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Income inequality in the UK

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Summary

This briefing presents statistics on income inequality, focussing on disposable incomes (income including benefits and after direct taxes).

The Gini coefficient for income inequality summarises income inequality into a single number between 0 and 100%, where a higher percentage means more unequal. The Gini coefficient was **35%** before housing costs and **39%** after housing costs in 2022/23.

A couple without children with disposable income below **£300** per week before housing costs were lowest-income 10% of households in 2022/23. To be in the highest-income 10% required an income four times higher, of at least **£1,200** per week.

In 2021/22, 37% of total disposable household income in the UK went to the fifth of individuals with the highest household incomes, while 8% went to the fifth with the lowest.

Trends in income inequality

Inequality in household incomes in the UK has remained at a roughly similar level since the early 1990s but is higher than during the 1960s and 1970s. While the share of income going to the top 1% of individuals by household income increased during the 1990s and 2000s, there was some reduction in inequality among the rest of the population (based on incomes before housing costs) with the result that inequality overall was fairly stable during this period.

The rising cost of living

The Office for Budget Responsibility forecasted in March 2024 that real household disposable income per person, a measure of living standards, will increase by 0.1% in 2024 and then by 1.7% in 2025. Based on these forecasts, real (inflation-adjusted) post-tax income per person will return to its pre-pandemic level (Q4 2019) in Q4 2025.

The budgets of low-income households are most affected by the rising cost of living. ONS data shows that households with the lowest incomes experience a higher than average inflation rate, while the highest-income households experienced lower than average inflation.

According to the Resolution Foundation, in 2023/24 real incomes will be relatively stable across the income distribution, but in 2024/25, there will be a 1% fall for households with the bottom half of incomes (not including pensioners) and a 1% rise for the top half. This will mean a sharp increase in the Gini coefficient in 2024/25.

Income inequality between regions, ethnic groups, and disability status

Historically, household income across the UK has varied significantly between regions and countries, ethnic groups, and the disability status of households.

The West Midlands (£553) had the lowest median income before housing costs in 2020/21 to 2022/23, while London (£735) had the highest. Households from a Bangladeshi ethnic group (£416) had the lowest median incomes before housing costs while households from an Indian ethnic group (£700) had the highest. Families with a disabled member had a median income of £549 before housing costs during this period, compared to £682 for households where nobody was disabled.

International comparisons

OECD figures suggest that the UK has among the highest levels of income inequality in the European Union (as measured by the Gini coefficient), although income inequality is slightly lower than in the United States.

1 A picture of income in the UK

1.1 What do we mean by income?

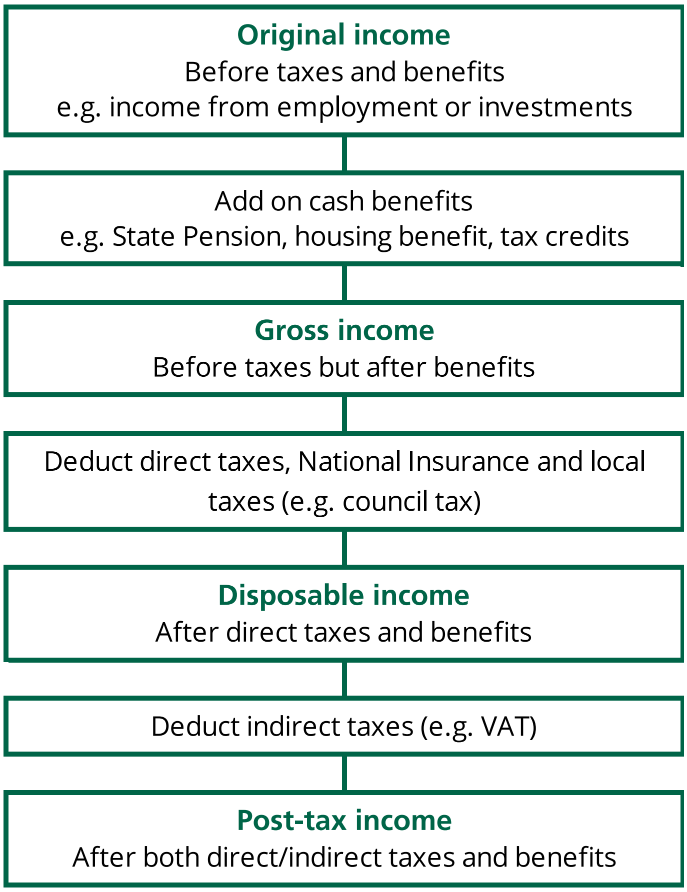
Individuals and households can get income from a range of sources. These include earnings from employment, cash benefits, income from investments, private pensions, and other forms of income. Some of this income may be taxed.

The two most common measures of income are:

- **Gross income** means the sum of all income before tax, including cash benefits.
- **Disposable income** means the amount left after direct taxes, National Insurance contributions and council tax (or Northern Ireland rates) are deducted from gross income.

The flowchart summarises the different stages of household income:[1]

[1] Adapted from ONS, The Effects of Taxes and Benefits on Household Income, Financial Year Ending 2014, 29 June 2015, Diagram A



Household living standards

This note focuses on household incomes, rather than incomes of individuals. Household income is likely to prove a better guide to living standards than income of individuals, since we may expect income to be shared between household members. Certain forms of income are also determined by household composition – for example, tax credit awards or child benefit payments.

Equivalisation: larger households need larger incomes

Statistics on household incomes are often **equivalised** (adjusted for household size and composition) to enable better comparisons of living standards. A large household is likely to need a higher level of income in order to enjoy the same standard of living as a smaller household.

Income before and after housing costs

Disposable income may be measured before or after deducting housing costs. There is more inequality in income after housing costs than in income before housing costs, as poorer households tend to spend a higher share of their income on housing than those higher up the income distribution.

A before housing costs measure acknowledges that some households may choose to pay more for housing so that they can have a better quality of accommodation. On the other hand, variations in housing costs do not always reflect differences in housing quality (for example, due to geographical variations), in which case an after housing costs measure is more helpful.

Income and wealth

This briefing does not discuss inequalities in household wealth. While income measures the flow of money to a household at a single point in time, wealth can be built up and retained over many years. Consequently, inequality in household wealth tends to be greater than inequality in income. Statistics on the distribution of household wealth are provided in the ONS report, Household Total Wealth in Great Britain: April 2018 to March 2020.

1 Measuring living standards: an expenditure approach

Measurement of inequality in household living standards tends to focus on differences in income. However, income may not be the best guide to a household's standard of living as some families have high or low incomes only temporarily.

An alternative is to assess living standards based on household expenditure. Households experiencing a temporary drop in income may sustain their previous spending patterns by drawing on savings or taking on debt, because they expect their income to increase again. Under-reporting appears to be less of a problem when measuring expenditure than when measuring income: surveys find that households with the lowest reported incomes are not the lowest spenders.

