population projections: 2020-based interim, January 2022.
82 OBR, Economic and Fiscal Outlook, November 2022.

- Given that **unemployment** is higher in most of our projection years than in 2019-20, according to the OBR's forecast, we 'make' an additional fraction of employed survey observations unemployed. This is done randomly within private sector earnings quintiles, with larger changes for lower earners (based on analysis of Understanding Society data).

- For 2020-21 and 2021-22 we model **furlough**, using figures on the overall (average) number of people furloughed, and an assumption that 30 per cent of these were actually furloughed on full-pay.

- We do not attempt to incorporate the significant decline that has taken place in **self-employment** relative to the number of employees, partly as some of this apparent shift is likely about recategorisation in response to IR35 policy changes.

- In every year, we model the **wage floor**: ensuring that no-one in our data falls below their age-appropriate minimum wage, based on OBR figures. We include some 'spill-over effect' for those just above the wage floor. We also model the extension of the National Living Wage from age 25 to ages 24 and 23 in 2021-22; and ages 22 and 21 in 2024-25.

- Beyond these changes, all employee and self-employed **earnings** are uprated equally in each year. Overall wage growth is constrained to match OBR figures, taking into account the effects of the wage floor, furloughing and compositional changes.

- **Private pension incomes** are uprated using the previous September's RPI inflation, based on the last OBR forecasts (but see also: Projecting underlying demographic change, above). For 2023-24, average earnings growth is used instead given extremely high RPI inflation.

- **Income from savings, dividends and property** are uprated by the OBR's forecasts, with adjustments to account for adult population growth.[83] These forecasts are discussed further in Box 6.

- **Private pension contributions** are increased in line with average earnings. We assume no changes to auto-enrolment after 2019-20, despite a Government commitment to implement reforms that would increase contributions for some people in the 'mid-2020s'.[84]

83 See OBR, Forecast of income streams subject to self-assessment income tax consistent with the March 2022 Economic and fiscal outlook (EFO), September 2022.
84 G Opperman, House of Commons Written Questions, 21 September 2021.

- We do not model **student loan repayments** (which are deducted from disposable income in HBAI). As graduates making substantial repayments become a larger fraction of the population, this will weigh on income growth, as will planned policies such as freezing or cutting repayment thresholds.

Projecting prices and housing spending

As our focus is on real disposable incomes, after housing costs, we must also account for changes in prices and housing costs.

- Our starting point in accounting for **inflation** is the OBR's November 2022 CPI forecast. However, we create a specific deflator for 'after housing costs' income, in line with DWP definitions. This removes any housing costs from CPI, in order to avoid double-counting their impact. In this calculation we make use of the OBR's actual rents forecast.
- In Box 7, we show the effect of using forecasts for **differential inflation** to adjust our distributional income growth forecasts. To create these forecasts, we used the Living Costs and Food Survey to calculate a (CPI-consistent) share of consumption on household gas and electricity bills. This is done for people aged between 18 and 65 and split by household equivalised income vigintile (after housing costs). We then combined that with the forecast for energy prices (the EPG) to obtain a contribution from energy for each vigintile, which was then translated relative to all households. This created a percentage that we added to the OBR headline CPI rate of inflation to get an electricity and gas bill-adjusted inflation rate for each vigintile.
- **Mortgage interest costs** are uprated uniformly using OBR projections.
- **Private rents** are assumed to rise in line with average earnings in future, matching the OBR's assumption. Ground rents and service charges are assumed to do the same. The ONS's Index of Private Housing Rental Prices is used in our nowcasting, but no regional variation in price changes is assumed beyond November 2022.
- **Social rents** are uprated based on the OBR's inflation forecast and the CPI + 1 per cent policy, except in 2023-24, where social rent rises in England will be capped by the government at 7 per cent,[85] and in 2024-25, where we assumed the same policy will apply, as the usual CPI + 1 per cent formula would result in an increase of 7.9 per cent otherwise.
- **Other housing costs** (including home insurance and water supply) are uprated using the OBR's CPI forecast.

