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

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

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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Introduction

The Welsh Government's Ministerial Task and Finish Group for Welfare Reform has commissioned a programme of work to assess the impact of the UK Government's welfare reforms in Wales. This paper outlines the key findings from Stage 1 of this programme of work. The main aim of this early analysis has been to analyse the existing evidence on the broad cumulative impact of the welfare reforms on individuals and households in Wales. This has largely drawn on evidence published by the Institute for Fiscal Studies (IFS), which has assessed the combined impact of the tax and benefit changes announced by the UK 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.

The analysis to date includes:

1. A summary of the main welfare reform policy announcements (**Annex 2**).
2. Estimation of the number of individuals that will be impacted by the reforms in Wales.
3. An assessment of the expected monetary impact:
    a) a comparison of the estimated impact in Wales compared to the UK as a whole and the other countries and regions of the UK
    b) an assessment of the likely spatial impacts within Wales
    c) disaggregation of the impacts of the main reforms according to the characteristics of the individual and/or household in Wales (including income group, families with children, lone parents, working-age adults without children, pensioners, and workless households)
    d) analysis of impacts on work incentives.
4. Assessment of the impact on poverty, including child poverty.
5. Analysis of the wider economic impacts.
6. Assessment of the wider social impacts such as the potential impact on crime and health in Wales.

An initial assessment of the administrative impacts that the welfare reforms are likely to have on delivery agents in Wales has also been undertaken internally. This assessment has highlighted a number of potential delivery issues. These will continue to be monitored as further detail becomes available on the implementation of the changes within the Welfare Reform Bill.

An outline of the programme of work in its entirety can be found at **Annex 1**.

Summary of the key findings

- As illustrated by Table 1, **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.

Table 1: Benefit claimants (aged 16–64) by statistical group, May 2011

Stat group*	Great Britain		England		Scotland		Wales	
	Number	Rate	Number	Rate	Number	Rate	Number	Rate
Job seeker	1,403,910	3.6	1,197,090	3.5	136,490	4.0	70,330	3.7
ESA and incapacity benefits	2,560,470	6.5	2,104,450	6.2	276,900	8.1	179,130	9.4
Lone parent	595,370	1.5	516,860	1.5	47,770	1.4	30,740	1.6
Carer	455,830	1.2	385,940	1.1	40,700	1.2	29,180	1.5
Others on income-related benefit	187,160	0.5	160,450	0.5	16,800	0.5	9,910	0.5
Disabled	410,500	1.0	345,220	1.0	39,430	1.1	25,860	1.4
Bereaved	80,410	0.2	67,960	0.2	8,290	0.2	4,150	0.2
Total	**5,693,650**	**14.5**	**4,777,970**	**14.1**	**566,380**	**16.5**	**349,290**	**18.4**

* Stat group is a hierarchical variable that allocates people to the main benefit they are claiming.
Source: Department for Work and Pensions (DWP) statistics, Nomis

- The June Budget 2010 and Spending Review 2010 announced by the UK Coalition Government included various changes to the benefit system, estimated to save over £18 billion by 2014–15. By far the largest contribution (£6 billion) to these savings will come from indexing almost all benefits to the Consumer Price Index (CPI) rather than the Retail Price Index (RPI). Further welfare changes have been announced in the Budget 2011 and Autumn Statement 2011. These changes amount to around £1.3 billion of savings by 2014–15 (see Table 2 on page 5 and **Annex 2** for more detail).

Table 2: Summary of the welfare policy decisions announced in the June Budget 2010, Spending Review 2010, Budget 2011, and Autumn Statement 2011 (£ million)

	2011–12	2012–13	2013–14	2014–15
June Budget 2010	2,010	4,710	8,150	11,040
Spending Review 2010	320	2,555	5,990	7,040
Budget 2011	30	-70	-50	-35
Autumn Statement 2011	0	1,240	1,245	1,295

- 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 1 of the analysis has largely drawn on evidence published by the 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.
- 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 (and are particularly affected by the changes pre-announced by the previous UK Government). In addition, households in London are also disproportionately impacted by the cuts to Housing Benefit. 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 be highly dependent on behavioural responses and wider economic conditions.

Stage 1 analysis

1. A summary of the welfare reform policy announcements (please see Annex 2)

2. Estimation of the number of individuals that will be impacted by the welfare reforms in Wales

The Department for Work and Pensions (DWP) has taken the approach to produce individual impact assessments for the main proposals contained in the Welfare Reform Bill, rather than a single overall cumulative impact assessment. Also, not all of the impact assessments contain figures for Wales. Therefore, at this stage it is difficult to estimate the total number of people that may be affected in Wales. However, to give an idea of the number of people in Wales that could potentially be affected by the welfare changes, this section provides an overview of the main welfare statistics. In addition, some of the DWP impact assessments that do include figures for Wales and other research projects that have assessed potential impacts have been drawn upon.

The latest statistics[1] show that a higher proportion of the working-age population in Wales are in receipt of some type of welfare benefit compared to England, Scotland and the average for Great Britain (GB). Table 1 (page 4) illustrates that 18.4 per cent of the working-age population in Wales were claiming welfare benefits in May 2011 (GB average 14.5 per cent). This is equivalent to around 350,000 claimants in Wales. Of these, around 290,000 were claiming out-of-work benefits[2]. Within this category, the largest claimant group are those in receipt of **Employment and Support Allowance (ESA) or Incapacity Benefit (IB)** (often in combination with other benefits) with nearly 180,000 people in Wales claiming this as their main benefit, equivalent to 9.4 per cent of the 16–64 population. In Great Britain, the proportion was 6.5 per cent.

In October 2008, ESA replaced IB and Income Support claimed on the grounds of incapacity for new claimants. Existing IB claimants will be migrated onto ESA between spring 2011 and spring 2014. ESA involves a medical assessment, the Work Capability Assessment (WCA), which categorises claims into fit for work (i.e. ESA claim is ceased but around 70 per cent will move onto another benefit[3]), the support group (for those with severe disabilities) and the work-related activity group (who are mandated to move towards

[1] For May 2011.
[2] Includes Job Seekers Allowance, Employment and Support Allowance, Incapacity Benefit, lone parents and other income-related benefits.
[3] Time Limiting Contributory element of ESA – Impact assessment (DWP, 2011)

the workplace with help and support). WCA figures relating to new ESA claims in Wales between October 2008 to February 2011 show that 5 per cent were placed in the support group, 18 per cent were placed in the work-related activity group, and 39 per cent were found to be fit for work[4]. Whereas IB was open-ended, from April 2012 the UK Government will time-limit contributory[5] ESA to one year for those in the work-related activity group, thereby encouraging a return to work. Claimants will be able to receive income-related ESA (which will not be time-limited) if they fulfil conditions of entitlement; otherwise they will move off ESA. The Department for Work and Pensions (DWP) estimate that around 40 per cent of those eligible for the time-limiting policy (i.e. ESA claim duration of more than one year) will no longer be entitled to ESA. This is estimated to be equivalent to around 700,000 people in Great Britain by 2015/16. Assuming an impact proportionate to the Great Britain aggregate based on caseloads, we may expect approximately 7 per cent of this total to be affected in Wales[6].

In May 2011, the proportion of the working-age population claiming **Job Seekers Allowance** (JSA or claimant-count rate) was 3.7 per cent in Wales (around 70,000 JSA claimants). This is slightly higher than in Great Britain, which had a claimant-count rate of 3.6 per cent (around 1.4 million JSA claimants). The latest JSA data for January 2012 continues to show broadly the same pattern.

Table 1 also illustrates that Wales has the highest proportion of disabled benefit claimants in GB at 1.4 per cent of the working-age population (around 26,000 disabled claimants), compared to the GB average of 1.0 per cent (around 400,000 disabled claimants). In terms of **Disability Living Allowance** (DLA) recipients, Wales has the largest proportion of individuals claiming this benefit in Great Britain. In May 2011, there were 142,000 working-age individuals claiming DLA in Wales, equal to 7.5 per cent of the working-age population. In comparison, 2.028 million working-age individuals in Great Britain were in receipt of DLA, equivalent to 5.2 per cent of the working-age population. Note that unlike the previous analysis this includes all DLA claimants, including those who are claiming other benefits.

4 ESA: Work Capability Assessment – Official Statistics for Wales, October 2011 (Table 1) (DWP, 2011).

5 Contributions-based ESA applies to those who have paid enough National Insurance contributions. Income-based ESA is received if claimants' income and savings are low enough.

6 Calculated using the caseload data in Table 1 of this report.

Reforms to DLA are currently being introduced. The impacts of these reforms are likely to be felt more in Wales than in Great Britain as a whole given the higher proportion of DLA claimants. The reforms involve DLA being replaced by the Personal Independence Payment (PIP), a new cash benefit to be introduced by 2013/14. It is expected that this reform (which includes a stricter medical test) will reduce the numbers eligible for DLA/PIP, targeting those in greatest need. The June Budget 2010 estimates that there will be a 20 per cent reduction in caseload and expenditures once the DLA reform has been fully rolled out (however, there is uncertainty as to whether this will be met). LE Wales (2011) have undertaken scenario modelling to assess the impact of changes to DLA payments in Wales. Among other scenarios, a baseline scenario (benefits continue as present) is compared to the DLA reform (as set out in the June Budget 2010). This projects that approximately 30,000 working-age people living in Wales who would have received DLA under the baseline scenario would not receive benefits by 2030. In comparison to the baseline projection, annual DLA expenditure on working-age recipients is projected to be around £200 million lower in Wales by 2030[7].

Given the focus of the welfare reforms on moving long-term benefit claimants back into work, it is useful to look at the duration of benefit claims in Wales. Table 3 illustrates that Wales has a significantly higher proportion of people claiming welfare benefits for five years or more at 8.4 per cent, compared to 5.8 per cent in Great Britain as a whole. This group will be particularly targeted by the welfare reforms. The main reason for this difference is that Wales has a greater proportion of people who have been claiming ESA/IB for more than five years (6.1 per cent compared to 4.1 per cent for GB[8]).