To expenditure we can also add benefits derived from goods bought previously that are still being 'consumed' (for example, housing or cars). This gives a more positive picture of living standards for households who may be on low incomes but own their own home.

An expenditure approach is not perfect. As with income-based measures, it does not take into account improvements in living standards arising from investment in public services. The survey used to collect data on household spending, the Living Costs and Food Survey, has fewer respondents than the Family Resources Survey used to collect incomes data.[2]

[2] For further information on the relative merits of assessing living standards based on consumption instead of income see: Mike Brewer and Cormac O'Dea, Measuring living standards with income and consumption: evidence from the UK, ISER Working Paper 2012-05, March 2012; Mike Brewer, Ben Etheridge and Cormac O'Dea, Why are households that report the lowest incomes so well-off?, University of Essex Department of Economics Discussion Paper series, No 736, April 2013

1.2 Collecting data on incomes via surveys

Official statistics on household incomes are primarily collected through two large household surveys: the Family Resources Survey and the Living Costs and Food Survey. This note uses data from both surveys.

The two surveys use slightly different definitions of income, so results are not directly comparable. The Family Resources Survey also has a larger survey sample of over 19,000, though due to Covid-19 restrictions, the 2020/21 sample was 10,000 the 2021/22 sample was 16,000. In 2022/23, the FRS sample was just over 25,000 households. The Living Costs and Food Survey collects information from around 5,500-6,000 households.

Surveys may not perfectly record all income received by a household and may struggle to obtain accurate data for certain groups of households. Collecting accurate data on incomes of very high-income or low-income households is a particular challenge. Therefore, the Family Resources Survey adjusts the reported incomes figures for those households in the survey with the very highest incomes, using data on individual income from HMRC's Survey of Personal Incomes (which is based on tax returns). This helps correct for volatility in the survey figures.[3] There is no such adjustment in the Living Costs and Food Survey. Neither survey applies an adjustment to income figures for households reporting the lowest income.

Additionally, the surveys underestimate the total amount of benefit income received by households compared to administrative data for government expenditure on benefits. Analysis by the Resolution Foundation indicates that there was an unexplained gap of £37 billion between benefit income reported in the Family Resources Survey in 2016/17 and what the government actually spent. This represented around 4% of total disposable household income as recorded in the survey. The gap has also increased over time, from around 2% of total income at the start of the 2000s.[4] The box in section 2.1 looks at how this under-reporting might affect estimates of income inequality levels in the UK.

Sources

Incomes data from the Family Resources Survey is published in an annual publication from the Department for Work and Pensions, Households Below Average Income. The latest data are for 2022/23 and were published on 21 March 2024.

Data from the Living Costs and Food Survey is published by the Office for National Statistics (ONS) in Household income inequality, UK: Financial year ending 2022, which provides data for 2021/22. The Living Costs and Food

3 For more details, see DWP, Households Below Average Income (HBAI) Quality and Methodology Information Report, 2017-18, p20

4 Resolution Foundation, The Living Standards Audit 2018, 24 July 2018

Survey also collects data on household expenditure, published in the ONS Family Spending release.

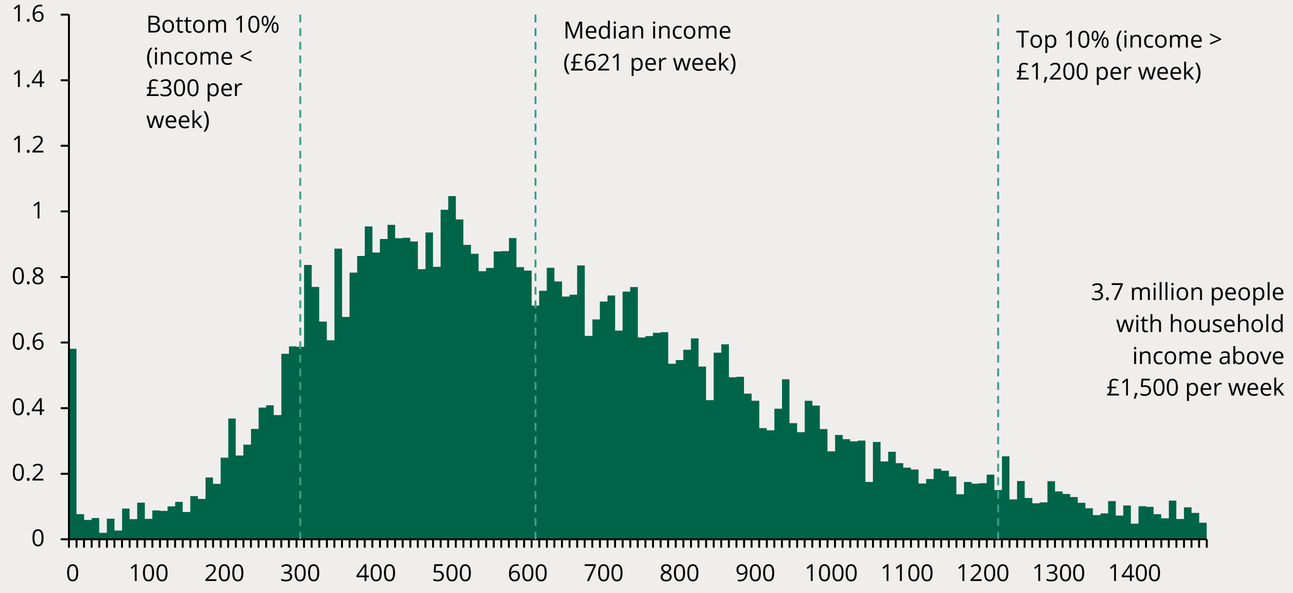
For further information on the surveys and related publications see ONS, A guide to sources of data on earnings and income.

1.3 What counts as high and low income?

As noted above, analysis of the income distribution tends to concentrate on equivalised disposable household incomes. The chart shows the distribution of incomes on this basis in the latest year.

The distribution of household income in the UK, 2022/23

Number of people in each £10 band of weekly disposable household income (millions)



Note: Income figures are equivalised and are measured before deducting housing costs

Source: DWP, Households below average income, 1994/95 to 2022/23, data behind chart 1.2 (before housing costs)

The equivalisation process adjusts reported income figures according to household size and composition (using a reference point of a childless couple). This is because a larger household is likely to need a higher income to enjoy the same standard of living as a smaller household.[5] So what income is received by different family types at different points along the distribution?

[5] Figures are adjusted using the OECD equivalence scale for income before housing costs. A single adult is given a weight of 0.67; each additional adult in the household or child aged 14 and over is given a weight of 0.33; each child under 14 years has a weight of 0.2. Therefore, a couple without children has a weight of 0.67+0.33=1; a couple with two children under 14 has a weight of 0.67+0.33+0.2+0.2 = 1.4. Different equivalence scales may be applied to income after housing costs.