85 See HM Treasury, Autumn Statement 2022 Policy Costings, November 2022.

Modelling taxes and benefits

We model the tax and benefit system in future years using stated government policy (e.g. 2023-24 benefit rates) and default policy (e.g. CPI uprating in many cases). But there are a number of choices to note:

- We model a mix of **UC** and legacy benefit systems, with our assumptions about the speed of the roll-out estimated using DWP projections and other figures. We assume that full roll-out of UC is not completed until 2026-27.
- We model incomplete **take-up** of the main means-tested benefits. For example, we assume 63 per cent take-up of Pension Credit, and 86 per cent take-up of UC. We assume for simplicity that these figures do not change between years.
- The **two-child limit** is applied to children born from April 2017 onwards, and so affects a growing proportion of the caseload each year. The abolition of the family element of Tax Credits and UC works in the same way.
- The change in the eligibility of mixed-age couples for **Pension Credit** in 2019 – with newly-claiming mixed-age couples now receiving (less generous) UC instead, but existing claims protected – is not modelled. We instead use the new eligibility rules for everyone, in every year.
- The replacement of Disability Living Allowance with **Personal Independence Payments** is not modelled.
- The introduction of the new **State Pension** for younger cohorts is modelled.
- We model the new means-testing of **free TV licenses** for those over the age of 75 (as this forms part of the DWP's household income definition), and assume this applies for the whole of 2020-21 onwards.
- **Council Tax i**s assumed to rise in line with OBR forecasts by nation, but as projections were not released in November 2022 we make an adjustment to reflect Autumn Statement 2022's changes to English Council Tax policy. Detailed changes to Council Tax Support by nation and local authority are not modelled.

- We model an extra £400 Energy Bills Rebate payment for every household in 2022-23, and another £150 for everyone in Council Tax bands A-D, including households in Northern Ireland, and £650 Cost of Living Payments for those on means-tested benefits, £150 for individuals on disability benefits, and £300 for pensioners. In 2023-24, we model £900 Cost of Living Payments for those on means-tested benefits, £150 for individuals on disability benefits, and £300 for pensioners. We do not model the effects of the Energy Price Guarantee; its impact is captured in the ONS's estimates of (and in the OBR's forecasts of) the CPI.[86]
- There are a number of Scottish policy differences that we do not model, such as the Best Start Grant and increased Carer's Allowance. The **Scottish Child Payment** is modelled, with partial take-up.
- There were a number of benefit changes within the financial year **2021-22**. For our full 2021-22 figures, we use the average benefit rates across the year. For example, the UC taper rate is modelled as around 60 per cent; rather than either 63 (until November) or 55 per cent (from December). We also model the suspension of the Minimum Income Floor and extra Council Tax Support as being partially in place in 2021-22.
- We are not able to model the effects of **benefit sanctions**, which were temporarily suspended during the pandemic.

Projecting changes rather than levels

Using all of the above, we model incomes in the years 2019-20 through to 2027-28 However, as our modelled estimates can systematically differ from survey data – e.g. due to survey data underestimating benefit incomes – we apply income growth rates (and absolute changes in poverty and inequality metrics) from our modelling to the 2019-20 outturn data, rather than directly using the projected levels.

Scenarios

In addition to our main projection, we also look at two different economic scenarios for income growth:

1. Nominal wage growth being one percentage point higher each financial year from 2022-23 to 2027-28.
2. Nominal wage growth being one percentage point lower each financial year from 2022-23 to 2027-28.

86 The OBR's report accompanying the Autumn Statement says that their projections include a slightly different version of the final Energy Price Guarantee policy, but that including the final policy would only have made a small difference to their inflation forecasts. See Office for Budget Responsibility, Economic and Fiscal Outlook, November 2022.

Annex 2

Table of projections

For ease of reference, Table 2 sets out our headline results, as well as many of the key inputs we have used and the alternative scenarios that we discuss.

It should be noted that our projections are primarily based on the latest OBR forecasts at the time of writing, but these forecasts will change.

Furthermore, we are not attempting to predict what survey data such as DWP's HBAI will show: these (invaluable) official results come with large margins of error and their own biases. Indeed, in this year's Outlook, we have continued to use the FRS's 2019-20 data as the base for our modelling, due to the effect of the Covid-19 pandemic on the quality and sample size of the 2020-21 data.[87] Most of the single year changes we project will not be able to be confirmed by the survey data to within 95 per cent confidence, even if the underlying economic forecasts and policy assumptions proved to be spot on. We hope that nowcasting and forecasting provide useful indicators of what is happening to living standards and inequalities, far in advance of outturn survey data becoming available.

87 Department for Work and Pensions, Technical report: assessment of the impact of COVID-19 on the HBAI statistics for FYE2021, May 2022.

