Chris Coates 0:07
Hello, and welcome to insights, a podcast from Understanding Society. The study that captures life in the UK in the 21st century, Understanding Society is a longitudinal survey. Every year we ask each member of 1000s of the same households across the UK about different aspects of their life. In each episode of this series, we're exploring how our data has been used in a key area. We'll look at what we found, what it tells us, and what we can learn from it. I'm your host, Chris Coats. And in this episode, we're looking at cost of living, who has been hit hardest? And what can government do about it? Here to discuss this are Hamish Low, the James Meade Professor of Economics at the University of Oxford, and Rebecca McDonald, the chief economist of the Joseph Rowntree Foundation, which works to solve poverty in the UK. Hamish, can we start by putting the crisis in context, you've used Understanding Society data to look at inequality during COVID, what's been the pattern there and who's been affected the most,

Hamish Low 1:06
Maybe I should start by saying just a little bit about what we did. So to understand society, it followed the same people through the first 18 months of the pandemic. So we were able to see how those individuals were affected by what happened. And in addition to that, we knew what the situation was going into the pandemic. So that's where I think it was quite a unique opportunity to see how the crisis affected people, and then to see how they were able to cope with it. I think that the most striking things about the patterns that came out was that there was a big difference between the initial impacts and what happened subsequently. And one of my key takeaways was people learn to adapt fairly quickly. So let me give you an example of that. So one example is, when the pandemic first hit, there's a lot of discussion about how, obviously, there was a big first lockdown, and the number of the people aged 20 to 29, a lot of them became unemployed, they weren't protected much at all, by the second lockdown that they completely bounced back. And so we saw that there was a lot of recovery happening. And part of the reason for that was because people were able to switch industry. And I think what one things I would say about it was that although some people were switching Industries, a lot of people who were not switching industry were those who were protected by the furlough scheme. So we saw differences across different sectors of the population into how they adapted to the ongoing pandemic. So some people bouncing back very quickly, other people remaining with very little labour market engagement for for a longer period of time. So I think that was the kind of broad pattern between what happened initially and then what happened longer term. And a lot of that was tied into what sort of other protection people had from the government or from elsewhere. The other thing that I think it's worth distinguishing is between what happened to earnings, or to income, and what happened to labour markets. So there was a lot of damage done to labour markets because of the lock downs. But for a lot of people, incomes were actually protected. And we see that in terms of the data, there's big distinction between people who are no longer working, but their earnings held up a bit and their incomes held up too.

Chris Coates 3:04
Okay, so essentially, what you're saying is you saw that furlough was working because people weren't working, but they were they weren't running out of money either.

Hamish Low 3:11
I think that's right, I think across the distribution, furlough worked very effectively for as middle-income groups. So there was a lot of people in the middle income deciles of the distribution, the middle the distribution, who ended up seeing that the earnings were actually maintained, they didn't lose earnings, despite the fact that they were no longer working hours, working positive hours, at all, at the top of the distribution, people lost out partly because the photo scheme was capped, and quite possibly rightly capped at £2,500. But that cap meant that they were losing money. Of course, they had more mechanisms to insure themselves through savings. And the bottom of the distribution. There was less use of the furlough scheme and a larger fraction of people actually became unemployed as a result of the shocks. And the protection there I think was happening more because of Universal Credit. And we see that in terms of incomes being protected, despite the fact that earnings were falling and labour markets are falling.

Chris Coates 4:09
Okay, so it looks like it's generally true that middle income and more affluent people did okay. But did people on lower incomes suffered disproportionately?

Hamish Low 4:19
They didn't suffer disproportionately in our data. But what I'm saying there is the people lost their jobs. But what happened their living standards was they weren't significantly worse off than the middle-income groups. And to us, this was a bit of a puzzle, because we saw the labour market impacts. We saw people becoming unemployed more in those lower groups and in middle income groups, but we didn't see them in terms of the incomes being much worse off. And it's partly because there's lower income groups, the levels that they're working on, much lower to start with, and so people are not working as much, then they're not going to be affected as much by workplace shutdown, and the benefit system continues to function. So I think that's part of the story, which explains why the incomes that people are bottom were not as badly impacted, as we'd expected, looking just at labour markets,

Chris Coates 5:12
I mean, you've looked at the whole period of COVID, of certainly the first two years with our data. And I think one of the things you said was that later lockdowns didn't affect earnings as much because people were able to work, but there weren't as many opportunities for spending. So some people were able to save, again, is that something that affects the wealthier and the middle income people, they're more able to save?