Table 3: Duration of benefit claims[9], May 2011

Duration	Great Britain		Wales	
	Number	Rate	Number	Rate
Up to 6 months	1,322,910	3.4	70,300	3.7
6 months up to 1 year	579,820	1.5	31,770	1.7
1 year and up to 2 years	580,500	1.5	32,160	1.7
2 years and up to 5 years	932,020	2.4	55,700	2.9
5 years and over	2,278,390	5.8	159,360	8.4
Total	**5,693,650**	**14.5**	**349,290**	**18.4**

Source: DWP Statistics, Nomis

7 *Impacts of DLA on working age people in Wales* (LE Wales, 2011). LE Wales have also undertaken research on the likely impact of changes to DLA and Attendance Allowance for older people (65-plus) in Wales.
8 Source: DWP statistics, Nomis
9 Includes the range of benefits listed in Table 1.

Table 4 illustrates **Housing Benefit** (HB) and **Council Tax Benefit** (CTB) caseloads for Great Britain as a whole and Wales[10]. At August 2011, the total number of people claiming HB in Wales was around 245,000 (10.0 per cent of 16-plus population), with around 326,000 claiming CTB (13.3 per cent of 16-plus population). This compares to around 4.9 million HB recipients and 5.9 million CTB recipients in Great Britain (10.0 per cent and 11.9 per cent of the 16-plus population respectively).

Table 4: Council Tax Benefit and Housing Benefit claimants (16-plus population), August 2011

Benefit	Great Britain		Wales	
	Number	Rate	Number	Rate
All HB recipients	4,909,510	10.0	244,900	10.0
All CTB recipients	5,860,150	11.9	325,770	13.3

Source: DWP statistics, Nomis

From April 2013, CTB which is currently paid by DWP to local authorities will be abolished and responsibility for establishing a replacement scheme will pass to the Welsh Government.
In England this responsibility will be localised – the UK Government claims this will provide local authorities with more control over the administration of the benefit as they will have more flexibility to set their own criteria for payments. In Wales a replacement system is yet to be determined. As announced in the Spending Review 2010, CTB funding levels will be 10 per cent lower than current spending on this benefit, saving £0.5 billion per annum. The IFS point out that this is likely to hit poorer households hard.

With regards to HB, this will be abolished following the introduction of Universal Credit, which will have a housing element. Prior to this, changes have already been made to the existing system with further amendments planned. The changes introduced in April 2011 included:

- changing the basis for setting Local Housing Allowance (LHA) rates from the median to the thirtieth percentile of local market rents
- introducing a cap on LHA rates which will be paid for a maximum of four bedrooms (five-bedroom rate no longer available)
- removing the provision for claimants to retain a maximum of £15 per week where their rent is below the LHA rate.

[10] This benefit data is excluded from Tables 1 and 3.

DWP has estimated that **48,530** LHA recipients[11] in Wales will lose money because of the above changes implemented in April 2011[12]. This represents 99.6 per cent of all recipients of LHA. The average weekly loss per person is estimated to be **£9** in Wales, compared with **£12** for the UK as a whole.

Further planned changes include:

- raising the age under which the Shared Accommodation Rate applies from 25 to 35 from January 2012. DWP estimate that this will affect **3,080** people in Wales, with an average weekly loss of **£24**[13]
- uprating LHA rates according to CPI from April 2013. DWP estimate that **48,530** LHA recipients in Wales will lose money as a result. The estimated average loss is **£5.50** per person per week[14]
- limiting the amount of HB paid to claimants living in social housing who are under-occupying their accommodation from April 2013. DWP estimate that **40,000** working-age HB claimants living in the social sector in Wales will be affected by this measure[15]. This is equivalent to 42 per cent of HB claimants in the social rented sector, a higher proportion than the average for Great Britain (32 per cent). This is due to a higher incidence of under-occupation in Wales. The average weekly HB loss per affected claimant is estimated by DWP to be **£11** in Wales (£13 in Great Britain).

Based on DWP impact assessments, these changes to HB will amount to a total average loss of **£1,217,605 per week** in Wales. This loss will be offset by short-term entitlements to discretionary housing payments. However, this average loss excludes the impact of capping benefit payments at £500 per week for families (£350 per week if single and no children), which is likely to impact on 67,000 claimants across the UK in 2013–14 and 75,000 in 2014–15. Fewer than 3 per cent of these affected households will be in Wales (i.e. less than 2,000), with a quarter of these in Cardiff. In 2013–14 prices, the average weekly loss in the UK is estimated to be around £83 per week[16] (data on weekly losses not currently available for Wales).

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[11] Not all of those claiming Housing Benefit in Wales have their benefit calculated by the LHA. LHA applies to those living in the private rented sector and for new claims after April 2008.

[12] Impacts of Housing Benefit proposals: Changes to the Local Housing Allowance to be introduced in 2011-12 (DWP, 2010). The figures in the DWP Housing Benefit impact assessment are likely to be understated as they are based on statistics from March 2010.

[13] Housing Benefit Equality Impact assessment (DWP, 2011)

[14] Housing Benefit – Uprating Local Housing Allowance Rates by CPI from April 2013 Impact assessment (DWP, 2011).

[15] Under-Occupation of Social Housing – Impact assessment (DWP, 2011).

[16] Household Benefit Cap – Impact assessment (DWP, 2012).

Specific welfare reforms will be analysed in more detail during later stages of this programme of work.

3. Expected cumulative monetary impact of the welfare reforms

As discussed above, the UK Government's welfare reforms are expected to impact on claimant groups in a variety of ways dependent on the changes made to each of the (single or multiple) benefits they are claiming and their household characteristics (e.g. income and household type). The ultimate effects will also depend in part on the strength of the wider economy and the extent to which people change their behaviour in response to benefit reductions. In particular, the availability and attractiveness of jobs will be an important factor in determining overall impact.

It is important to note that the IFS analyses discussed below take a static approach and therefore do not incorporate behavioural responses. The UK Government has also modelled the distributional impact of the tax and welfare changes on households. Their approach shares the same limitation in that it focuses on the 'next day' impact of the policy measures, and therefore behavioural effects over time are not modelled (Stage 2 of the Welsh Government's programme of work will try to estimate likely behavioural responses to the welfare reforms). The UK Government's distributional analysis also has further limitations, specifically, the latest analysis at an individual level is partial, covering around 70 per cent of tax credit and benefit changes coming into effect in 2012–13 only. Due to these limitations, the IFS analyses, which are considered to be more complete, have been drawn upon throughout this paper.

As mentioned, the June Budget 2010 and Spending Review 2010 identified approximately £18 billion in welfare savings by 2014/15 (see **Annex 2**). By far the largest contribution (£6 billion) to these savings will come from indexing almost all benefits to the CPI rather than the RPI. CPI is generally lower than RPI, with the average CPI rate being 3.1 per cent over the five years to October 2011 compared to 3.5 per cent for RPI. The change to this uprating mechanism is therefore highly likely to suppress increases in income for benefit claimants. Furthermore, it is likely that this change will be felt disproportionately in Wales owing to the greater dependence of the Welsh population on benefit payments. In addition, the Budget 2011 and Autumn Statement 2011 announced further changes to the welfare system, amounting to around £1.3 billion of savings by

2014/15. Specifically, the above-inflation increase in the child element of Child Tax Credit will not go ahead, saving around £1 billion by 2014/15. Also, the couple and lone parents elements of Working Tax Credit will be frozen and not uprated by CPI saving £275 million by 2014/15.

Although the focus of this programme of work is on the impact of the welfare reforms in Wales, some of the published evidence that has been drawn on below has assessed the combined impact of the tax and benefit changes. 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.

a. Regional impacts

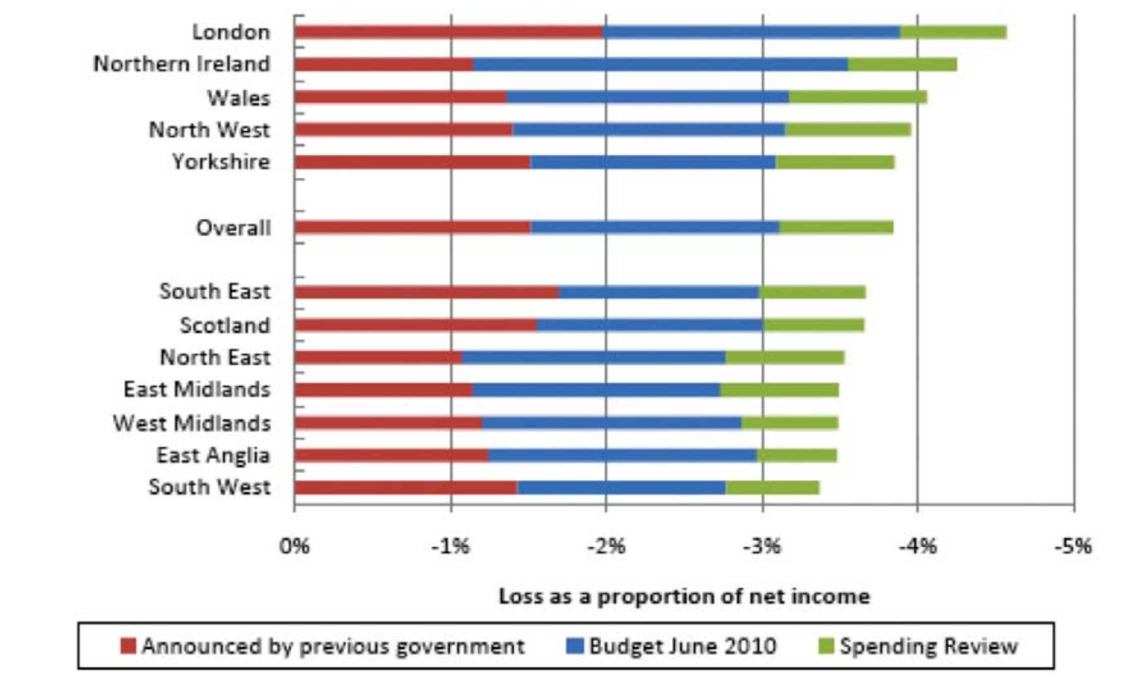
Following the Spending Review 2010, the IFS undertook some analysis of the potential cumulative impact of the tax and benefit reforms across the regions of England and devolved UK countries[17]. Spatial variations in the impact of the reforms are due to differences in the characteristics of households. As expected, given the higher proportion of the Welsh population claiming benefits and also due to average incomes being lower in Wales, the IFS estimate that the proportional impact in Wales will be slightly more severe than the average across the UK as a whole. As Figure 1 shows, by 2014–15 households in Wales are expected to lose 4.1 per cent of their income on average (or £1,110 per year) as a result of the tax and benefit changes. This compares to a UK average loss of 3.8 per cent (or £1,170 per year). Out of the 12 UK regions and countries analysed by the IFS, only households in Northern Ireland and London are expected to lose proportionately more than Wales.

