

DOUBLE TROUBLE

A review of the relationship between UK poverty and economic inequality



Council housing in Tower Hamlets, London, dwarfed by financial buildings at Canary Wharf.
Photo: Abbie Trayler-Smith/Oxfam

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The key finding of this research is that a positive correlation between income inequality and relative income poverty in the UK over recent decades can be clearly established. This suggests that to reduce UK poverty, it is also important to address high levels of economic inequality. A review of the evidence on a selection of mechanisms linking inequality with poverty helps to explain why higher levels of inequality are associated with higher levels of poverty.

The full report is available at <http://policy-practice.oxfam.org.uk>

FOREWORD

Oxfam's core purpose is the ending of poverty and suffering. Yet, in recent years, we have grown increasingly alarmed by extreme and growing inequality around the world. Some have questioned why an anti-poverty organisation should concern itself with the gap between rich and poor. The reason for our twin focus is simple: extreme inequality is a barrier to reducing, and ultimately, ending poverty across the world.

Globally, this analysis has become increasingly mainstream thinking. Indeed, when world leaders agreed the Sustainable Development Goals (SDGs) in 2015 they included – for the very first time – a specific goal to reduce inequalities, alongside the goal of ending poverty in all its manifestations. They have set themselves a stretching 2030 target.

Significantly, the SDGs do not apply only to developing countries, they apply everywhere – including in developed countries like the UK. However, to date, the relationship between poverty and economic inequality in the UK context has been woefully neglected. It is this gap that this report, *Double Trouble* helps to fill, and with significant implications for anti-poverty efforts within the UK.

Published with Oxfam GB's academic partners, CASE/LSE, *Double Trouble* has taken the long view by exploring the trends in relative income poverty in the UK over the last five decades. We have focused on the relative income poverty measure as it is one of the key indicators used widely by all. This research asked the urgent, and controversial, main question – do these relative income poverty trends have anything to do with the high levels of UK income inequality that we have also witnessed?

The stark answer emerging from this comprehensive independent review of the empirical data is a resounding 'yes'. This report makes clear there is a positive correlation between income inequality and relative income poverty in the UK. The strength of this connection depends on which measure of inequality is used and this report makes no claim about causation – but the central conclusion is clear.

The significance of this finding is that we can no longer treat poverty and economic inequality as separate problems which can be tackled in isolation. They are instead closely linked and must be tackled together.

We acknowledge that our report is only a humble first step - a problem diagnosis of the reality of the entwinement of income poverty and income inequality in the UK. We identify the broad range of policy directions which could address this, but more research is required to identify the suite of policy solutions.

However, we hope and believe that '*Double Trouble*' makes a strong intellectual contribution to the academic and policy debate on the state of UK poverty by partially filling some of the existing knowledge gaps. We are also sober in the knowledge that, to have genuine impact, this research must do more than merely plug an intellectual gap; it must drive towards substantive policy and practice change.

Our key finding of a positive correlation between income poverty and economic inequality, must serve as an overdue and urgent call to action for all anti-poverty actors in the UK to seriously question whether a focus on reducing poverty alone is now sufficient to tackle the complexity of the challenge we face today. This could prove an uncomfortable challenge.

The shift Oxfam GB has made in widening its focus to encompass both poverty and inequality reduction has not been without its critics internationally or here in the UK. Yet the empirical data outlined in this report demands this reassessment. 'Business as usual' interventions to address domestic poverty in isolation from broader economic inequalities are no longer sufficient for Oxfam, or anyone else.

At the very least, the UK data contained in *Double Trouble* means the positive relationship between these two insidious realities can no longer be dismissed as either ungrounded ideological conjecture or even, as the report makes clear, as little more than the product of an inherent mathematical relationship.

For our part, *Double Trouble* will serve to reinforce and re-invigorate our global analysis that more unequal countries have less success in tackling poverty. We will therefore continue, unflinchingly, to sound the emergency alarm about the problematic relationship between poverty and inequality, this 'double trouble', wherever we find it occurring.

We ask all those with an interest in poverty reduction, from the governments of the UK to the anti-poverty sector itself, to explore with us the implications of this positive correlation. We know we don't have all the answers. Nor can we turn these insights into action on our own. It will take all of us to recognize the deep connections between poverty and economic inequality in the UK, and to act together to tackle these twin challenges.

Dr Philomena Cullen

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SUMMARY

A positive correlation

The research report, *Double Trouble*, investigates the relationship between economic inequality and poverty in the UK and examines the trends in relative income poverty rates and income inequality over the period 1961 to 2015/16 (the latest year income data are currently available). Oxfam GB commissioned this research because the relationship between UK poverty and inequality is complex and not well understood; not least because historically these phenomena have tended to be researched separately.