Disposable income (before housing costs)

An individual was at the **middle** of the distribution in 2022/23 if they lived in a household which had total disposable weekly household income of:[6]

- £621 for a couple with no children,
- £416 for a single person with no children,
- £665 for a single person with two children aged under 14,
- £870 for a couple with two children aged under 14.

An individual was in the **bottom 10%** if they had household income less than:

- £300 for a couple with no children,
- £201 for a single person with no children,
- £321 for a single person with two children aged under 14,
- £420 for a couple with two children aged under 14.

An individual was in the **top 10%** if they had household income greater than:

- £1,200 for a couple with no children,
- £804 for a single person with no children,
- £1,284 for a single person with two children aged under 14,
- £1,680 for a couple with two children aged under 14.

Gross income

Disposable income is income after income tax, National Insurance, council tax and domestic rates, contributions to occupational pension schemes and student loan repayments, among other items. Therefore, it is not perfectly correlated with gross income: households with the same gross income may face different deductions (for example, a household with two earners on £10,000 per year will pay less in income tax than a household with one earner on £20,000). Therefore, someone with a relatively high gross income may occupy a lower position on the distribution of disposable income, and vice versa.[7]

6 DWP, Households below average income: 1994/95 - 2022/23, Table 2.2db and Library calculations using the OECD equivalence scale for income before housing costs

7 There is no specific equivalisation scale for gross income so when comparing between family types, we must use the same equivalisation scale as for disposable income before housing costs. Estimates are not directly comparable with estimates for gross household income published in the National Accounts or other sources.

An individual was at the **middle** of the gross income distribution in 2022/23 if his or her gross weekly household income was:[8]

- £775 for a couple with no children,
- £519 for a single person with no children,
- £829 for a single person with two children aged under 14,
- £1,085 for a couple with two children aged under 14.

8 DWP, Family Resources Survey, via Stat-Xplore

2 Indicators of income inequality

2.1 Gini coefficient

The Gini coefficient for income inequality was 35% before housing costs and 39% after housing costs in 2022/23.

A widely used indicator of income inequality is the Gini coefficient. This summarises inequality in a single number which takes values between 0 and 100%. A higher value indicates greater inequality.

In the UK, inequality as measured by the Gini coefficient increased during the 1980s but from 1990 onwards has remained more stable, based on data from the Family Resources Survey. The latest estimate is for 2022/23 and shows that the Gini coefficient for the UK was 35% based on income before housing costs and 39% based on income after housing costs. Inequality levels are higher based on income after housing costs because lower-income households tend to spend a larger share of their income on housing than higher-income households.

The Gini coefficient in 2022/23 was one percentage point higher than the previous year, both before and after housing costs.

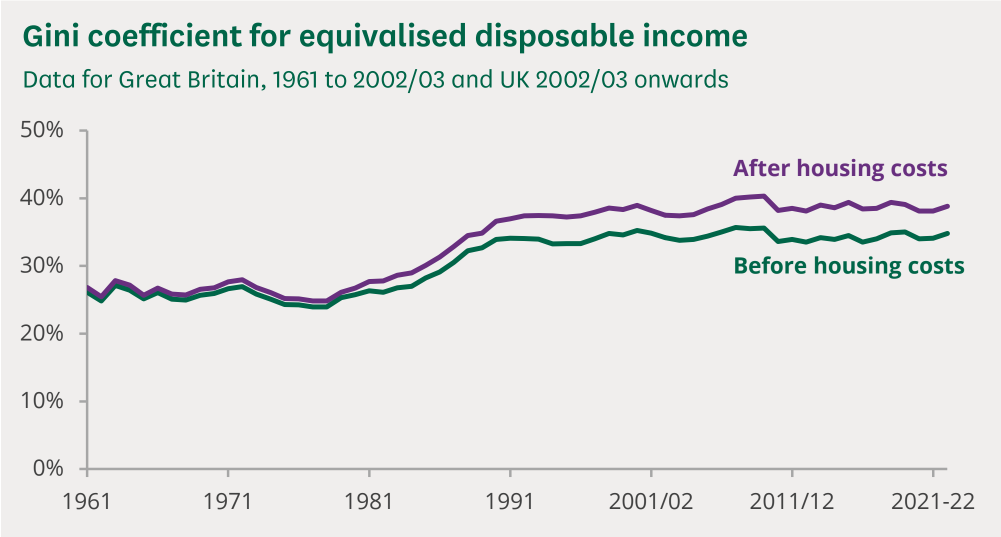
The Institute for Fiscal Studies found that since 2011/12 there has been little growth in incomes in the bottom half of the income distribution, particularly the bottom 10%, where there was essentially no growth between 2013/14 and 2020/21. This is partly because the growth rate in employment income was lower for lower-income households, and partly because employment income makes up a smaller share of net income for poorer households, as poorer households also receive benefits.[9]

In the year to 2022/23, incomes for those in the bottom 80% fell before housing costs and incomes for those in the top 10% increased.

Incomes fell for the bottom 10% between 2019/20 and 2022/23, but not as much as median incomes. This was due to temporary increases in benefits during coronavirus lockdowns and increased support for low-income households during the period of high inflation.[10]

9 IFS, Living standards, poverty, and inequality in the UK: 2021, 8 July 2021

10 IFS, Living standards since the last election, 21 March 2024



Source: Institute for Fiscal Studies, using data compiled from Family Expenditure Survey and Family Resources Survey

Income inequality on this measure was slightly lower in 2022/23 than it was immediately before the economic recession began in 2008. Between 2009/10 and 2010/11, the Gini coefficient fell by 2 percentage points based on incomes before housing costs (from 36% to 34%) as a result of real incomes at the top of the distribution falling by more than at the bottom of the distribution.[11] The IFS explains:

> The primary reason for the fall in inequality was that real earnings fell sharply while benefit entitlements remained relatively stable. Median income for non-working households (including pensioners) was 60% of that of working households in 2007/08, but 67% by 2012/13.[12]