In cash terms, Wales is 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. These households are particularly affected by the changes announced

[17] *The Impact of Tax and Benefit Reforms to be Introduced between 2010–11 and 2014–15 in Northern Ireland* (IFS, 2010). As this analysis was published following the Spending Review 2010, it does not incorporate the changes announced in the Budget 2011 and the Autumn Statement 2011. Also, it does not account for the impact of Universal Credit (which is intended to be run from October 2013). More recent analysis by the IFS suggests that the regressive nature of the tax and benefit changes to be introduced by 2014–15 is much less pronounced once the full effect of Universal Credit is taken into account. The impact of Universal Credit will be assessed in detail as part of Stage 3 of the Welsh Government's programme of work to analyse the impact of the welfare reforms in Wales.

by the previous UK Government. In addition, households in London will also be disproportionately impacted by the cuts to Housing Benefit given that it is a high-rent area. With regards to Wales, this will be one of the regions that loses the most from the benefit changes announced in the Spending Review 2010, particularly due to the large numbers of long-term ESA recipients (as noted in Section 2).

Figure 1: The effect of tax and benefit changes to be introduced between 2010–11 and 2014–15 by UK region



Notes: Assumes increases in employer NICs are passed on to employees in the form of lower wages.

Source: *The Impact of Tax and Benefit Reforms to be Introduced between 2010–11 and 2014–15 in Northern Ireland* (IFS, 2010)

Just as the benefit changes that will be implemented over the next several years will be regressive for the bottom four-fifths of the income distribution at a UK level, they will also be regressive in Wales (i.e. they will take more proportionately from lower-income groups than from higher-income groups, except the very highest income group), according to IFS analysis. Table 5 shows the expected impact by income quintile[18] for each of the regions of England and devolved

18 This IFS analysis has used income quintile groups (as opposed to deciles) due to the small sample sizes for regions. Quintiles are derived by dividing all households into five equal-sized groups according to income adjusted for household size using the McClements equivalence scale. Quintile group 1 contains the poorest fifth of the population, quintile 2 contains the second poorest, and so on up to quintile group 5, which contains the richest fifth.

UK countries. We can see that the loss for the poorest four quintiles is higher for those in Wales than the average for the UK as a whole but slightly less for the richest quintile. Poorer households in Wales lose more on average from the benefit reforms than their counterparts in the rest of the UK, but the richest quintile is less affected by measures affecting the very richest households in the UK, simply because very few of the richest households are in Wales. In Wales 14 per cent of households are in the top income quintile. Only Northern Ireland has a lower proportion of households in this richest quintile (12 per cent) out of all of the UK countries. Around two-thirds of Welsh households are in the bottom three quintiles[19].

Table 5: Loss as a percentage of net income from tax and benefit changes to be introduced between 2010–11 and 2014–15 by UK income quintile

Region	Poorest	2	3	4	Richest	All
North East	-5.1%	-4.6%	-3.9%	-2.9%	-2.8%	-3.5%
Yorkshire	-5.1%	-4.2%	-2.9%	-2.9%	-4.5%	-3.8%
North West	-5.6%	-4.6%	-3.8%	-2.9%	-4.0%	-4.0%
East Midlands	-4.6%	-3.8%	-3.5%	-2.8%	-3.3%	-3.5%
West Midlands	-4.9%	-4.4%	-3.4%	-2.7%	-3.2%	-3.5%
East Anglia	-4.6%	-3.6%	-3.3%	-2.9%	-3.6%	-3.5%
London	-5.3%	-4.6%	-4.2%	-3.6%	-4.8%	-4.6%
South East	-5.0%	-4.0%	-3.2%	-3.0%	-3.8%	-3.7%
South West	-4.8%	-4.0%	-3.4%	-2.9%	-3.1%	-3.4%
Wales	-5.6%	-5.4%	-4.0%	-3.2%	-3.8%	-4.1%
Scotland	-4.8%	-3.5%	-3.5%	-2.8%	-3.9%	-3.7%
Northern Ireland	-5.5%	-5.1%	-3.5%	-4.0%	-3.8%	-4.2%
All	-5.2%	-4.4%	-3.6%	-3.0%	-3.9%	-3.8%

Source: *The Impact of Tax and Benefit Reforms to be Introduced between 2010–11 and 2014–15 in Northern Ireland* (IFS, 2010)

The IFS analysis discussed above is based on the impact of the tax and benefit reforms by income quintile. An alternative way of assessing the impact would be by expenditure quintile/decile. Some households have an annual expenditure that exceeds their annual income, particularly those towards the bottom of the income

19 *Households Below Average Income – An Analysis of the Income Distribution 1994/95 – 2009/10*, May 2011 (DWP, 2011)

distribution. For these households, their expenditure is not being entirely funded from income. It is possible that, for these households, expenditure is a better indicator of standard of living than income. On this basis, IFS analysis (at a UK level) following the Budget 2011 suggests that the UK Coalition Government's policies are still regressive, with low expenditure households expected to lose more than those in the higher groups.

b. Spatial impacts within Wales

Within Wales, the welfare changes will adversely impact some areas more than others. Undertaking a detailed analysis of the specific impact is limited since individuals will claim a range of different benefits. However, as Table 5 shows, the IFS have estimated the impact on households according to their income. By using this information, we can look at the distribution of income in England and Wales to show the concentration of low-income households in Wales[20]. As Figure 2 (see page 20) shows, low income is particularly concentrated in the South Wales Valleys and the inner city areas of Cardiff, Newport and Swansea. All of the shaded areas in Figure 2 are in the bottom half of the income distribution for England and Wales.

As one would expect, there is a strong correlation between low income households and households that are also claiming out-of-work benefits[21]. Figure 3 (page 20) maps the distribution of out-of-work benefit claimants in Wales. As mentioned above there were around 290,000 people claiming out-of-work benefits in Wales in May 2011. Using the proportion of the population claiming benefits together with the distribution of low income in Wales will tell us the areas in Wales that are most likely to be disproportionately impacted following the welfare changes.

Figure 3 shows that the South Wales Valleys and inner city areas of Cardiff, Newport and Swansea have the highest concentration of benefit claimants. In some of these areas more than 40 per cent of the resident working-age population are claiming out-of-work

[20] The data in Table 5 relates to the income distribution across the UK. We do not have consistent information on the income distribution for the UK as a whole. Figure 2 therefore looks at the income distribution for England and Wales. While excluding Scotland and Northern Ireland may overestimate the number of areas in Wales in the bottom income deciles, the general pattern of low income in Wales will not be affected. Areas that are in the bottom end of the income distribution on an England and Wales basis will also be in the bottom end of the distribution on a UK level.

[21] Out-of-work benefits include Job Seekers Allowance, Employment and Support Allowance, Incapacity Benefit, lone parents and other income-related benefits.

benefits. The distribution of benefit recipients for most of Wales maps across well with the distribution of low income shown in Figure 2. Although some rural areas in Wales are identified as being in the bottom-income deciles, these areas are not associated with high concentrations of households claiming out-of-work benefits. However, it is worth noting that, on average, incomes are higher in rural than non-rural areas.

