Analysing the impact of the UK Government's welfare reforms in Wales – Stage 1 analysis

Summary of the key findings

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Audience

This report has been produced primarily for the Welsh Government's Ministerial Task and Finish Group for Welfare Reform (the group includes the Minister for Education and Skills; the Minister for Local Government and Communities; the Minister for Housing, Regeneration and Heritage; the Deputy Minister for Children and Social Services) and relevant policy officials.

Overview

This report, produced by Knowledge and Analytical Services (Welsh Government) has aimed to analyse the existing evidence on the potential cumulative impact of the UK Government's welfare reforms on individuals and households in Wales.

Action required

None – for information only.

Further information

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Additional copies

This document can be accessed from the Welsh Government's website at www.wales.gov.uk/educationandskills

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Introduction

Outlined on the next page is a summary of the key findings from Stage 1 of the Welsh Government's programme of work that aims to assess the impact of the UK Government's welfare reforms in Wales.

Key findings

- **Wales has a higher dependence on welfare benefits than Great Britain as a whole**. The latest statistics (for May 2011) show that 18.4 per cent of the working-age population in Wales were claiming welfare benefits compared to the Great Britain average of 14.5 per cent. The main reason for the higher benefit claimant rate in Wales is the higher proportion of people claiming disability and sickness benefits.
- Stage 1 of the analysis has largely drawn on existing evidence published by the Institute for Fiscal Studies (IFS), which has assessed the **combined impact of the tax and benefit changes** announced by the Coalition Government. To our knowledge, there is currently very limited evidence on the cumulative impact of the benefit changes in isolation, and particularly at a Wales level. However, this will be considered as part of Stage 2, which we currently anticipate will be completed around the end of 2012.
- The ultimate effects of the welfare reforms will largely depend on the **strength of the wider economy and the extent to which people change their behaviour in response to benefit reductions**. Although existing analysis is mostly static in nature in that it does not attempt to estimate likely behavioural responses, it is a useful starting point. Stage 2 will try to estimate the likely behavioural responses including how these responses may change depending on a range of scenarios for the economy in Wales.
- Analysis from the IFS following the Spending Review 2010 estimates that the impact of the tax and benefit changes to be implemented by 2014–15 will mean that **on average households in Wales can expect to lose 4.1 per cent of their income (or £1,110 per year)**. This compares to a UK average loss of 3.8 per cent (or £1,170 per year). Variations in the impact of the tax and benefit reforms across countries and regions in the UK are due to differences in the characteristics of households.
- Out of the 12 UK regions and countries analysed by the IFS, households in Wales are expected to have the **fifth largest average cash loss**, although this is less than the average cash loss for the UK as a whole. This is because the overall cash loss for the UK is skewed upwards by some very large cash losses for the very richest households, a disproportionate share of which are located in London. However, the average loss as a percentage of income is estimated to be greater in Wales than the UK as a whole. This is because average incomes are lower in Wales than in the UK.

- The IFS note that the tax and benefit changes to be implemented over the next several years will be regressive in nature at the UK level (i.e. they will take more proportionately from lower-income groups than from higher-income groups except the very richest income group), and are likely to be even **more regressive in Wales**.
- Looking at the proportion of the population claiming out-of-work benefits together with the distribution of low-income households in Wales suggests that the **South Wales Valleys and the inner city areas of Cardiff, Newport and Swansea are most likely to be disproportionately impacted by the benefit changes**.
- Recently extended IFS analysis (which includes measures announced in the Autumn Statement 2011) estimates the impact of the tax and benefit reforms on different household types (at a UK level). **Families with children are expected to lose proportionately more of their income** across the income distribution compared to pensioner households and working-age households without children. Furthermore, **the poorest households with children are estimated to lose the largest proportion of their income** as a result of the tax and benefit changes. In particular, **non-working lone parents** and **workless couples with children** are expected to suffer a disproportionate financial hit. **Families with children aged under five** and **families with more than two children** will also be particularly badly affected.
- The IFS has also analysed the impact on poverty of the tax and benefit reforms announced by the Coalition Government up until summer 2011. This suggests that the reforms will **raise poverty among families with children more than among working-age adults without children**. Furthermore, as announced in the Autumn Statement 2011, the above-inflation increase in the child element of Child Tax Credit will not go ahead, meaning more bad news for families in Wales. Both the IFS and HM Treasury estimate an increase in UK relative child poverty of around 100,000 in 2012–13. Based on proportionate shares adjusted for differences in poverty, the Welsh Government provisionally estimates that the tax and benefit reforms could increase relative child poverty in Wales by about 6,000 in 2012–13.

- IFS analysis of the impact of the tax and benefit changes (including Universal Credit) to be introduced by 2014 suggests that, on average, the **incentive to undertake paid work will be strengthened for the UK population as a whole**. However, there are likely to be different impacts on subgroups of the population.
  - **Those without children**: on average, incentives to undertake paid work for single people with no children and couples without children are expected to be strengthened.
  - **Those with children**: on average, financial work incentives for lone parents are expected to be significantly strengthened, while couples with children are likely to have a slightly weakened incentive to undertake paid work.
- In assessing the potential impact of the welfare reforms on incomes and spending in Wales it is necessary to consider multiplier effects. It is difficult to precisely quantify these effects but broadly speaking evidence suggests that **each £1 of income lost could be associated with a total loss of income to Wales somewhere in the range of £1.00–£1.50** (i.e. a multiplier in the range of 1.0–1.5). This should be regarded as an interim assumption pending fuller analysis at Stage 2. It is important to note that the multiplier effects will be smaller, and could even be positive, if people move into work.
- Limited analysis appears to have been undertaken on the potential social impacts of the welfare reforms to be introduced over the next few years. However, a small number of studies that have looked at the impact of past welfare reforms on crime have been drawn upon (given their broad similarities to the current reforms). These suggest **cuts to benefits and more stringent benefit entitlement rules may push people out of unemployment and into crime activities. There is also some evidence that the timing and frequency of welfare payments can impact on crime levels**.
- The Department for Work and Pensions note in a number of their impact assessments that the welfare policies could have **positive impacts on health if they lead to more people moving into work**. As with wider economic impacts, social impacts will also be highly dependent on behavioural responses and wider economic conditions.