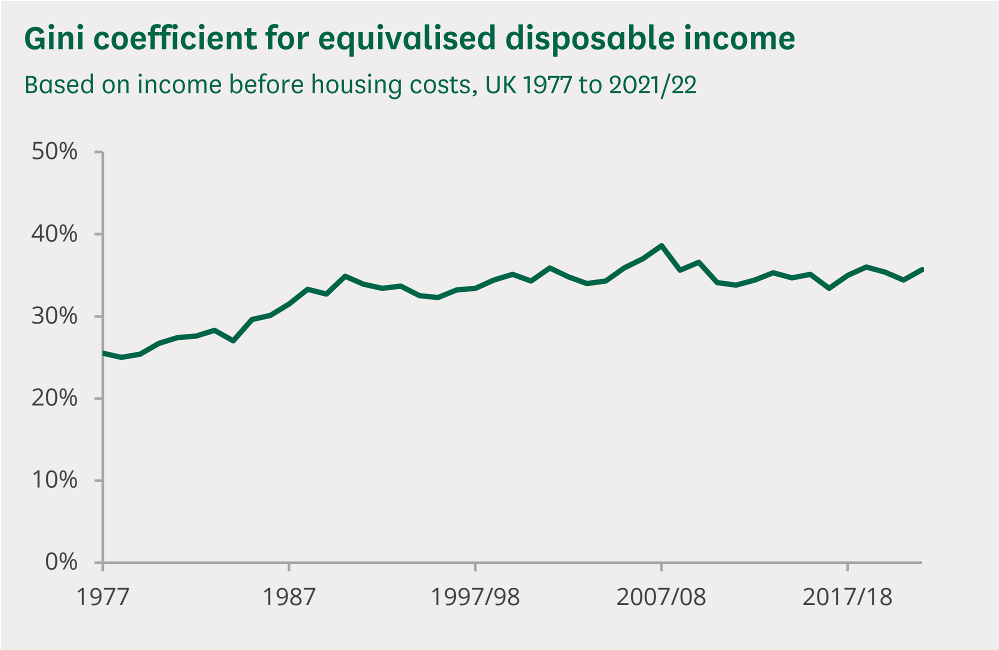
The longer-term picture shows that income inequality rose sharply during the 1980s, before largely stabilising in the 1990s.[13]

These figures are based on analysis of the Family Resources Survey although a broadly similar picture emerges using data from the Office for National Statistics' Living Costs and Food Survey. There are small differences arising between the two sources which partly reflect different methodologies. ONS has published a time series from 1977 onwards – figures are on a before housing costs basis only.

11 DWP, Households below average income, 2020/21 (and 2010/11 edition)

12 C Belfield, J Cribb, A Hood and R Joyce, Living standards, poverty and inequality in the UK: 2014, 15 July 2014, IFS Report R96, Chapter 3, p34

13 Resolution Foundation, Last year saw living standards stagnate and poverty rise, blog post by Adam Corlett, 28 March 2019



Source: ONS, Household income inequality, UK: Financial year ending 2022, using data from the Living Costs and Food Survey and Family Expenditure Survey

2 Are levels of income inequality overstated? The effect of under-reporting of benefit income in household surveys

As discussed in section 1.2, the household income surveys underestimate the amount of benefit income received by households compared to what the government actually spends on benefits. The size of this discrepancy has increased over time.

The Resolution Foundation has adjusted Family Resources Survey data for 1994/95 to 2016/17 so that total benefit income in the survey balances with administrative data on benefit expenditure.

The analysis shows that levels of income inequality are reduced once we factor in the missing benefit income in the survey data. (This is not surprising, as we would expect benefits to have a redistributive effect.) The Gini coefficient was around 2-3% points lower over the period based on the adjusted data, both before and after housing costs. Other measures of income inequality are also revised down. However, inequality still remains some way above the levels seen in the 1960s and 1970s.

Trends in inequality since 1994/95 also appear slightly more favourable using the adjusted data, although the Resolution Foundation comments, “The big picture remains that inequality has been broadly flat but high over this period”.

The DWP is now able to link at least 95% of survey responses to its administrative data.[14] In future, this should allow incorrect survey responses about benefits income to be corrected.

2.2 Percentile ratios

An alternative way of looking at inequality is to compare incomes at different points along the income distribution.

A person at the 90th percentile of the income distribution (a relatively high income) had an income **4 times higher** than someone at the 10th percentile (a relatively low income) in 2022/23, before housing costs.

The P90/P10 ratio compares income for someone at the 90th percentile of the distribution (the point at which 90% of individuals have lower household income and 10% have higher income; a relatively high income) with the 10th percentile (the point at which 10% have lower income and 90% have higher income; a relatively low income).

- The **P90/P10 ratio** was 4.0 in 2022/23 based on incomes before housing costs, meaning someone at the 90th percentile had a household income four times larger than someone at the 10th percentile. The ratio was 5.0 on an after housing costs basis.
- Similarly, the **P90/P50 ratio** compares the 90th percentile with the 50th percentile (i.e. the median). This ratio was 2.0 based on incomes before housing costs and 2.1 after housing costs in 2022/23.
- The **P50/P10 ratio** compares the median with the 10th percentile. This ratio was 2.0 based on incomes before housing costs and 2.4 after housing costs in 2022/23.

All three ratios increased during the 1980s (see charts below). However, the sharp increase in the P50/P10 ratio during the second half of the decade contrasts with a more gradual rise in the P90/P50 ratio since the late 1970s. Based on income before housing costs, the P90/P10 and P50/P10 ratios were slightly lower in 2022/23 than in 1990.

After housing costs, the P50/10 ratio reached a record high of 2.54 in 2018/19, although it has since fallen to 2.39 in 2022/23. In contrast, the 90/10 and 90/50 have largely stayed at a similar level since just before the financial crisis. This suggests the middle is catching up to the top and the bottom is falling further behind.[15]

These percentile ratios show inequality is higher when income is measured after housing costs. The inclusion or exclusion of housing costs makes a