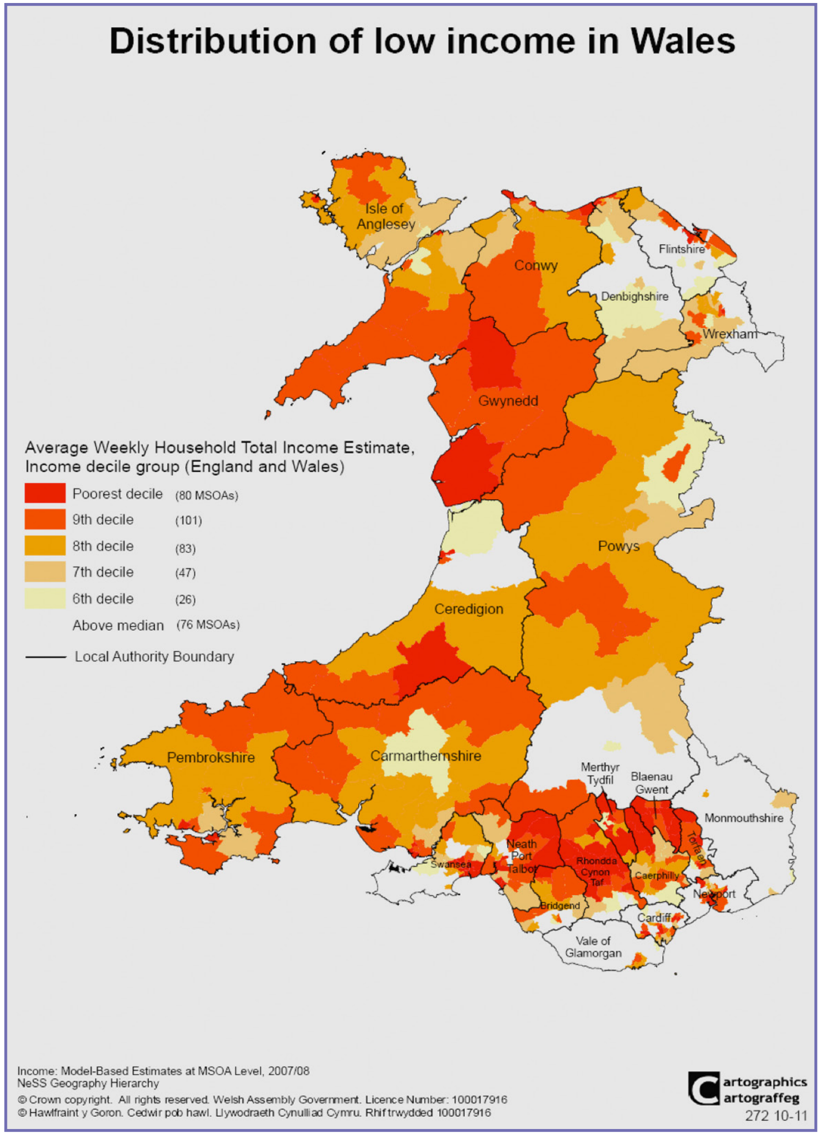
Wavehill Ltd (2011) have undertaken research to investigate the impact of Welfare to Work policy in some of those areas in Wales with high levels of benefit claiming, namely Merthyr Tydfil, Blaenau Gwent and Rhondda Cynon Taff. Given this high dependency on benefits, the report suggests that large numbers of residents within this three-borough area are highly likely to be impacted by the major changes in levels of benefit payments and assessment regimes for particular benefits. For these three boroughs, Wavehill Ltd estimate that the impacts of particular benefits could include[22]:

- '16,900 individuals affected by the introduction of the Work Programme from June 2011
- over 12,000 workless households affected by Tax Credit changes totalling a potential drop in income to 2014 of £8.7 million
- over 33,200 households affected by Housing Benefit changes
- over 25,000 individuals affected by the changes to Incapacity Benefit
- over 39,000 individuals affected by the changes to DLA with a potential reduction in income received of £12.1 million to 2014
- over 5,300 lone parents affected by Income Support changes
- over 6,200 individuals affected by changes to Employment Support Allowance with a potential reduction in income received of £24.8 million by 2014.'[23]

[22] Wavehill's estimates are based on DWP and HM Revenue & Customs (HMRC) official statistics as well as other research including 'From Witney to Wigan: How national changes to welfare benefit rules have a differential impact on local communities' by A Franco (2011).

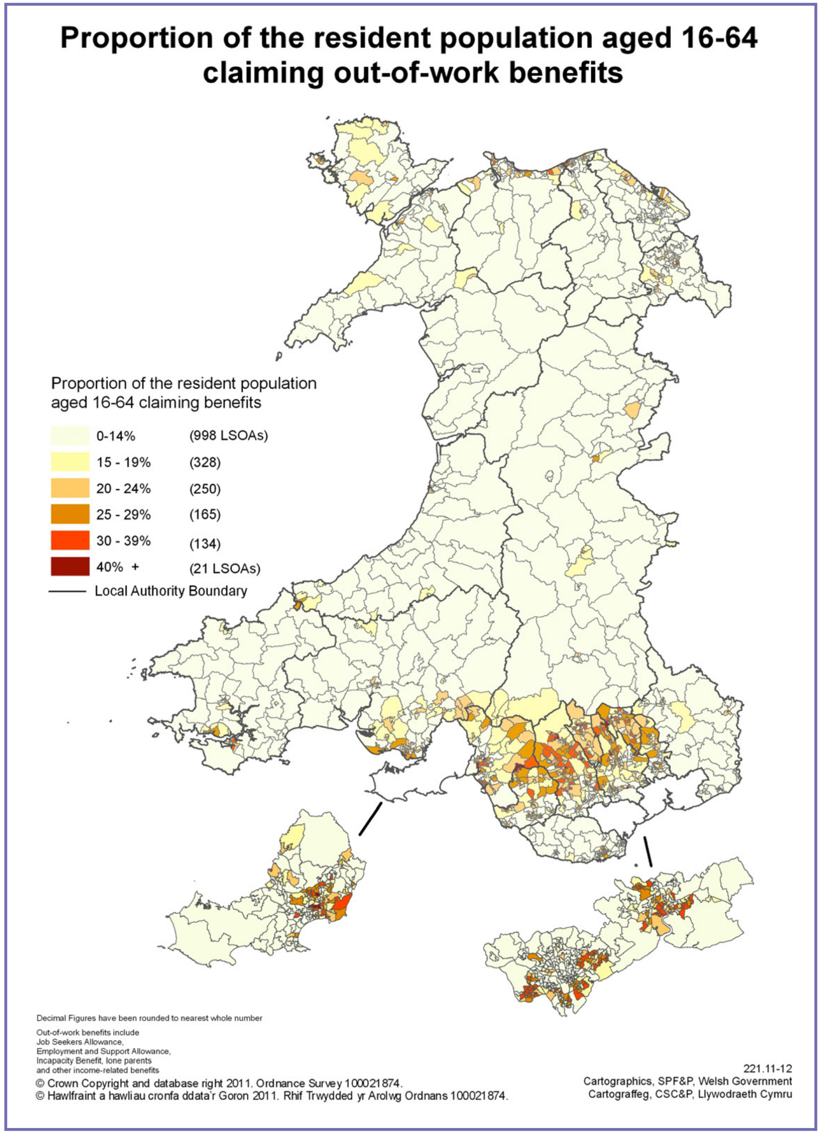
[23] *Research Review of the Impact of Welfare to Work Policy in Merthyr Tydfil, Blaenau Gwent and Rhondda Cynon Taff* (Wavehill, 2011)

Figure 2



Source: ONS, Small Area Income Estimates (2007/08)

Figure 3



Source: DWP Statistics (May 2011)

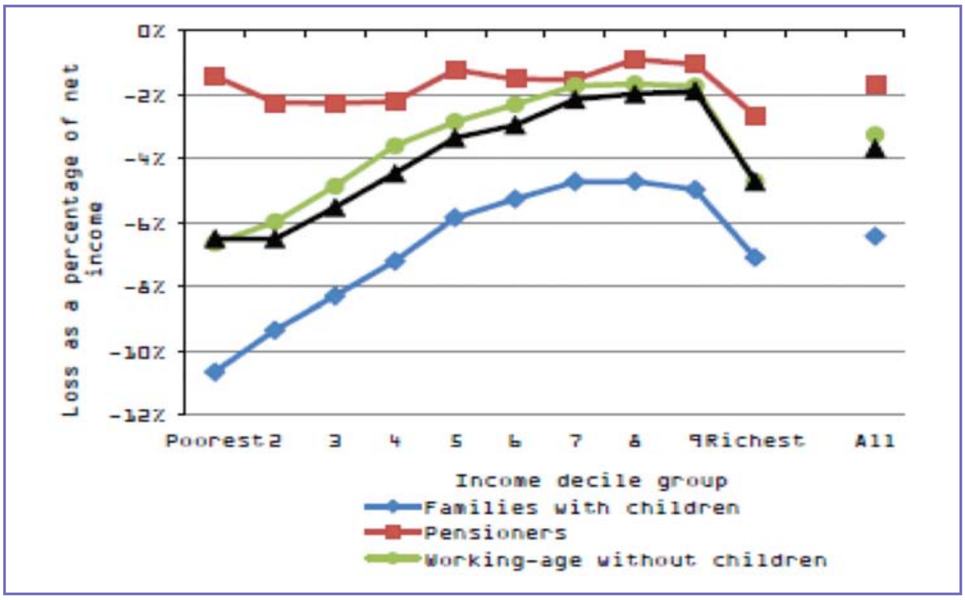
c. Impact by household type

The IFS has also analysed the distributional impact (on net income) of the tax and benefit changes to be introduced between January 2011 and April 2014 on different household types. This analysis has recently been extended to incorporate measures announced in the Autumn Statement 2011 and now also includes a scenario where Universal Credit is fully in place by 2014–15[24]. Although claimants will start to be moved across from the current tax and benefit system to Universal Credit from April 2014, this process will take four years to complete. Therefore, the actual situation in 2014–15 will be somewhere in between the two scenarios analysed (namely with and without Universal Credit). On average the IFS expect this to be closer to the scenario without Universal Credit in place.

Although this analysis was undertaken at a UK level, inferences can be made for Wales. Figures 4 and 5 (page 22) summarise this recent analysis, which illustrates that families with children lose proportionately more of their income across the income distribution compared to all other household types analysed, regardless of whether Universal Credit is accounted for. For example, looking at the scenario before the introduction of Universal Credit we see that, on average, families with children are estimated to lose just over 6 per cent of their income in 2014–15 (or £2,390), compared to just under 4 per cent for all households (or £1,080) and 3 per cent for working-age households without children (or £1,090). Pensioners lose less than 2 per cent of their income (or £320). These findings reflect the cuts to working-age benefits and the greater reliance on benefits of families with children compared to those without children. Wales has a higher proportion of children in families claiming out-of-work benefits compared to England (21.4 per cent and 19.7 per cent respectively[25]). As such, the impact on this household type is likely to be greater in Wales.