Hamish Low 5:32
So I think just to kind of sort of tease out a little bit is this big contrast between what was going on first and second, or the first lockdown and then essentially the major lockdown that third lockdown, in the third lockdown firms had adapted to how they were working. So you see that, for instance, in manufacturing, you saw this kind of substantial fall in the amount of work that was going on that first lockdown by January, February 2021, there was very little fall happening in manufacturing. So I think that was a sign that the firms have adapted. And as a consequence of that there were fewer people on furlough. And in addition to that, that meant then earnings per then kept up. I think what's interesting is thinking about what happened to spending, in that you can think that spending might be

restricted, or might be lower, because people are, I've got new opportunities to spend, or because they're worried about the future. And I think particularly that in the later lockdowns, because incomes were still maintained, earnings was still maintained. But the opportunity to spend were substantially reduced, we saw these big increases in saving. And those increases in savings led to big increases in wealth across the distribution. The exception was in the kind of bottom third of the distribution, the bottom third of the distribution, were very much consuming their incomes, and there was no change in their savings rate. But for the top two thirds, the distribution, you see these increases in wealth. And you see this, this build-up of resources which happen. And I think part of what that did was it generated pent up demand, which then was coming through later on in 2021. And the start of 2022. On the other hand, you could think that the fact that all those extra savings been built up, would have meant that people had more of a buffer going into what's happening now.

Chris Coates 7:13
And early on in the pandemic, how were people on lower incomes coping with the changes that were happening? Were they able to take out loans? How did they cope?

Hamish Low 7:22
There's a couple of things to kind of stress here. What is the thing, people the bottom third, the distribution, there's a lot of differences across different people. So you did see sizable numbers of people increase the amount of debt that we're taking out. And that's correlated with how big impacts that were on their incomes, there are other people whose debt declined. But I think the main message is that the was the increase in debt at the bottom, which we didn't see further up the distribution was the increase in debt, there was an increase in transfers between family and friends. So think about what are the kind of mechanisms to mitigate these shocks. Debt was one of them, transfer some family and friends was another, particularly in early stages. And the increase in Universal Credit was similarly important. I think as time went by, we see less evidence for those transfers taking place, and more evidence in terms of Universal Credit. The only encouraging thing we did see was that the increase in debt that happened at the start the pandemic, but we didn't see that continue as the pandemic went on. Of course, that could be because people didn't have the opportunities to borrow more at that stage.

Chris Coates 8:24
One of the question did you notice much difference in terms of gender split, were women more effective than men or vice versa?

Hamish Low 8:31
In the UK, we didn't. And the reason why I'm specifying UK is because one of the striking things about the US was the was this big gender split. And we were expecting to see that in the UK as well. But the path of labour market outcomes for men and women, how they felt the start the pandemic, how they recovered, and how they've evolved over time, they were basically moving in parallel. So the was no difference between men and women in terms of labour market outcomes. The interesting thing, looking at it in a bit more detail was the share of women who are working in particular sectors is very different. So in some sectors like hospitality, there's a large share of women who work when compared to men, and the

hospitality was very badly affected. So that would mean you'd expect women to be more affected than men by the pandemic. On the other hand, the share of women working in education and working in in healthcare is way higher than it is for men. And in those industries, there was no decline at all. So I think that's part of what was going on. We saw this, where these differences across industries and how big the declines were. So some industries where they were heavily affected, other industries they were not affected at all. And so the bottom line was, there was no difference between men and women. And what we found. The only place we see a little bit of a difference is once we condition or when we look at within an industry and comparing between women who've got children at home, and men who've got children at home, and then we see a slight difference. But even then the main takeaway for us was, there's no real difference between men and women. I think what that potentially hides is, what the kind of long-term implications are of things like home-schooling, and who bore the responsibility for looking after children while keeping up their jobs. And I think that's something which we don't know enough about. Yet, there is some initial evidence that women were more involved in home-schooling than men through the pandemic. And that may have had implications in the long run. We can't tell that long run yet. But just in terms of thinking about the data, it is one of the nice things about the data themselves society data in that those same people we solve for the pandemic, keep on getting followed through. So we'll see what happens to them each year for the next hopefully, decades, and be able to see the long term implications.