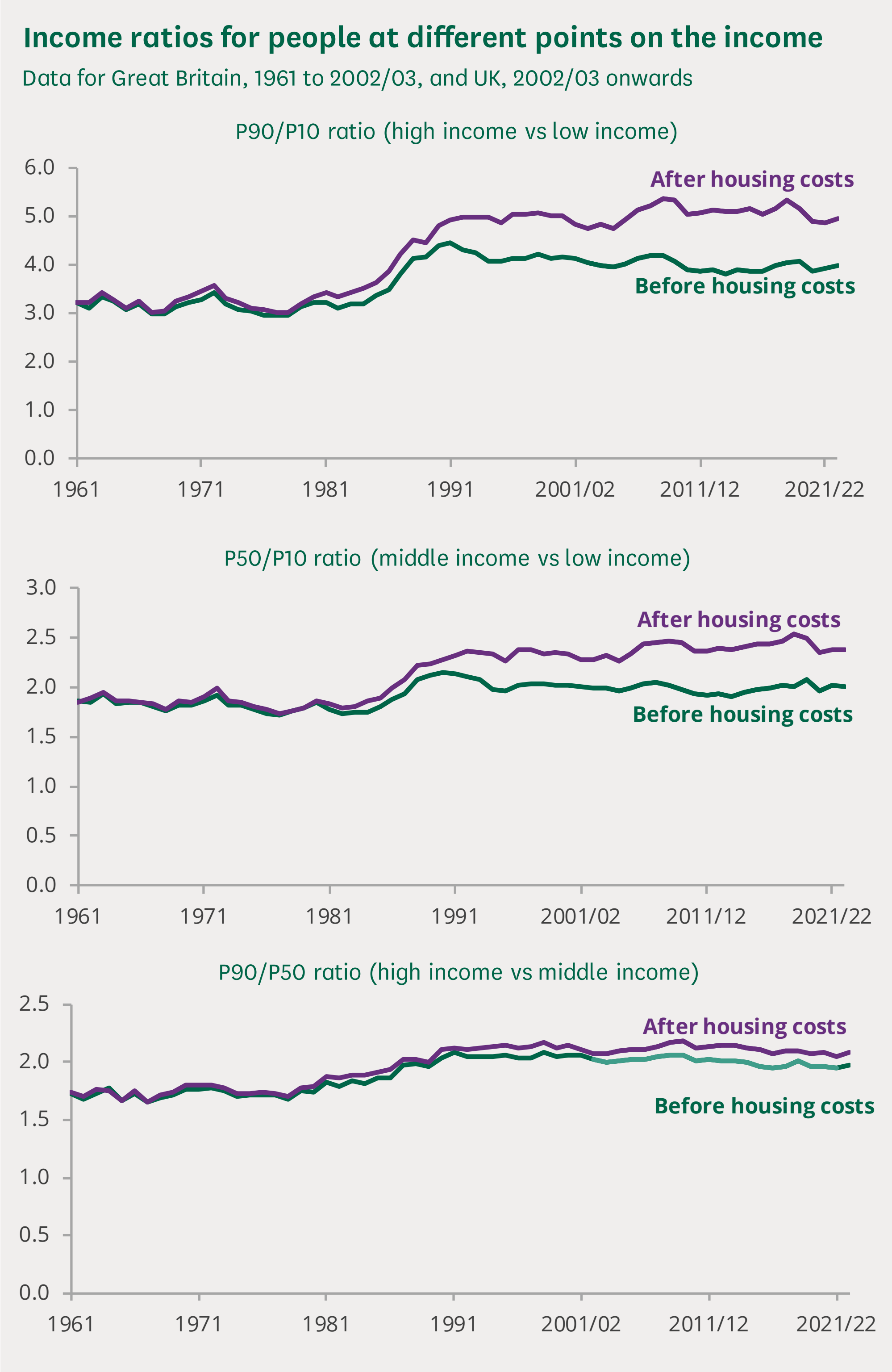
[14] Department for Work and Pensions, Statistical work programme, 4 March 2024, section 2.4

[15] Resolution Foundation, The Living Standards Audit 2020, 21 July 2020

greater difference at the lower end of the distribution, as can be seen by comparing the P50/P10 chart with the P90/P50 chart.

Since the 2008 recession, there has been a substantial fall in housing costs for higher-income households: these households are more likely to own their home so have benefited from the low mortgage rates offered in recent years. This has acted to increase incomes at the top of the distribution relative to incomes at the bottom, thus offsetting some of the fall in inequality in before housing costs income since the recession.[16] The increase in mortgage rates in autumn 2022 meant income after housing costs fell for those who own their home with a mortgage, but an increase in rent did the same for private renters.

[16] For further discussion, see: C Belfield, J Cribb, A Hood and R Joyce, Living standards, poverty and inequality in the UK: 2014, 15 July 2014, IFS Report R96, pp41-44



Source: [Institute for Fiscal Studies](), using data compiled from Family Expenditure Survey and Family Resources Survey, Households below average income, 2022/23

2.3 Income shares

The 20% of people with the highest household incomes received 37% of total disposable income before housing costs.

Income inequality can also be considered in terms of the share of total household income going to different groups.

In 2021/22, 37% of total disposable household income in the UK went to the fifth of individuals with the highest household incomes, while 8% went to the bottom fifth.[17]

The share of income going to the top income quintile (top fifth) increased during the 1980s while the share going to lower-income households decreased. ONS estimates for 1977 onwards are shown in the chart.

Note the composition of each quintile group is in flux: households may move in and out of the top fifth (or other 20% bands) from year to year.

Quintile shares of equivalised disposable income

% share of total income (before housing costs) going to each quintile: UK, 1977 to 2021/22

Source: ONS, Household income inequality, UK: Financial year ending 2022, using data from the Living Costs and Food Survey and Family Expenditure Survey

Top 1% income share

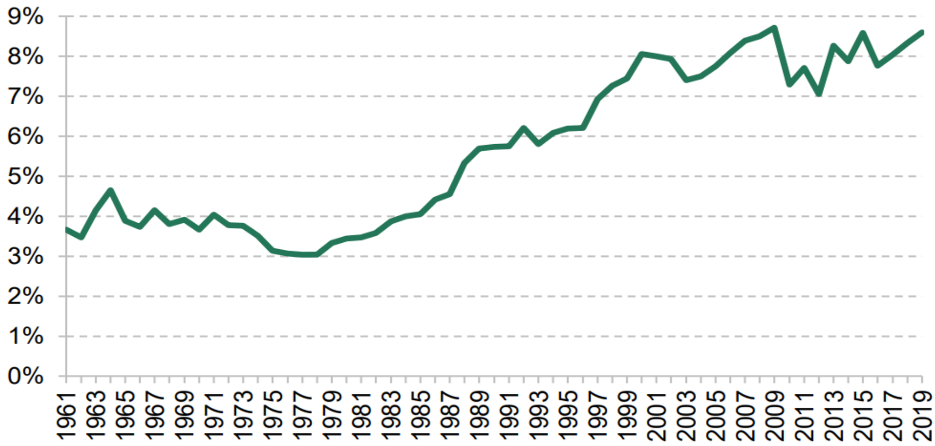
The indicators discussed so far only capture to a very limited extent the inequality between individuals with the very highest incomes and the rest of the population. Although the share of income going to the top 20% levelled off from the start of the 1990s, the share of income going to the top 1% continued to increase into the 2000s.

The Institute for Fiscal Studies (IFS) has calculated the share of household income going to the top 1% of individuals from 1961 up to 2019/20, although it

17 ONS, Household income inequality, UK: Financial year ending 2022, using data from the Living Costs and Food Survey and Family Expenditure Survey

has noted the household surveys used to produce these estimates are not a robust source of information on incomes of the very rich. The chart below is taken from the IFS report Living standards, poverty, and inequality in the UK: 2021.[18]

Figure 2.10. Share of net household income going to the top 1%



Note: Great Britain only. Financial years since 1994.

Source: Authors' calculations using the Family Expenditure Survey and the Family Resources Survey, 1961 to 1993 and 1994–95 to 2019–20.