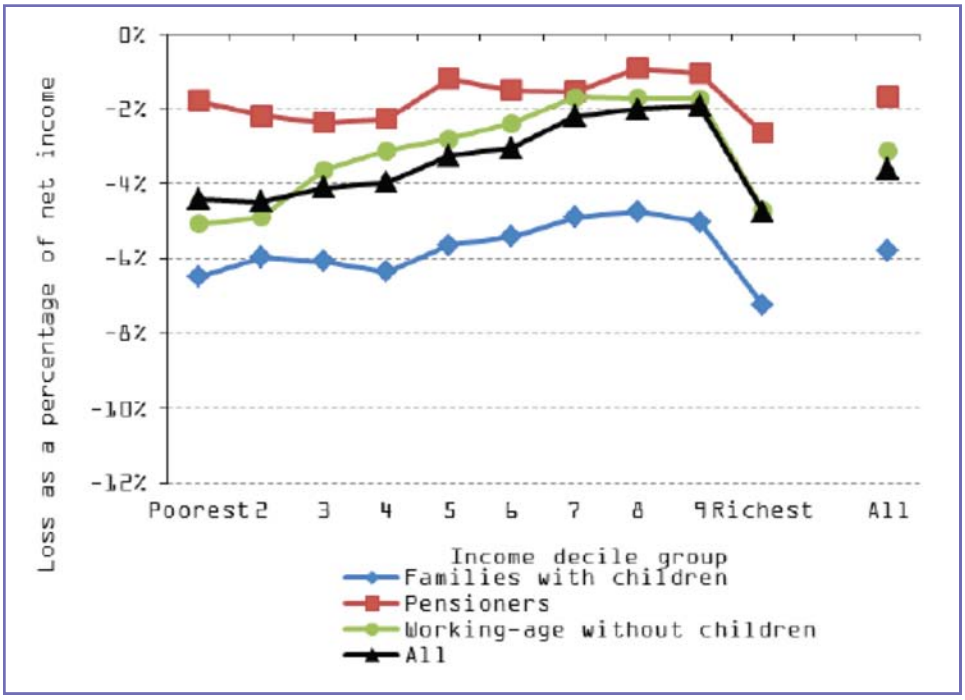
[24] *The Impact of Austerity Measures on Households with Children* (IFS, 2012)
[25] Source: HMRC

Figure 4: Losses from tax and benefit changes to be introduced between January 2011 and April 2014 by income decile group and household type, without Universal Credit



Source: *The Impact of Austerity Measures on Households with Children* (IFS, 2012)

Figure 5: Losses from tax and benefit changes to be introduced between January 2011 and April 2014 by income decile group and household type, with Universal Credit



Source: *The Impact of Austerity Measures on Households with Children* (IFS, 2012)

Furthermore, Figures 4 and 5 also suggest that the poorest households with children will lose the largest proportion of their income as a result of the tax and benefit changes. Under the scenario where Universal Credit is not taken into account, the IFS estimate that on average families with children in the poorest-income decile[26] will lose around 10 per cent of their income in 2014–15 (or £1,810) compared to the situation where no changes are made to the tax and benefit system. This group continues to lose proportionately more than average (at around six per cent or £1,100 per year) even after the introduction of Universal Credit, despite being the group who gain the most from this particular welfare change.

Looking at household types in more detail, non-working lone parents are expected to be hardest hit in terms of their loss as a proportion of income (as illustrated by Figures 6 and 7). They are expected to lose more than 12 per cent of their income on average in 2014–15, equivalent to around £2,050–£2,100 (depending on whether Universal Credit is accounted for). These findings align with earlier analysis on the impact of the tax and benefit changes by gender, which was published by the IFS in summer 2011[27]. This suggests that the tax and benefit reforms to be introduced between 2012–13 and 2014–15 would proportionately reduce the incomes of households with a single woman more than those with a single man. The IFS have attributed this difference to the fact that very few men who live with no other adults are lone parents (over 90 per cent of lone parents are female). Given that lone parents are particularly reliant on income from benefits, they lose a particularly large amount from some of the benefit reforms especially the change to using CPI to uprate benefits each year.

Workless couples with children are also expected to be particularly hard hit by the tax and benefit changes, losing around 11–12 per cent of their income on average in 2014–15 (or around £2,410–£2,800 per year), depending on whether the impact of Universal Credit is included – see Figures 6 and 7.

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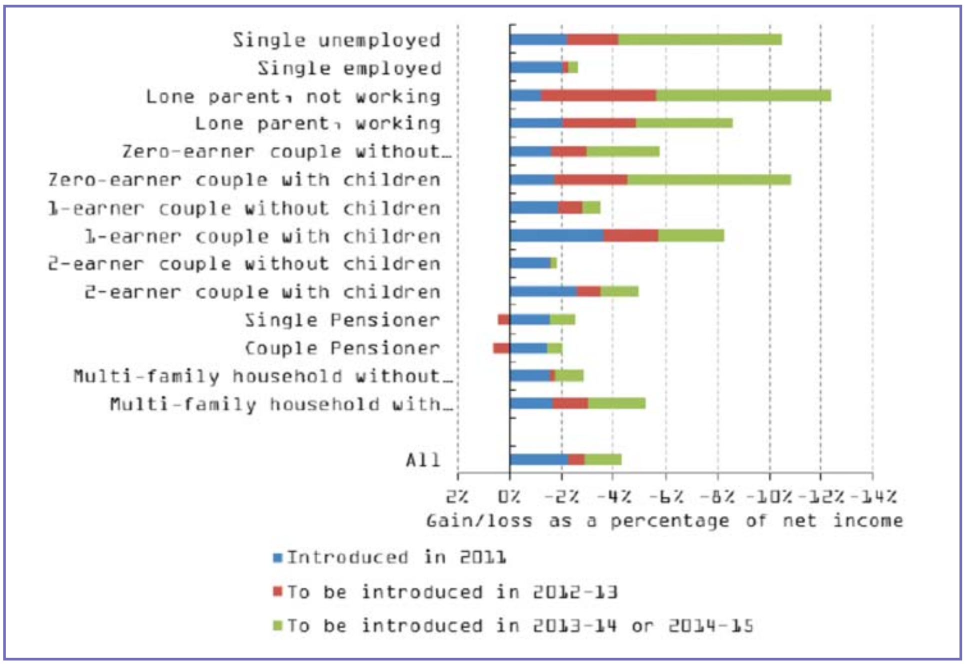
[26] The IFS derive income decile groups by dividing all households into 10 equal-sized groups according to income adjusted for household size using the McClements equivalence scale. Decile group 1 contains the poorest tenth of the population, decile group 2 contains the second poorest, and so on up to decile group 10, which contains the richest tenth.

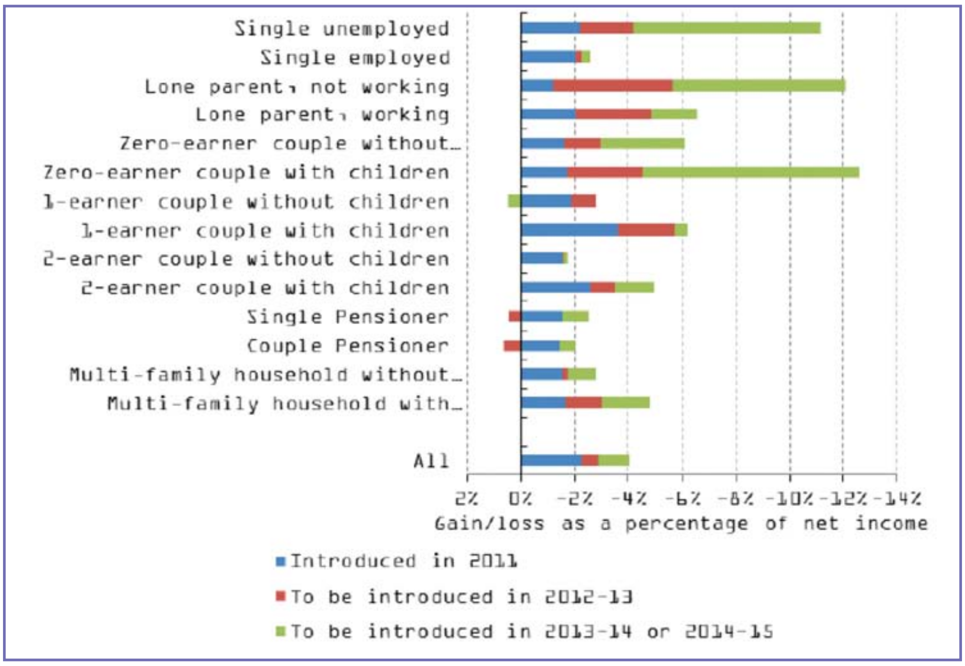
[27] *The impact of tax and benefit reforms by sex: some simple analysis* (IFS, 2011). As this report was published in summer 2011, it does not take into account the tax and benefit changes announced in the Budget 2011 and Autumn Statement 2011. Therefore, the findings underestimate the impact on lone parents as these do not reflect the announcement that the above-inflation increase in the child element of the Child Tax Credit will not go ahead.

Figure 6: Losses for different household types arising from tax and benefit changes to be introduced between January 2011 and April 2014, without Universal Credit



Source: *The Impact of Austerity Measures on Households with Children* (IFS, 2012)

Figure 7: Losses for different household types arising from tax and benefit changes to be introduced between January 2011 and April 2014, with Universal Credit



Source: *The Impact of Austerity Measures on Households with Children* (IFS, 2012)

The proportion of children in workless households in Wales is higher than in the UK – 19.4 per cent for Wales compared to 16.2 per cent for the UK (Quarterly Labour Force Survey data for 2009–11). As such, any negative impacts on this household type are expected to be felt disproportionately in Wales.

The IFS has also investigated how the impact of tax and benefit changes varies according to the number of children in a household and the age of the youngest child. The findings suggest that the fall in family incomes will be worse for those families with two or more children, who are estimated on average to lose around 6–10 per cent of their income in 2014–15 (depending on whether or not Universal credit is accounted for and how many children they have). The average loss for all households with children is around 6 per cent. Large families are more likely to be in the lower income groups (which are hardest hit by the regressive nature of the welfare changes). They are most reliant on benefits and therefore lose the most from the planned welfare cuts to be introduced between 2012–13 and 2014–15. They will be particularly hit by the benefit cap to be introduced in 2013–14. However, in the longer run, the IFS expect the introduction of Universal Credit to somewhat lessen the impact. As well as hitting large families hard, according to the IFS, the benefit cap will also disproportionately impact families living in high-rent areas. As rents in Wales are lower than in the UK, the effect of this change, while negative, should be less adverse than in Great Britain. Indeed, the recently updated DWP impact assessment for the Household Benefit Cap estimates that fewer than 3 per cent (under 2,000) of the affected households in the UK will be in Wales.