Chris Coates 10:42
Rebecca, can I turn to you how of the last two or three years fed into where we are now? Can you talk us through that a bit?

Rebecca McDonald 10:48
Yes, of course, so I think how the last couple of years or so have fared is is incredibly important when we then think about how in particular low-income families are faring at the moment when they're facing very high levels of inflation. And of course, when energy bills have been going up a lot, both in terms of the last couple of years and COVID. And obviously all of the different effects that Hamish was talking about from his research. And in particular, I think the rise in debt is an important one to mention. Our survey of low-income households from October 2021 found that 4.4 million families who fall within the kind of bottom 40% of household income had had to take on new or extra borrowing during the pandemic, which kind of agrees with the findings, Hamish was talking about earlier. And that highlights that even though in some ways, low-income families experience that the pandemic wasn't worse than other families, and they weren't necessarily disproportionately worse affected. But there was because of the scale of this shock and some of the other factors going on, there was still an increase in borrowing. And I think it will have had a kind of toll on people's finances. That meant that when they then experienced high inflation at the moment, they were starting from a slightly weaker position. But I also think it's important to look further back and not just to talk about the context of COVID. But actually to look at the position for many of these low income families in 2019, or the beginning of 2020, when the pandemic then hit, and the fact that for many of these families in the UK, poverty was already a daily part of their lives, we know that there have been kind of persistently significant poverty rates in the UK over the last couple of decades. And while they hadn't really increased the relative poverty line rate that is hadn't really increased.

Beneath that there were worrying trends. So for example, we know that there was a deepening of poverty, so families were falling further below the poverty line. And we also know there was a rise in destitution. So in terms of people who are at that very, very sharp end of poverty, and lacking basic aspects of life, like housing, or clothing, or food, there was a 50% rise in destitution between 2017 and 2019. Meaning that by the time we got to just before the pandemic, there were around 2.4 million people who'd experienced destitution at some point that year. So this kind of paints a picture of the fact that even before the first of these two kind of very significant economic shocks, even as we came into these, for many families, across the country, on low incomes, their financial situation was already very difficult. They were already struggling, many of them to afford all of the essentials and are unable to have a decent quality of life. And that was the situation within which they then had to face, you know, high levels of inflation and energy bills going up. And I think that's really important when we then look at, and we try and understand why this period has been so difficult for many of those families and, and why it's warranted such a bold government intervention.

Chris Coates 14:00
So what are we looking at now in terms of energy bills, who is being affected most now?

Rebecca McDonald 14:05
Yeah. So the kind of simple point, I guess, to make at the beginning of this is that, you know, if your energy bills take up a bigger share of your budget, then it's much more difficult to handle the increases in energy bills that are happening at the moment. Sounds like a very obvious point. But when we look at low-income families, and we look at their budgets last year, so before this April, before some of the biggest increases in energy bills, we know that for households in the bottom fifth by incomes, roughly about 12% of their disposable income was taken up by energy bills, and for households in the middle quintile by income that was 4%. So you can see that they came into this period of energy bill increases with very different amounts of kind of vulnerability to energy bills going up. Then when we saw energy bills rise this year, obviously, it's been harder for those lower incomes to adjust to the rises. So even if some households because of their various usage or the type of building they're in, have seen similar increases in their bills, the way in which they're able to adjust and account for that in their budgets is very different depending on whether it takes up 12% or 4% of their budgets. What we've done is we've tried to map how that share of budgets has changed throughout this period of rising energy bills. And if we look at this financial year, so from April, earlier this year to next April, and we account for the various different support packages that have been put in place by the government, and now also the energy price guarantee, we think that probably over this financial year for that bottom quintile of households, the budget taken up by energy will increase to 16%, from 12%. And for middle income households, it will rise to 6%. And obviously, that is still an increase, but it's reduced quite far from what we would have expected had there not been an energy price guarantee. And then if we look ahead to next year, so from next April onwards, the figures for next year were due to be very, very bad for low-income households, we were expecting about half of their budgets to be taken up by energy bills. Now, thanks to the guarantee, that will fall down to 20%. So there's a kind of two parts of the story. On the one hand, the government support is making a very big difference to what would have been horrendous, and that's a people's budgets taken up by energy. But on the flip side, we're still seeing an increase. And

you know, for a family who are on a low income, having a fifth of their disposable income taken up just by energy will be difficult to manage even so.