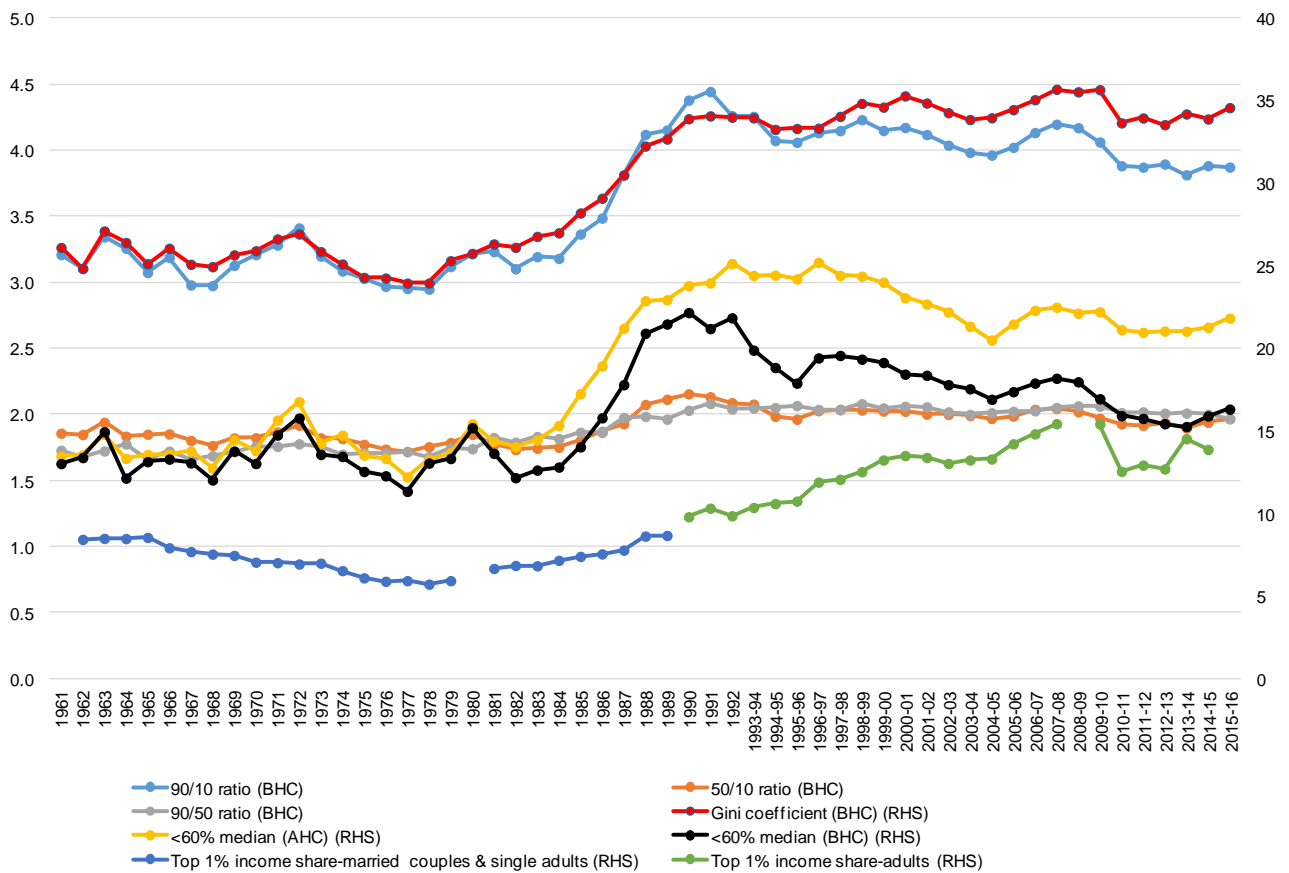
The key finding of this research is that a positive correlation between income inequality and relative income poverty in the UK over recent decades can be clearly established. We found that relative poverty rates tend to be higher when income inequality is higher, and this suggests that increases in income inequality are associated with increases in relative income poverty rates. Focusing on the Gini coefficient as a measure of income inequality, we show that, on average over the period 1961–2015/16 for the before-housing costs measure of income; this equates to an increase in the Gini coefficient of 1 point being associated with an increase in the rate of relative income poverty by 0.6 percentage points. For the after-housing costs measure, an increase in the Gini coefficient of 1 point is associated with an increase in the rate of relative income poverty by 0.7 percentage points.

Some of the relationship we observe between these two related but distinct phenomena is likely to be due simply to the mechanical (mathematical) relationship between commonly used measures of inequality and poverty. This is particularly the case between measures of relative income poverty and income inequality in the lower half of the income distribution, as both effectively summarise certain aspects of the distribution of income. More revealing is the observed relationship between inequality in the top half of the income distribution and income poverty. We find a positive correlation for inequality estimates which measure the ratio of high incomes to average (median) income and for the concentration of income among those on the highest incomes (for example, the top 1% share).