With regards to the impact of the age of the youngest child in the household, the IFS point out that the difference between households is less remarked than that for the number of children in a household. Under both the 'with and without Universal Credit' scenarios, households with a youngest child aged 0–4 or 5–10 lose more than the average household with children, whereas households with a youngest child aged 11–18 fare better (but are still negatively impacted). Households with newborns are particularly affected by some of the changes introduced in April 2011 including the abolition of the baby element of tax credits and the restriction of the Sure Start Maternity Grant to the first child. These households are also likely to lose more than average from the reduction in the childcare element of the Working Tax Credit from April 2011. As households with older children are less likely to use childcare they are less affected. Furthermore, IFS analysis notes that households with older children are more likely to have two earners rather than one. This household type loses less from the welfare cuts in 2013–14 and 2014–15 as a proportion of income than other households with children, also suggesting that households with older children will be less affected.

The distributional impact among households with children by housing tenure has also been investigated by the IFS. Under the without Universal Credit scenario, households who rent (in both the social and private rented sector) lose around 9 per cent of their income in 2014–15, a greater loss than that for households that are mortgaged or owned outright (around 6 per cent). This is because households with children who rent are more likely to be poorer on average, and as mentioned poorer families with children are expected to lose more on average than richer ones (especially from the changes in later years). In particular, those in social rented accommodation who are considered to be under-occupying their home will be negatively affected by the cuts to housing benefit for this group (in 2013–14), while those in the private rented sector will be particularly affected by the changes to Local Housing Allowance in 2011. However, the IFS expect the introduction of Universal Credit to significantly reduce the average loss for private and social rented households. This is because those in rented accommodation and in paid employment gain the most from Universal Credit given that one of its key aims is to strengthen the financial incentive to work, particularly for those with the weakest work incentives (e.g. renters under the current system). Therefore this group will receive an increased amount of benefit if they undertake paid employment.

With regards to pensioners, Figures 4 and 5 (above) illustrate that this household type is least affected by the tax and benefit changes across the income distribution. This is because benefits for pensioners have not been significantly affected by the welfare cuts affecting those of working age. Also, pensioners do not pay National Insurance contributions and therefore will be unaffected by the increases in these rates. Analysis in *Average losses for pensioner households from tax and benefit changes to be introduced between January 2011 and April 2014* (IFS, 2011) suggests that the key measures negatively affecting pensioners are the increase in the standard VAT rate to 20 per cent and the decision to uprate most disability benefits in line with the CPI. Working-age adults without children in the upper-middle of the income distribution also lose a relatively low proportion of their income from the tax and benefit changes because they are unaffected by welfare cuts and gain the most from policies such as increasing the income tax personal allowance.

d. Impact on work incentives

In addition to assessing the impact of the tax and benefit changes on household incomes, the IFS has examined the impact on both the incentive to do paid work at all and the incentive for those currently in paid work to increase their earnings[28] over the period 2010–2014. These incentives are measured by the Participation Tax Rate (the proportion of earnings lost in either higher taxes or lower benefit entitlements when an individual enters work) and the Marginal Effective Tax Rate (the percentage of a small increase in earnings that is lost in tax or lower benefit entitlement) respectively.

The IFS analysis suggests that the tax and benefit changes (including Universal Credit) to be introduced by 2014 will, on average, strengthen the incentive for the population as a whole to undertake paid work. 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. This is mainly due to the reforms to income tax personal allowance, National Insurance and the CPI-indexation of out-of work benefits.
- **Those with children:** on average, financial work incentives for lone parents are expected to be significantly strengthened (particularly due to the impact of Universal Credit). While on average, couples with children are likely to have a slightly weakened incentive to undertake paid work (partly as a result of the changes to the tax credit system).

It is worth noting that although the tax and benefit changes (including Universal Credit) to be implemented by 2014 are expected to strengthen the incentive to undertake paid work for most subgroups of the population, on average, work incentives are expected to be weakened for a second earner in a couple (for those with and without children).

With regards to the incentives for those in paid work to earn more, IFS analysis suggests that the reforms to be introduced by 2014 (including Universal Credit) will weaken the incentive to earn more, on average, for the population as a whole. With regards to the impact on particular subgroups of the population, on average, the incentive to increase earnings for those without children (both single people and couples) is expected to be weakened, as is the case for

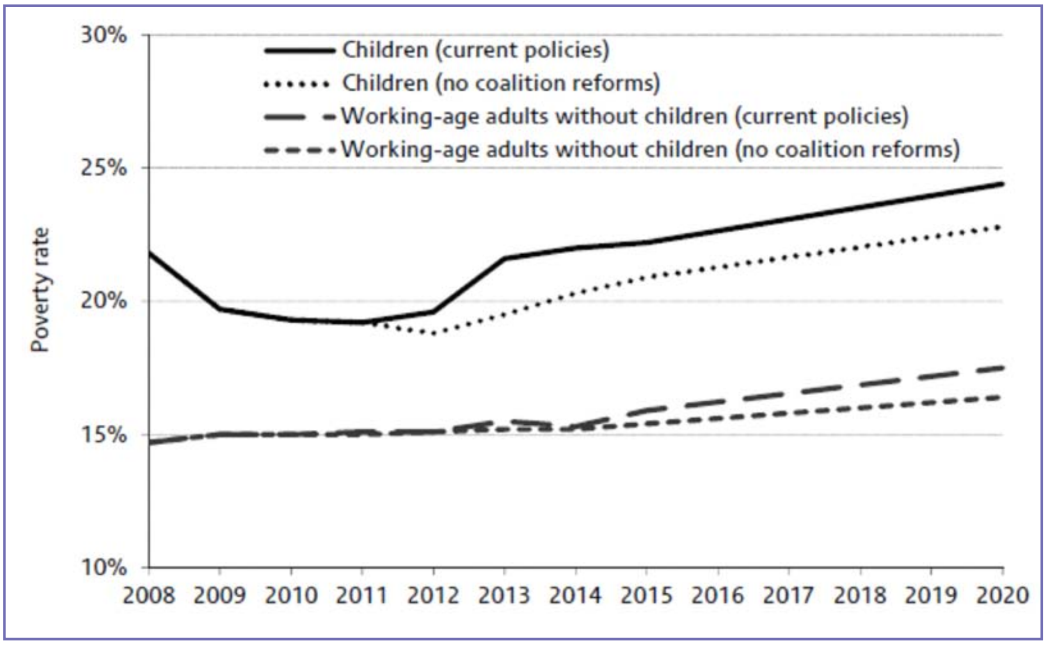
[28] This analysis can be found in the report *The Impact of Austerity Measures on Households with Children* (IFS, 2012)

couples with children. However, on average, lone parents are likely to have a significantly strengthened incentive to earn more mainly due to the impact of Universal Credit.

4. Impact on poverty

The IFS has also estimated the direct impact on poverty (at a UK level) of the tax and benefit reforms announced by the Coalition Government by comparing the forecasts with a projection which assumed that none of the government reforms were introduced[29]. As Figure 8 illustrates, the Coalition welfare reforms announced up until summer 2011 are expected to raise relative income poverty[30] among families with children more than among working-age adults without children[31].

Figure 8: Projected relative income poverty rates before housing costs under current policies and without the Coalition Government's tax and benefit reforms.



Source: *Child and Working-Age Poverty from 2010 to 2020* (IFS, 2011)

[29] Source: *Child and Working-Age Poverty from 2010 to 2020* (IFS, 2011).

[30] As set out in the Child Poverty Act (2010), an individual is in relative income poverty in a particular year if their household income is less than 60 per cent of the national median household income in that year. An individual is in absolute income poverty in a particular year if their household income in that year is less than 60 per cent of the 2010–11 national median (in real terms).

[31] It is worth noting that in the years preceding the current period, there has been a long-term erosion of means-tested benefit levels relative to average earnings for working-age adults without children (based on DWP benefit data and ONS earnings indices).

As illustrated by Figure 8, the IFS estimate that the Coalition Government's reforms will have a negative impact on child poverty. For 2012–13 their analysis suggests that the reforms will increase relative child poverty in the UK by about 100,000, absolute child poverty by about 200,000, and absolute poverty among working-age adults without dependent children by about 100,000. Welsh Government provisional estimated proportionate shares for Wales adjusted for differences in poverty are 6,000, 10,000, and 5,000 respectively[32]. In 2013–14, IFS projections for the UK suggest that Coalition Government reforms will increase both relative and absolute poverty by around 300,000 children and 100,000 working-age adults without dependent children. Welsh Government provisional estimated proportionate shares for Wales adjusted for differences in poverty are an increase in relative and absolute child poverty of 17,000 and 16,000 respectively. Both absolute and relative poverty among working-age adults in Wales is estimated to increase by 5,000. Beyond 2013, the reforms have a slightly smaller overall effect on relative child poverty (due to the introduction of Universal Credit) while absolute child poverty remains fairly constant. As mentioned above, the reforms are expected to have larger effects on relative and absolute poverty among those of working age without children as time goes on.

Although Universal Credit in isolation is expected to reduce relative poverty significantly, this will be more than offset by the poverty-increasing impact of the government's other changes to the tax and benefit system, particularly the change to CPI indexation (IFS, 2011). However, the IFS suggest that wider economic conditions, such as high inflation and weak earnings growth, will have a greater impact on poverty levels than the welfare reforms.