Hamish Low 16:31
Could I come in and just ask? So if I think about how the energy price increases are going to impact people further up the distribution; in a way it's going to benefit them. Because the rise in energy price use means demand for other goods is going to fall, which will drive prices down on goods, such as eating out and so on. So will that benefit people further up the distribution by more in some senses when we think about the cost people the bottom, but it feels very redistributive? And I wonder if there's just something you had on that?

Rebecca McDonald 16:59
Yes, I think that's a great point. I don't have fingers on that. But I agree with you, I think there will be interesting dynamics there. And I think, to some extent, people on middle and in particular, people on high incomes, I would say will benefit to some extent from some of these changes. The reason I specify high incomes is because I think for many families on middle incomes, because the extent and the scale of bill increases, next year, if there hadn't been the Price Guarantee was so huge, I actually do think that was probably a kind of clear rationale for also giving them some kind of shield and protection from energy bill rises, because even though it might not have led them to, you know, not be able to afford food, it would have probably required a very significant adjustment in their budgets to afford such huge increases in energy. But for those on high incomes, you know, those huge increases may well have been affordable. And now there's more of a kind of political point as to whether you want people to have to pay those huge bills. But given that they probably would have been affordable, they would have adjusted by cutting back on luxuries. There is a very kind of interesting question about whether going universal in that policy choice was the right thing. And whether the gains and the I guess the savings that those high-income households will have in relation to what would have happened otherwise, whether that was kind of the right decision or whether that's fair.

Hamish Low 18:17
So just one other related that is that the protection is all here in terms of households. And I guess the price of a lot of goods will go up if the they're very energy intensive. So when you have some of the the extra cost is that's just the extra costs directly for energy is not allowing for the costs of increases in other goods, which are using energy in that production.

Rebecca McDonald 18:37
Yes, exactly. So this modelling in particular, or this analysis, just looks at energy bills, and looks at the Ofgem price gap that was forecast for next year before the price guarantee, as you say, of course, those higher energy bills would have fed through into broader inflation, we are using forecasts for inflation for next year. Now, I think that because things are changing so rapidly, those forecasts, as you say, probably don't account for the full extent of those energy costs feeding through to other goods and services. So it may well be that actually there are other impacts that are not fully accounted for and maybe underestimated in this. And we'll just have to see how much those kinds of inflationary pressures are reduced by the price guarantee, because of course, now that there will be support for businesses too at least over the next six months, that may help reduce some of that pass

through into the cost of goods and services. But I'm not sure how significant that will be and how much of future inflation and other goods and services that will manage to limit.

Chris Coates 19:39
Rebecca, can I ask you a quick follow up? You were talking just then about the difference between a universal approach and presumably a more targeted approach by the government. And I just wondered if could you expand on whether Joseph Rowntree Foundation were hoping for something different from the government because you've said it's helping somewhat. Were you hoping for specific different things that might have done more?

Rebecca McDonald 20:02
Yeah, so I think the benefit of what's been announced is that it does a significant amount for low-income households in terms of preventing their energy bills going up further during this financial year. Now the choice to go universal, it's tricky, because I think on the one hand, I don't really mind because as long as the policy protects those who need the support the most, then that is sufficient. If you know, politically, they've chosen to also give that support to all households, then it doesn't take away from what low-income households receive, and they're still getting what they need in terms of energy protection. However, two kind of caveats on that, firstly, it does worry me around the universality means it's a very expensive policy, of course, now, if the fact that the government has gone universal and spent a lot of money on the price guarantee means that they will have to cut back elsewhere, then I would start to worry about the kind of trade-offs there. So for example, if it means that public spending has to either be cut or cannot increase sufficiently to kind of allow public services to be delivered to a quality level, given the high increases in costs and things that they're facing, or if it meant that very, very urgently needed investment in benefits and social security in the longer term is no longer or is less feasible as a result, then I'd be very worried about that trade off. And the fact that we've chosen a universal and very expensive policy, at the expense of some of these very important longer-term changes. The second caveat being that while this policy choice does enough to prevent energy bills, in particular, going up further this year, there is still a shortfall for families, particularly those who are in the bottom fifth by incomes. And those who are receiving means tested benefits, the extra costs that they face across this financial year in particular, are still higher than the extra income and support that they've been receiving. And so they are still going to be worse off and given the situation they came into this position in. I don't think that's feasible for many of them, and is incredibly difficult for them to manage. So the Joseph Rowntree relation was asking for additional support. And I do think that over this winter, I think the government probably thinks its job is done in terms of cost of living just for the next six months. But actually, for those are low-income families, I think there is a very urgent need for either an additional payment, or bringing forward the upgrading and increase in benefits that's due next April, because there is still a kind of chunk of money that people are going to need to find over the winter, to keep their quality of life constant, that's going to be very difficult to find.