Source: Institute for Fiscal Studies, Living standards, poverty, and inequality in the UK: 2021, 8 July 2021

This series is sensitive to changes in the tax system. Most recently, some of the decrease in the top 1% share between 2015/16 and 2016/17 may reflect individuals bringing income forward into 2015-16 to avoid paying higher taxes on dividends after April 2016.[19]

Likewise, the fall in the top 1% share in 2010/11 may be partly explained by the introduction of the 50% additional rate of income tax in April 2010, as high income individuals brought income forward into 2009/10 in order to pay less tax. The reduction in the additional rate of income tax in April 2013 (from 50% to 45%) is similarly likely to explain some of the dip in the top 1% share in 2012-13 and subsequent increase in 2013/14, as individuals shifted income between years in order to benefit from the change.[20]

The increase in the share of income going to the top 1% during the 1990s and 2000s contrasts with the relative stability in the Gini coefficient and the modest decrease in the P90/P10 ratio. This suggests that if we exclude the very top end of the income distribution, then incomes must have become more equal across the rest of the income distribution over this period. Previous IFS research explains:

[18] Institute for Fiscal Studies, Living standards, poverty and inequality in the UK: 2021, 8 July 2021

[19] See for example H Miller and B Roantree, Tax revenues: where does the money come from and what are the next government's challenges?, IFS Briefing Note BN198, 1 May 2017

[20] J Cribb, A Hood, R Joyce and D Phillips, Living Standards, Poverty and Inequality in the UK: 2013, 14 June 2013, IFS Report R81, pp39-40

> "To get a sense of the difference the 'racing away' of top incomes over the long run has made to changes in the Gini coefficient, we can calculate the Gini just for the bottom 99%, excluding the effect of increasing inequality between the top 1% and the bottom 99% (and changes in inequality within the top 1%). Over the past two decades, income inequality among the whole population has remained unchanged: the Gini coefficient in 2011-12 was not statistically significantly different from its 1991 value. However, inequality among the bottom 99% has fallen: the Gini coefficient for the bottom 99% was 5% lower in 2011/12, at 0.30, than in 1991, when it was 0.314 (and the difference was statistically significant)."[21]

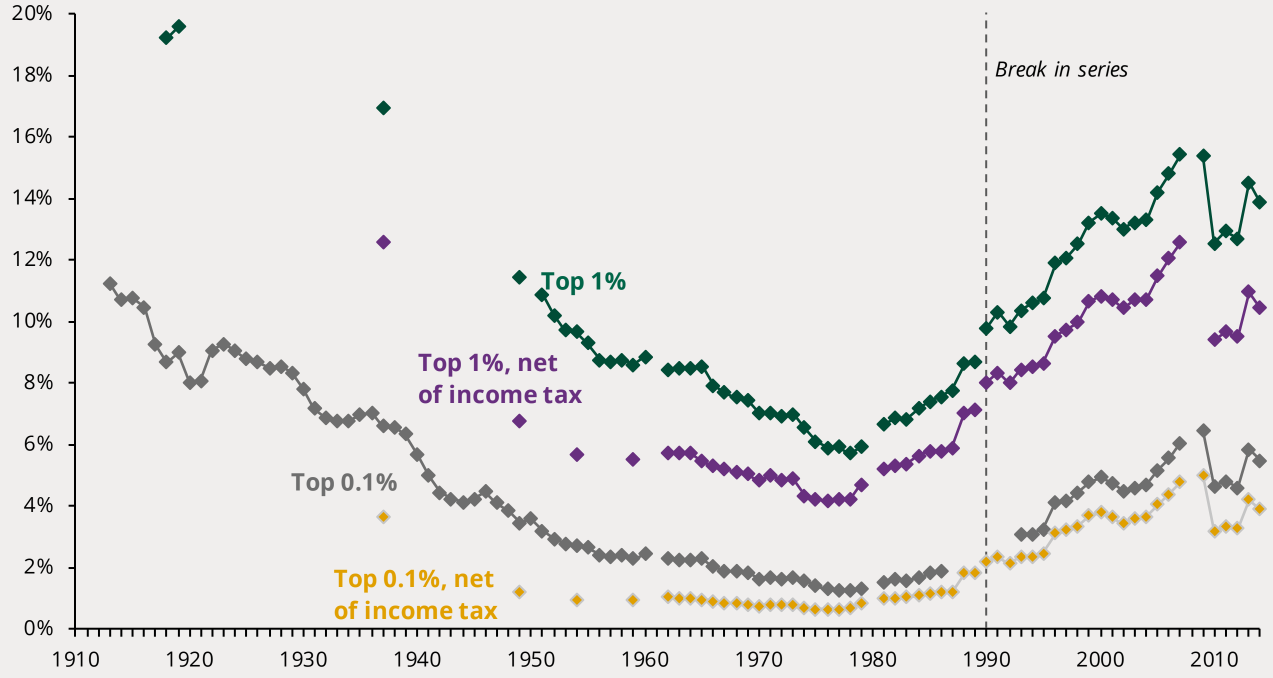
Top income shares over the century

Researchers at the World Wealth & Income Database have constructed a longer time series using tax returns. The chart below shows the share of income going to the top 1% and 0.1% of taxpayers from the start of the twentieth century, up to 2014. Unlike the data above, figures cover taxpayers only rather than all individuals and only count income reported for tax purposes.

[21] Institute for Fiscal Studies, Living Standards, Poverty and Inequality in the UK: 2013, 14 June 2013, p40. See also Institute for Fiscal Studies, Racing away? Income inequality and the evolution of high incomes, 17 January 2008

% share of income going to top 1% and 0.1% of taxpayers

UK, 1913-2014: data are for tax units (married couples and single adults) up to 1989 and for all adults from 1990



Note: Up to 1920, estimates include what is now the Republic of Ireland. Until 1974, estimates relate to income net of certain deductions; from 1975, estimates relate to total income.

Source: Facundo Alvaredo, Anthony B. Atkinson, Lucas Chancel, Thomas Piketty, Emmanuel Saez, and Gabriel Zucman, The World Wealth and Income Database, http://www.wid.world, accessed 18/9/2017.

Estimates up to 1989 are based on the top 1% and 0.1% of 'tax units' (the group of married couples or single adults with the highest incomes) while those from 1990 are based on the top 1% of all adults with the highest incomes. This reflects a change in the taxation system in 1990, which moved from treating couples as a tax unit to an individual base and may explain part of the reported increase in the share of income going to the highest income individuals during the 1980s and 1990s.

As noted above, some of the dip in income shares of the top 1% and 0.1% in 2010 and the increase in 2013 is likely to reflect individuals shifting income between years in order to benefit from changes in the top rate of income tax.

2.4 IFS Deaton Review of inequality

In May 2019, the Institute for Fiscal Studies (IFS) launched a new in-depth research project on inequalities in the UK. Chaired by the Nobel Laureate economist Sir Angus Deaton, the review aims to address a multitude of questions over its five-year lifespan. The IFS explain what the review is seeking to do:

> "Crucially, we will examine the role of policies, from taxes and benefits through to trade policy, education policies, the labour market, regional development, competition policy and regulation. This will give the UK government, and those in other developed countries, a far clearer and more holistic view of the effectiveness of available policy options, how they can best work alongside each other and the trade-offs between them."[22]

The Deaton review has since published reports including Unequal Britain, exploring attitudes towards inequalities among the UK public, and COVID-19 and inequalities, which focuses on the impact of the pandemic. It recently published Living standards since the last election.