Until recently, HM Treasury analysis concluded that the reforms would not have a negative impact on relative income child poverty through to 2012–13. However, their most recent distributional analysis that accompanies the Autumn Statement 2011 estimates that the reforms will increase relative child poverty in the UK by around 100,000 in 2012–13 (Welsh Government provisional estimated share for Wales is 6,000[33]). This is due to their modelling now including the LHA reforms, and also due to the impact of the tax credit cuts announced in the Autumn Statement 2011.

32 Estimates calculated by Knowledge and Analytical Services, Welsh Government. They are based on the population of children in Wales relative to the UK adjusted by the ratio of child poverty in Wales to child poverty in the UK. Figures are before housing costs and are rounded to the nearest 1,000.

33 Ibid

It is important to note that the impact on poverty will be affected by the behavioural response following the reforms. For example, the UK Government expects a number of the welfare reforms to increase the incentive for individuals to become active in the labour market. The behavioural response will however, be dependent on wider economic conditions. It is planned that Stage 2 of the Welsh Government's programme of work to analyse the impact of the welfare reforms will try to estimate these likely responses under a range of scenarios for the economy in Wales.

5. Wider economic impacts

In assessing the potential magnitude of loss to Wales from the welfare reforms it is necessary to consider second round or multiplier effects, which attempt to quantify the additional effects of a policy change beyond those that are immediately measurable.

As per the approach taken by the IFS, it is assumed that the tax and benefit reforms do not change households' labour supply decisions. On this basis, the reduction in income in Wales resulting from benefit cuts will be larger than the 'headline' reduction because of second round or multiplier effects. The multiplier effect captures, for example, the effect of reduced spending by benefit recipients on goods and services, which in turn might reduce employment in businesses in Wales that experience lower demand. As the negative impact on household income is estimated to be more severe in Wales, the negative impact on businesses in Wales could also be felt with greater force. The total effect of the welfare reforms would therefore equal the effect of the policy measures times the multiplier.

It is difficult to quantify precisely multiplier effects but broadly speaking evidence suggests that each £1 of income lost could be associated with a total loss of income in Wales somewhere in the range of £1– £1.50[34]. In other words the multiplier is likely to be in the range of 1.0–1.5 (with the mid-point of 1.25 providing a central estimate). This should be regarded as an interim assumption pending fuller analysis at Stage 2. It is important to note that this initial analysis does not incorporate potential labour supply responses. If these were to be accounted for, the multiplier effects would be smaller, and could even be positive if people move into work. Therefore, the magnitude of impact largely depends on external factors such as the labour market and wider economic conditions.

[34] Estimates calculated using *The Input-Output Tables for Wales 2007* (Welsh Economy Research Unit, 2010).

Given the regressive nature of the welfare reforms, it is useful to look at data from the Living Costs and Food Survey (2010), which reports on household expenditure by income. This shows that households in the lowest-income decile group spent a larger proportion of their total average weekly expenditure on housing, fuel and power (23 per cent), and food and non-alcoholic drinks (15 per cent), than those in the highest-income decile group (8 per cent in both cases). This suggests that businesses related to these sectors in Wales will be particularly affected by the likely reduced consumption by affected benefit claimants. However, it is important to note that not all of Welsh household expenditure will take place in Wales and the extent of this impact will also depend on the income elasticity of demand associated with these goods and services (i.e. the responsiveness of the demand for goods to a change in the income of the people demanding those goods). Transport, and recreation and culture are likely to be less affected as households in the lowest-income decile group spend proportionately less on these commodities and services compared to the highest-income decile.

The distribution of income, and also benefit claimants, in Wales provides an indication of the areas in Wales that are most likely to be adversely impacted following the welfare changes. As mentioned above, there is a strong correlation between the distribution of low-income households and households that are also claiming benefits. These households are particularly concentrated in the South Wales Valleys and the inner city areas of Cardiff, Newport and Swansea.

6. Wider social impacts

Research on the potential wider social impacts of recently introduced and future planned welfare reforms appears to be quite limited. However, a small selection of research studies relating to past changes made to the welfare system that are of relevance to the welfare reforms announced by the Coalition Government have been drawn upon.

Clearly, estimated impacts of past welfare reforms will be influenced by the specific policy changes made. For example a study by Machin and Marie (2006) investigated the impact on crime since the introduction of the Jobseeker's Allowance to the UK labour market in 1996, which involved imposing sanctions on people who did not fulfil the job-search requirements. There was also a reduction in the duration of non-means-tested contributory benefits from 12 months to 6 months. Although the study focuses on this particular policy, it does have broad similarities to the welfare reforms announced more recently in that there was a general toughening and tightening of the benefit regimes through cuts to benefits (leading to a reduction in income) and sanctions. Thus, despite the focus on this particular benefit reform, the findings are potentially of general applicability and relevance to other welfare-to-work programmes. In particular, it has notable similarities to the conditionality requirements under Universal Credit and time-limiting the contributory element of Employment and Support Allowance.

The research findings show that the areas in the UK that were more affected by the introduction of JSA had greater increases in crime rates. These were also the areas with higher outflows from unemployment, with those people dropping off the register tending not to move into work (education or training, or onto other benefits). In studying the relationship between crime and sanctions after the introduction of JSA, the research confirms that those areas where more people were sanctioned were those where crime rose by more. As such these results seem to suggest that benefit cuts and sanctions in JSA shifted people off the benefit system leading to reduced income and increased crime rates.

Other research of relevance has investigated the timing and frequency of welfare payments on levels of crime. For example, Foley (2009) undertook analysis of patterns of crime in 12 US cities to see if there was any relationship with the cycle of welfare payments. The findings reveal that criminal activity was increasing in the amount of time that had passed since welfare payments occurred. This reflects an increase in crimes with a direct financial motivation (e.g. burglary and motor vehicle theft) given the raised incentive to supplement welfare income with criminal income. Temporal patterns in crime were not observed where welfare payments were relatively more frequent. This suggests that welfare beneficiaries consume welfare-related income quickly and then attempt to supplement it with criminal income. As well as smoothing patterns in crime, this study also suggests that more frequent welfare payments may lead to lower crime rates under certain assumptions. These findings are particularly relevant to Universal Credit given that this is planned to be paid monthly, replacing mainly fortnightly payments. This aims to help smooth the transition into work. However, as suggested there may be unintended consequences on crime as a result of this policy. As with the wider economic impacts, it is important to note that any potential social impacts on crime that may result from the welfare reforms will be highly dependent on behavioural responses particularly in relation to the labour market.

With regards to the potential impact of the Coalition Government's welfare reforms on health, it appears that limited analysis has been undertaken. This is mainly due to modelling approaches by the IFS and

DWP being static in nature. As a result, to our knowledge, the dynamic impacts of policy changes (e.g. the increased number of people in work and associated benefits such as health impacts) have not been included in any modelling. As well as wider economic conditions, the overall impact on individuals will also depend on which specific benefits they are claiming and the changes made to each of those benefits.

DWP do note in a number of their impact assessments relating to the Welfare Reform Bill 2011 that the welfare policies could have positive impacts on health if they lead to more people moving into work. This earned income would compensate for the loss of welfare income resulting from benefit cuts and sanctions. DWP refer to evidence that shows that work is generally good for physical and mental health and well-being, including for disabled people and people with health conditions, and may help to promote recovery. In addition, DWP note that if a parent moves into work, potentially lifting the family out of poverty and providing a better lifestyle, this may result in an increase in their child's welfare. Whereas being out of work often leads to poorer health as well as other negative outcomes[35]. This is especially true given the links between income and health, with those on low incomes having higher rates of disease, ill health and mortality than those on high incomes. However, DWP suggest that evidence is limited as to whether a change in income has an effect on health[36]. Health impacts of welfare reform policies will be considered in more detail by DWP upon further development of each policy. Further research into the wider social impacts of the welfare reforms will be undertaken as part of Stage 2 of this programme of work.

Next steps

The above analysis forms Stage 1 of the programme of work to analyse the impact of the UK Government's welfare reforms in Wales. Information on the next stage of this research, Stage 2, can be found at Annex 1. It is currently anticipated that this will be completed around the end of 2012.

Knowledge and Analytical Services, Welsh Government
February 2012

35 Abolition of concessionary Employment and Support Allowance (ESA) 'youth' National Insurance qualification conditions – Impact assessment (DWP, 2011). *Is work good for your health and well-being?* by G Waddell and A Burton (Department for Work and Pensions, 2006)

36 Disability Living Allowance Reform – Impact assessment (DWP, 2011). 'Determining the effect of change in income on self-rated health using regression models – ordered, linear, fixed or random?' by F I Gunasekara, K Carter, T Blakely and I Liu (2009)

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www.ifs.org.uk/publications/5440

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'Crime and Benefit Sanctions' by S Machin and O Marie in *Portuguese Economic Journal* Volume 5(2), pages 149–165 (August 2006)

'Determining the effect of a change in income on self-rated health using regression models – ordered, linear, fixed or random?' F I Gunasekara, K Carter, T Blakely and I Liu (2009)

Disability Living Allowance Reform – Impact assessment (DWP, 2011)

Employment and Support Allowance: Work Capability Assessment – Official Statistics for Wales, October 2011 (Table 1) (DWP, 2011)

'From Witney to Wigan: How National Changes to Welfare Benefit Rules have a Differential Impact on Local Communities' by A Franco (2011)

Households Below Average Income – An Analysis of the Income Distribution 1994/95 – 2009/10, May 2011 (DWP, 2011)

Household Benefit Cap – Impact assessment (DWP, 2012)

Housing Benefit equality impact assessment (DWP, 2011)

Housing Benefit – Uprating Local Housing Allowance Rates by CPI from April 2013 – Impact assessment (DWP, 2011)

Impacts of Attendance Allowance and Disability Living Allowance on Older People in Wales (LE Wales, 2011)

Impacts of DLA on working age people in Wales (LE Wales, 2011)

Impacts of Housing Benefit Proposals: Changes to the Local Housing Allowance to be introduced in 2011–12 (DWP, 2010)

Is work good for your health and well-being? by G Waddell and A Burton (DWP, 2006)

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Small Area Income Estimates, 2007/08 (Office for National Statistics, 2011)

Spending Review 2010 (HM Treasury, 2010)

The Impact of Austerity Measures on Households with Children (IFS, 2012)
www.ifs.org.uk/publications/5973

The impact of tax and benefit reforms by sex: some simple analysis (IFS, 2011)
www.ifs.org.uk/publications/5610

The Impact of Tax and Benefit Reforms to be Introduced between 2010–11 and 2014–15 in Northern Ireland (IFS, 2010)
www.ifs.org.uk/publications/5369

The Input-Output Tables for Wales 2007 (Welsh Economy Research Unit, 2010)

Time Limiting Contributory element of Employment and Support Allowance – Impact assessment (DWP, 2011)

Under-occupation of social housing – Impact assessment (DWP, 2011)

'Welfare Payments and Crime' – NBER Working Paper by CF Foley

Annex 1: Programme of work to analyse the impact of the UK Government's welfare reforms in Wales

Aims

There are two significant areas of analysis that will be covered by the programme of work:

- the first is to get a better understanding of what the cumulative impact of all the changes to welfare and the benefits system will be on the individuals and households in Wales. This will need to look at a number of different scenarios for people in different circumstances receiving different benefits
- the second is to estimate the impact on organisations administering the current programmes and the potential impact on the delivery of devolved services in Wales.