Chris Coates 22:41
Can I just ask what sort of things come in there in that this kind of suppression of the price of energy, are you worried there's going to be an impact on rationing? And in a way, we've

got a number of different countries which are trying to cap energy prices. Presumably prices were rising to start with because there was under supply? So is there a concern now there'd be rationing and how that will play out?

Rebecca McDonald 23:01
Yes, no, I agree with you. And I'd be very interested to know the answer to that. But I myself don't know how it will work. If there is a kind of shortage of energy. I don't know what that is a real risk or not this winter. It reminds me of the discussions that were happening maybe a few weeks or a few months ago now around whether it really was the right thing for the government to intervene so directly into the price, because if prices had been allowed to rise further, obviously, that incentivizes both people and businesses to cut back more on their energy use. And so one of the kind of downsides of intervening in this way is that they'll have a weaker incentive to cut back and as you say, that might then mean that energy usage is higher overall. And maybe rationing is a consequence of that. I'm not sure. But I think the thing that was often forgotten in that debate is that for people on low incomes, it's really not possible for them to cut back on their energy use any more. We know that last winter, many people were already having to go without heating when they needed it at various points during the winter. And so for them, I think the incentive argument is not important. And you know, they've cut back as much as possible, and it's dangerous for them to cut back more. But when we then think about the support, being universal and helping businesses and also helping those on higher incomes, I do think that is a cost and a downside to the choice, which is that it will it will weaken their incentives, and probably they will now consume more energy than they would have done otherwise.

Chris Coates 24:23
I had a couple of sort of looking at the big picture questions for both of you. Were talking about a crisis. Can you give us a perspective? Are we in unprecedented territory here?

Hamish Low 24:33
In the last 15 years, people have used the terms unprecedented crisis multiple times. There was the kind of 2008 financial crisis those the Euro crisis 2012 when it looked like the Euro was going to collapse. There was COVID and there's the current inflation crisis, I think is what it kind of speaks to is something Rebecca said at the start, which is we shouldn't take one crisis in isolation, we should look at the long-term impact of a series of if you like shocks have happened over people's lifetimes. And if you think about the households who've lived through all these last kind of 15 years of ongoing shocks, not necessarily if anyone's sort of creation, that's the right way to think about this as being a kind of crisis. I think the term unprecedented is not the right one, because I think we have seen these ongoing things happening now several times. I think what's unprecedented is the scale and the persistence of the lack of productivity growth and lack of income growth, particularly for people in the bottom half the distribution. And I don't think that's related just to the current crisis. I think that's more of a long-term phenomenon.

Rebecca McDonald 25:37
Yes, I completely agree, I think, unprecedented, has been used so much recently, I do think it's, I guess, unusual, or very unfortunate that we've had two very significant shocks in close succession. So a pandemic is a rare event, usually. We happen to have also had an energy