Historical trends

The history of this relationship shows that both income inequality and relative income poverty have followed similar time trends (see figure below). The series in the chart show trends in UK income inequality and relative income poverty from the early 1960s until 2015/16. In terms of the broad picture, the main increase in income inequality and relative income poverty occurred over the 1980s. There was some success in reducing income poverty rates in the 1990s, but high housing costs for low-income households limited the impact of these changes. For a number of years following the financial crisis poverty rates declined, but this was due to falling average incomes reducing the poverty threshold, and therefore the share beneath the threshold, rather than due to an improvement in living standards among low-income households (Belfield *et al.*, 2014). The overall dispersion of income measured by the Gini coefficient has remained fairly stable since the mid-1990s, but inequality measured by the concentration of income among the top 1% has continued to increase, with recent trends in this series since the financial crisis being linked to behavioural responses of the most well-off to changes in taxation.

Figure: UK income inequality and poverty trends 1961–2015/16



Sources: Institute for Fiscal Studies: Living Standards, Inequality and Poverty Spreadsheet 2016. Top income shares from the World Wealth and Income Database (WWID). The authors would like to thank Facundo Alvaredo (at WWID) for providing an updated series for UK top income shares.

The geography of inequality and poverty

Inequalities between England, Scotland, Wales and Northern Ireland have also increased over time, and the cost of housing plays an important role here. There is also evidence of increasing geographical segregation of ‘the rich’ and ‘the poor’ which has important implications, not least for people’s perceptions of inequality, which can in turn alter preferences for redistribution or other policy action designed to tackle poverty and inequality.

Identifying drivers of the correlation

Various mechanisms appear to drive the relationship between inequality and poverty, and in this review we begin the process of exploring the existing evidence. It is beyond the scope of this project to review the evidence on all potential mechanisms and therefore we focus on a selection. Across all areas covered in the review we found evidence that helped to explain why a positive relationship between economic inequality and poverty exists. For example, reviewing the evidence on the role of public opinion, voting behaviour and broader features of the political economy we find:

- While most Britons believe that inequality is too high (McKnight and Tsang, 2013), there is a tendency for people to underestimate the true level of inequality and overestimate social mobility (Osberg and Smeeding, 2006; Orton and Rowlingson, 2007); this is linked to sub-optimal pressure on governments to reduce inequality to a more acceptable level (Georgiadis and Manning, 2012).

- Increasing inequality has been related to a change in the composition of the voting electorate, who are now better off on average than the population as a whole. This has skewed government policy in favour of better-off households, and made them less likely to tackle poverty (McKnight and Tsang, 2014).
- Evidence suggests that a growing rich and powerful elite with access to political power and decision making are influencing legal frameworks and government policy in their favour. This leads to a greater concentration of income and wealth, fewer resources to be shared among the rest of the population and less concern for low-income households (e.g. Stiglitz, Piketty, Atkinson, etc.).

Future policy directions

There is a growing body of evidence that high and rising economic inequality is harmful for growth (e.g. Cingano, 2014 and Ostry et al., 2014), and that tackling poverty alone is not enough to reduce economic disparities and poverty in the long run. Although tackling inequality through redistribution may not be the only solution, recent evidence has shown that redistribution is not damaging for economic growth and that poverty reduction efforts are more effective in environments of lower inequality (Ostry et al., 2014).

The Equality Act 2010 and the broader equality agenda are important elements in reducing inequality, but it is clearly possible to reduce inequalities between population groups (e.g. equalising poverty rates or pay between genders or ethnic groups) without reducing *overall* inequality and poverty. This suggests that an equality agenda needs to be combined with both an anti-poverty strategy and a focus on reducing overall economic inequality, to produce positive long-term change.

Projections of inequality and poverty trends in the UK suggest that inequality and poverty will increase further in the next five to fifteen years (Hood and Waters, 2017). However, experts are optimistic about the role that policy can play, both to curb increasing rates of inequality and poverty and to bring those rates down.

The finding of this research supports the view that there exists a series of mechanisms linking inequality with poverty more broadly. We therefore conclude that for organisations and governments concerned with reducing poverty, it is also important that they focus on addressing high levels of economic inequality if they are to be successful. This is the urgent policy challenge that Oxfam would like to see the UK government respond to, so that it matches the apparently greater appetite for tackling inequality and poverty that we have seen in the devolved administrations of the UK since 2010. We recommend that the recently agreed UN Sustainable Development Goals offer a real vehicle for action for the UK government to create a fairer society, with the gains from any future growth being shared more equally.

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