[22] IFS, About The IFS Deaton Review (accessed 17 April 2024)

3 Redistribution

We can examine the extent to which the tax and benefit system reduces inequality by looking at inequality in different types of income. The data in the previous section are based on households' equivalised disposable income; income after direct taxes and benefits, adjusted for family size and composition. Disposable income is distributed more equally than original incomes (before taxes and before benefits) and gross incomes (before taxes but after benefits).

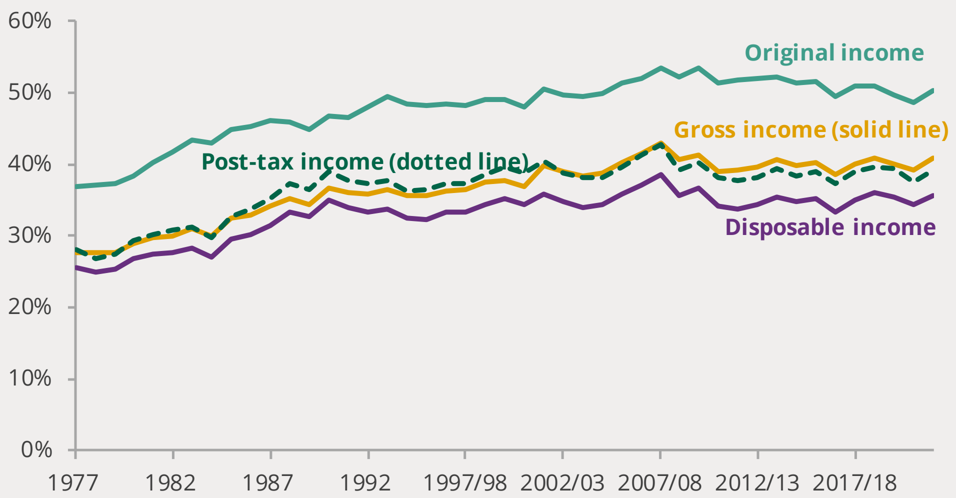
In 2021/22 the Gini coefficient was:

- 50.2% for equivalised original income,
- 40.9% for equivalised gross income (including benefits),
- 35.7% for equivalised disposable income (after direct taxes).
- 39.2% for equivalised post-tax income (after all taxes).

As noted above, disposable income is net of direct taxes which are mostly related to income. However, households also pay indirect taxes, for example Value Added Tax (VAT) and duties on alcohol and fuel, based on their expenditure. Poorer households tend to spend a higher proportion of their income in indirect taxes than richer households. Consequently, there is more inequality in 'post-tax incomes' (net of both direct and indirect taxes) than in disposable incomes.

The tax and benefit system acts to reduct income inequality

Gini coefficients for different stages of household income: UK, 1977 to 2021/22



Note: Income figures are equivalised and measured before deducting housing costs.

Source: Post tax income: ONS, Effects of taxes and benefits on household income, 18 July 2023
All other data: ONS, The effects of taxes and benefits on household income, disposable income estimate, 25 January 2023

4 The impact of the rising cost of living on income inequality

The cost of living has been increasing in the UK since early 2021. Consumer Price Index inflation peaked at 11.1% in October 2022, a 41 year high, before starting to fall.

The Library briefing Rising cost of living in the UK covers the latest inflation statistics, the impact on households and Government support.

4.1 Real post-tax household income is falling across the income distribution

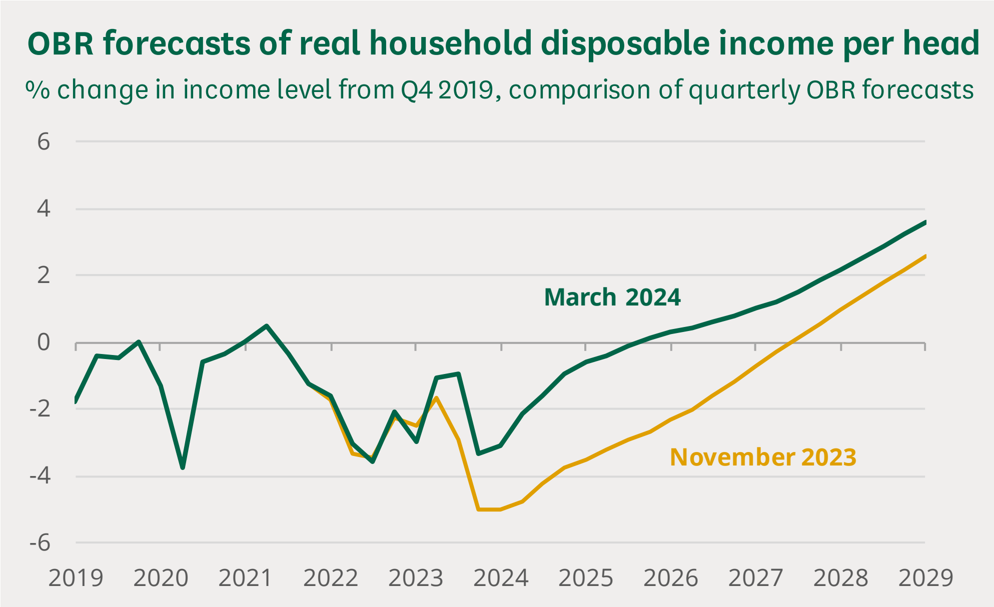
High inflation meant real (adjusted for CPI inflation) median household incomes fell across the income distribution outside the top 20%. Median income fell by 0.5%. After housing costs, median income fell by 1.5%. The Institute for Fiscal Studies reported that this was due to rents and mortgage interest rates rising sharply and says much of this effect has not yet been felt.[23] Median income for households with the lowest 10% of incomes fell by 3.5% between 2021/22 and 2022/23.[24]

In March 2024 the Office for Budget Responsibility forecasted that real household disposable incomes per head will increase by 0.1% in 2024 and then by 1.7% in 2025. Based on these forecasts, real (inflation-adjusted) post-tax income per person will return to its pre-pandemic level (Q4 2019) in Q4 2025.[25] The OBR is an independent fiscal watchdog that analyses public finances and fiscal policy.