crisis triggered by a war straight afterwards. So that is, in many ways always going to be incredibly difficult to handle economically as a country. But I agree with Hamish I think probably What's difficult is the position we have been in in the long term, which means that the resilience to these kinds of shocks, especially for those who live in poverty, or near poverty is very low. And that means that when these kinds of shocks do come in, (a) it's very difficult to handle for those people financially. But secondly, also, it means that we have to turn to a very large ad hoc big emergency intervention, whereby I think, you know, there would always be some need for emergency intervention and either a pandemic or an energy bill increase like this. But I think we could have had more resilience built in, you know, if we had a Social Security system that was more adequate, then that would automatically have provided a lot of support, we wouldn't have needed emergency uplift in Universal Credit, we wouldn't have needed emergency benefit top up so much, because it would have already been built into the system. So I think there are ways in which we haven't been ready as ready as we could have been as a country in an economy to deal with shocks. But they will always come and that kind of, I guess one of the lessons after this, we'll be trying to build more of that resilience in and as Hamish says, if we can get stronger productivity growth and stronger economic growth after this is over, then that will also help build that resilience.

Hamish Low 27:19
I think just just on that, I think other things promising but how do you build resilience and the government should be doing, the government is kind of very much reacting to these situations. If I think about since 2010, what we've seen and seen the systematic decline in spending on education at all levels. And you can see that why that really matters is we need a workforce which is able to adapt in the way we still some people in adapting to the pandemic, you need to see that kind of people having skills, which are more adaptable skills. And I think that's kind of speaks to issues which have been discussed a lot recently, which is, why do we have a better apprenticeship scheme? Why don't we have a scheme which is actually able to build up that labour market resilience across the whole population. And I think that we will talk about resilience, I think it's really important we do distinguish between labour market resilience and financial resilience. Because financial resilience often can be substituted for by government policies after the event, like capping enterprises, increasing Universal Credit and so on the furlough scheme, but that labour market resilience is what is kind of lacking. And that's what seems to be the key to having a more long-term stability for families going looking forward.

Chris Coates 28:25
Those are really interesting points. And they lead me to my final question, you both talked a bit there about looking to the longer term, and there are various ideas floating around from different bits of the political spectrum, you know, should we nationalise energy companies? Should we invest in nuclear and sustainables? Can either of you talk a little bit about that in terms of, you know, what would be effective? And what are the best long-term measures? Do you think in terms of the energy market?

Hamish Low 28:52
I'm not sure at all about whether we should be nationalising energy companies. It feels like that's a very political question concerning ownership. And this is really about incentives. And I think that the incentive question is really about how do we incentivize companies to be

investing in long term energy changes like renewables. But I think even that misses the point, because it ties in with the whole issue about, are we gonna to be able to make net zero. And it feels like talking about incentivizing investment in renewables is one part of things. But another major part of this is how do we actually change people's demand? And that's where the kind of price cap, in some ways, I see it as a missed opportunity to get people to really think about what energy they're using, and what the long-term impacts in terms of carbon are. And so that kind of allowing people carry on with kind of business as usual, is, I believe, a missed opportunity. Instead, it could have been say what's the long term situation long term situations, we have to change substantially the way we're thinking about energy and make consumers face up to that. The reasons missed opportunity is that this was a chance for people to do that when they can see the real short-term reason for it, rather than some abstract what we need worry about the planet in 20 years time.

Rebecca McDonald 30:02
Yes, no, I agree with that completely, I don't have enough expertise in the energy market to know to be honest on the longer term policies that will kind of either prevent future situations like this or make us more resilient as a country energy wise, I think one of the things that I do think this highlights in importance, and, you know, maybe is secondary, but I think it's very important is energy efficiency, particularly of housing and in terms of the quality of homes, which are built from now on, but also in terms of making homes, especially for those on low incomes, so homes and the social rented sector or private rented sector or lower rents, making those homes more energy efficient. And that being beneficial, not just in terms of people's pockets and financially, but also so that when things like this do happen in the future, and there are shocks to something that is such an essential good, that people on their incomes are less vulnerable to those cost increases because their homes are more energy efficient.

Hamish Low 30:57
I think just the main thing, which I'm just going to reiterate is that we do go from crisis to crisis of one form or another. And it is about how do we make the economy more resilient, rather than reacting to what the latest problem is, and it feels like that's what we haven't managed to achieve the last 15 years.

Chris Coates 31:15
My thanks to Hamish Low and Rebecca McDonald. You can find out more about how the data from Understanding Society are changing practice and informing policy by visiting our website understandingsociety.ac.uk. This was a Research Podcasts production. Thank you for listening, and remember to subscribe wherever you receive your podcasts