TABLE 2: **Key inputs and outputs from our living standards projections**

	2019-20	2020-21	2021-22	2022-23	2023-24	2024-25	2025-26	2026-27	2027-28	Primary source for projection
Annual changes in economic determinants										
Av. earnings (& private rents from 2022)		2.2%	6.6%	5.6%	3.5%	1.6%	1.7%	2.1%	2.7%	OBR
Higher earnings growth scenario				*6.6%*	*4.5%*	*2.6%*	*2.7%*	*3.1%*	*3.7%*	*RF scenario*
Lower earnings growth scenario				*4.6%*	*2.5%*	*0.6%*	*0.7%*	*1.1%*	*1.7%*	*RF scenario*
National Living Wage		6.2%	2.2%	6.6%	9.7%	6.1%	1.6%	1.7%	1.9%	OBR/LPC/RF Calculations
Dividend income		-6.2%	12.2%	8.8%	-3.8%	2.7%	3.5%	4.7%	3.8%	OBR NGDP/person
Main benefit uprating		1.7%	0.5%	3.1%	10.1%	6.9%	0.0%	0.0%	0.9%	Based on OBR
Unemployment rate, 16+, ppts		+0.9%	-0.6%	-0.6%	+0.7%	+0.6%	-0.3%	-0.4%	-0.1%	OBR
Participation rate, 16+, ppts		-0.7%	-0.2%	-0.1%	-0.0%	-0.0%	-0.0%	+0.0%	-0.0%	OBR
CPI		1.7%	0.6%	4.0%	10.1%	5.5%	0.0%	-1.0%	0.8%	OBR
CPI excluding all housing costs		0.5%	4.2%	10.8%	5.6%	-0.3%	-1.3%	0.8%	1.9%	Derived from OBR
Mortgage interest payments		-7.2%	0.3%	42.1%	66.9%	12.1%	-0.8%	-0.1%	-0.3%	OBR
RF Projected changes (after housing cost measures)										
Real non-pensioner median h'h' income		+0.6%	+1.2%	-2.9%	-4.3%	+1.3%	+2.8%	+0.9%	+0.3%	
Relative poverty (all), ppts		-1.6%	+1.4%	-0.7%	-1.0%	+0.6%	+0.1%	+0.4%	+0.3%	
Relative poverty (child), ppts		-2.8%	+2.4%	-0.1%	-1.3%	+0.8%	+0.7%	+1.3%	+0.8%	
Absolute poverty (all), ppts		-1.9%	+1.3%	+0.5%	+0.6%	-0.4%	-0.7%	-0.0%	+0.1%	
Absolute poverty (child), ppts		-3.1%	+2.2%	+1.6%	+1.3%	-0.6%	-0.5%	+0.3%	+0.5%	
Gini coefficient, ppts		-1.3%	+1.0%	+0.3%	+0.8%	+0.6%	+0.1%	+0.1%	+0.2%	
90:10 ratio		-0.37	+0.30	-0.18	-0.12	+0.14	+0.04	+0.04	+0.06	
RF Projected levels (based on 2019-20 DWP figures)										
Real non-pensioner median h'h' income	£29.1k	£29.3k	£29.6k	£28.8k	£27.5k	£27.9k	£28.7k	£29.0k	£29.0k	
Relative poverty (all)	22.0%	20.4%	21.8%	21.1%	20.2%	20.8%	20.9%	21.3%	21.6%	
Relative poverty (child)	30.6%	27.8%	30.2%	30.1%	28.8%	29.6%	30.3%	31.6%	32.5%	
Absolute poverty (all)	17.9%	15.9%	17.2%	17.7%	18.3%	17.9%	17.3%	17.3%	17.4%	
Absolute poverty (child)	24.8%	21.7%	23.9%	25.6%	26.8%	26.2%	25.8%	26.1%	26.5%	
Gini coefficient	39.0%	37.7%	38.7%	39.0%	39.8%	40.4%	40.5%	40.6%	40.8%	
90:10 ratio	5.16	4.79	5.09	4.91	4.79	4.93	4.97	5.01	5.08	

NOTES: Although outturn household income figures are available for 2020-21, the figures shown here are our nowcasts, for consistency with later years. RF projections include use of the IPPR Tax Benefit Model. Real household income figures are in 2022-23 prices.

The Resolution Foundation is an independent research and policy organisation. Our goal is to improve the lives of people with low to middle incomes by delivering change in areas where they are currently disadvantaged.

We do this by undertaking research and analysis to understand the challenges facing people on a low to middle income, developing practical and effective policy proposals; and engaging with policy makers and stakeholders to influence decision-making and bring about change.

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