Approach

Estimating the impact of the UK Government's welfare reforms is a difficult task due to the complexity of the current system and the range of likely responses from individuals and households in Wales following the changes. This is especially difficult to predict before the reforms have been implemented. Due to these issues, we are following a three-stage approach. Stage 1 has involved analysis of the existing evidence on the cumulative impacts with a second stage to commission extensions to this existing evidence base to investigate the impact in Wales in more detail. A third stage is then proposed that attempts to investigate the potential impact of specific cross-cutting reforms such as the Universal Credit if deemed necessary.

Stage 1

The first stage of the impact assessment has aimed to analyse the existing evidence of the likely impact on individuals and households in Wales by looking at the welfare reform measures as a package.

This analysis includes the following.

1. A summary of the main welfare reform policy announcements (**Annex 2**).
2. Estimation of the number of individuals that will be impacted by the reforms in Wales.
3. An assessment of the expected monetary impact:
   a) a comparison of the estimated impact in Wales compared to the UK as a whole and the other countries and regions of the UK

b) an assessment of the likely spatial impacts within Wales
c) disaggregation of the impacts of the main reforms according to the characteristics of the individual and/or household in Wales (including income group, families with children, lone parents, working-age adults without children, pensioners, and workless households)
d) analysis of impacts on work incentives.

4. Assessment of the impact on poverty, including child poverty.

5. Analysis of the wider economic impacts (e.g. multiplier effects of a decrease in income on local economies).

6. Assessment of the wider social impacts such as the potential impact on crime and health in Wales.

Stage 1 has also included an assessment of the administrative impacts that the welfare reforms are likely to have on delivery agents in Wales.

Stage 2

Much of the analysis published to date does not include estimates of the likely behavioural response following the reforms. These behavioural responses are important to understand in order to estimate the likely medium-term impact in Wales. For example, the UK Government expects a number of the welfare reforms to increase the incentive for individuals to become active in the labour market. The likely behavioural response will however be dependent on wider economic conditions. 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.

This analysis is likely to include the following.

1. Evidence on how individuals/households are likely to respond following the reforms.

2. How the reforms are likely to change the demand for public services in Wales.

3. How the reforms are likely to change expenditure patterns and further consideration of the wider economic impacts.

4. Further assessment of the wider social impacts such as the potential impact on crime and health in Wales.

5. How the impact of the welfare reforms may change depending on a range of scenarios for the economy in Wales.

Stage 2 will also try to estimate the cumulative impact of the main welfare reforms in isolation (i.e. excluding potential impacts of the tax changes) on household income Wales. It is currently anticipated that Stage 2 will be completed around the end of 2012.

Stage 3

If deemed necessary, the third stage could involve estimating the impact of specific welfare reforms that are likely to have particular cross-cutting impacts. Stage 3 would include much of the analysis undertaken during Stages 1 and 2 but for any specific reform where it is deemed that additional evidence is required.

Annex 2: A summary of the welfare reform policy announcements

June Budget 2010 policy decisions, £ million

	2010–11	2011–12	2012–13	2013–14	2014–15
Welfare measures	**385**	**2,010**	**4,710**	**8,150**	**11,040**
Benefits, tax credits and public service pensions: switch to CPI indexation from 2011–12	0	1,170	2,240	3,900	5,840
Disability Living Allowance: reform gateway from 2013–14	0	0	0	360	1,075
Lone-parent benefits: extend conditionality to those with children aged 5 and above from October 2011	0	0	50	150	180
Health in Pregnancy Grant: abolish	40	150	150	150	150
Sure Start Maternity Grant: apply to first child only from 2011–12	0	75	75	75	75
Support for Mortgage Interest: set payments at the average mortgage rate from October 2010	15	-75	-10	40	65
Saving Gateway: not introduce in July 2010	10	0	75	110	115
Housing Benefit reforms					
Local Housing Allowance: set at the thirtieth percentile of local rents from 2011–12	0	65	365	415	425
Deductions for non-dependents: reverse previous freezes on uprating and maintaining link with prices from 2011–12	0	125	225	320	340
Social sector: limit working-age entitlements to reflect size of family from 2013–14	0	0	0	490	490
Switch to CPI indexation for Local Housing Allowance from 2013–14	0	0	0	300	390
Reduce awards to 90% after 12 months for claimants of Jobseekers Allowance	0	0	0	100	110
Additional bedroom for carers from 2011–12	0	-15	-15	-15	-15
Local Housing Allowance: caps on maximum rates for each property size, with 4-bed limit from 2011–12	0	55	65	70	65

Additional Discretionary Housing Payments from 2011–12	0	-10	-40	-40	-40
Tax Credit reforms					
Tax credits second income threshold: reduce to £40,000 from 2011–12	0	140	145	155	145
First and second withdrawal rates: increase to 41% from 2011–12	0	640	710	730	765
Child Tax Credit: taper the family element immediately after the child element from 2012–13	0	0	510	515	480
Child Tax Credit: remove the baby element from 2011–12	0	295	275	270	275
Working Tax Credit: remove the 50-plus element from 2012–13	0	0	35	40	40
Child Tax Credit: reverse the supplement for children aged one and two from 2012–13	0	0	180	180	180
Reduce the income disregard from £25,000 to £10,000 for two years in 2011–12 then to £5,000 from 2013–14	0	105	140	340	420
Introduce an income disregard of £2,500 for falls in income from 2012–13	0	0	550	560	585
New claims and changes of circumstances: reduce backdating from 3 months to 1 month from 2012–13	0	0	315	320	330
Child Tax Credit: increase the child element by £150 in 2011–12 and £60 in 2012–13 above indexation	0	-1,200	-1,845	-1,930	-1,995
Child Benefit: freeze rates for three years from 2011–12	0	365	695	940	975
Basic State Pension: introduce triple guarantee from 2011–12	0	0	-195	-420	-450
Pension Credit Minimum income guarantee: matching basic State Pension cash increase in 2011–12	0	-415	-535	-535	-535
Child Trust Funds: phased abolition of Government contributions from 2010–11	320	540	550	560	560

Spending Review 2010 Annually Managed Expenditure (AME) policy decisions, £ million

	2011–12	2012–13	2013–14	2014–15
Welfare measures	**320**	**2,555**	**5,990**	**7,040**
Contributory Employment and Support Allowance: time limit for those in the Work Related Activity Group for one year	0	1,025	1,530	2,010
Housing Benefit: increase age limit for shared room rate from 25 to 35	0	130	225	215
Total household benefit payments capped on the basis of average take-home pay for working households	0	0	225	270
Disability Living Allowance: remove mobility component for claimants in residential care	0	60	130	135
Savings Credit: freeze maximum award for four years from 2011–12	165	215	260	330
Support for Mortgage Interest: extend temporary changes to waiting period and capital limit until January 2012	-70	-20	0	0
Cold Weather Payments: increase rate permanently to £25 from November 2010	-50	-50	-50	-50
Council Tax Benefit: 10% reduction in expenditure and localisation	0	0	485	490
Child Benefit: remove from families with a higher-rate taxpayer from January 2013	0	590	2,420	2,500
Working Tax Credit: freeze in the basic and 30-hour elements for three years from 2011–12	195	415	575	625
Working Tax Credit: reduce payable costs through childcare element from 80% to 70% restoring 2006 rate	270	320	350	385
Child Tax Credit: increase the child element by £30 in 2011 and £50 in 2012	-190	-510	-545	-560
Working Tax Credit: increase working hours requirement for couples with children to 24 hours	0	380	385	390
Child and Working Tax Credits: use real-time information	0	0	0	300

Budget 2011 policy decisions, £ million

	2011–12	2012–13	2013–14	2014–15
Welfare measures	**30**	**-70**	**-50**	**-35**
Housing Benefit: not introduce reductions for long-term jobseekers	0	0	-105	-115
Disability Living Allowance: mobility components for claimants in residential care	0	-75	0	0
Local Housing Allowance: transitional protection for existing claimants	30	-30	0	0
Employment and Support Allowance Youth: abolish National Insurance concession	0	10	10	15
Benefit fraud: sanctions and debt recovery	0	25	45	65

Autumn Statement 2011 policy decisions, £ million

	2011–12	2012–13	2013–14	2014–15	2015–16	2016–17
Welfare measures	**0**	**1,240**	**1,245**	**1,295**	**1,270**	**1,275**
Child Tax Credit: remove over-indexation	0	975	955	1,020	995	995
Working Tax Credit: freeze	0	265	290	275	275	280