23 Institute for Fiscal Studies, Living standards since the last election, 21 March 2024

24 DWP, Household Below Average Income 2022/23, 21 March 2024, Table 2.1ts

25 Library calculations based on OBR detailed economy table 1.5 and paras 2.39-2.40 of the OBR EFO



Source: OBR, Economic and fiscal outlook – March 2024, 6 March 2024

4.2 Income inequality may increase in 2024/25

Cost of living payments for lower income households and benefits being uprated by CPI inflation stopped the incomes of the poorest third of households falling very much in 2022/23.[26]

According to the Resolution Foundation, in 2023/24 real incomes will be relatively stable across the income distribution, but in 2024/25, there will be a 1% fall for households with the bottom half of incomes (not including pensioners) and a 1% rise for the top half. [27] The Resolution Foundation predicts that the Gini coefficient will rise sharply in 2024/25.

In January 2023, the Resolution Foundation predicted the Gini coefficient to reach a record high of 40.8% in 2027/28, because the top of the income distribution will see their incomes from investment and savings increase because of rising interest rates.[28]

26 Institute for Fiscal Studies, Living standards since the last election, 21 March 2024
27 Resolution Foundation, The Living Standards Outlook – Summer 2023 update, 6 September 2024
28 Resolution Foundation, The living standards outlook 2023, 9 January 2023

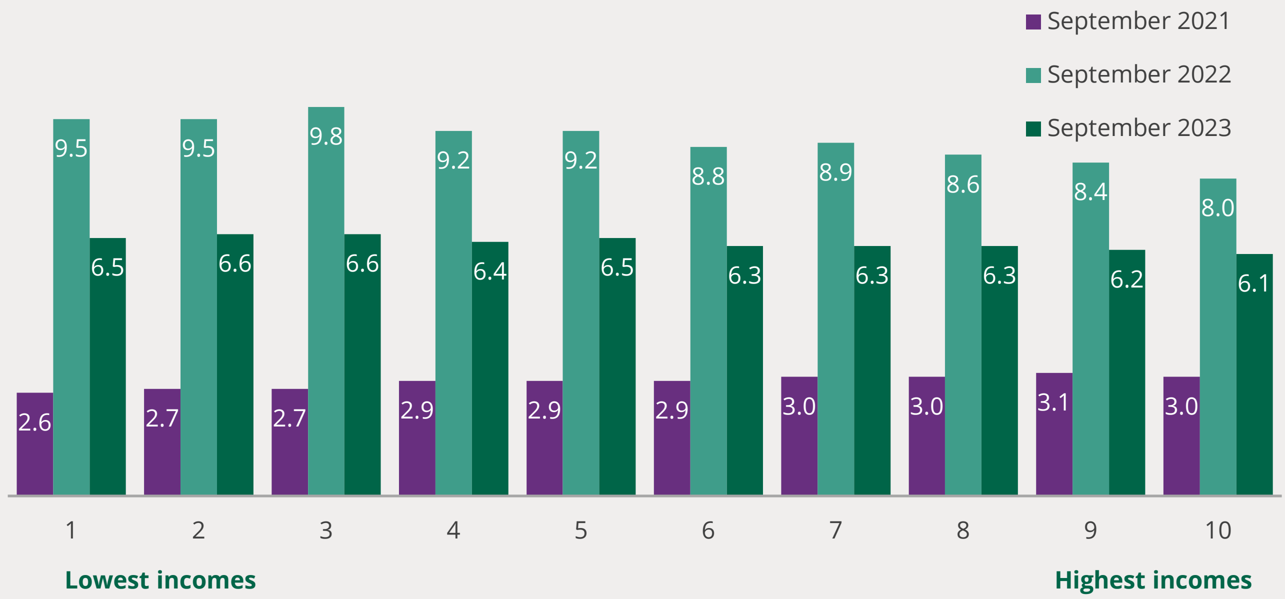
4.3 Low-income households are particularly affected by rising prices

The budgets of low-income households are most affected by the rising cost of living.

ONS data shows that households with the lowest incomes experience a higher than average inflation rate, while the highest-income households experienced lower than average inflation.[29] This disparity is due to the fact that low income households are more affected by high food and energy prices, which are driving inflation.[30] Low-income households spend a larger proportion than average on energy and food and will therefore be relatively more affected by increases in their prices.[31]

Inflation is highest for households with the bottom 30% of incomes

CPI by household income decile, %



Source: ONS, Provisional CPIH and CPI-consistent inflation rate estimates for UK household groups: January to September 2023, 15 November 2023

The Library briefing Rising cost of living in the UK provides more information on the effect of high prices on low income households.

[29] ONS, Provisional CPIH and CPI-consistent inflation rate estimates for UK household groups: January to September 2023, 15 November 2023

[30] ONS, Inflation and cost of living for household groups, UK: October 2022, 16 November 2022, Figure 1

[31] ONS, Living Costs and Food Survey, 16 March 2021

3 The impact of the coronavirus pandemic on income inequality

During coronavirus lockdowns, the wages of low-income workers were disproportionately affected by the economic fallout. However, the benefits system means that the incomes of low-income households were not more affected than other households.[32] The Gini coefficient was 38.1% in 2020/21, down from 39.1% in 2019/20.[33]

This partly reflects the temporary increase in benefits until October 2021, and the Coronavirus Job Retention Scheme and Self Employment Income Support Scheme. It also reflects the fact that the benefits system replaces a relatively large share of lost earnings for the lowest earners.[34]

The Institute for Fiscal Studies found that households in the poorest fifth before the coronavirus experienced a fall in earnings of 15% (£160 a month), but that they saw very little change in income between January and May 2020.[35]

Spending, savings, and debt

The spending most affected by the pandemic lockdowns was 'social consumption'; things like eating out or live entertainment, which accounts for a larger proportion of high-income households' spending. [36]

The Resolution Foundation found that between February 2020 and June 2021, 32% of people with the lowest incomes saw a fall in savings and 12% saw a rise. 9% of people with the highest incomes saw a fall, and 47% saw a rise in savings.[37]

Lower-income families were also more likely to have seen significant increase in their debt levels. The Resolution Foundation found that 54% of adults in families from the lowest income fifth borrowed more in March-June 2020 to cover everyday costs like food and housing.[38]

The Library paper Coronavirus: impact on household savings and debt provides more information and statistics.

32 HM Treasury, Impact of COVID-19 on working household incomes: distributional analysis as of May 2020, July 2020.
M Brewer & I Valentinova, Did the UK policy response to Covid-19 protect household incomes?, Institute for Social and Economic Research, University of Essex, June 2020.

33 IFS, Living standards, poverty, and inequality in the UK: 2022, 14 July 2022

34 Note that furlough payments are counted as earnings in the IFS data, and not as benefits.

35 IFS, The effects of coronavirus on household finances and financial distress, 29 June 2020

36 Bank of England, Monetary Policy Report and Financial Stability Report - August 2020, 6 August 2020

37 Resolution Foundation, The Living Standards Audit 2021, 1 July 2021

38 Resolution Foundation, Return to spender, Findings on family incomes and spending from the Resolution Foundation's coronavirus survey 9 June 2020

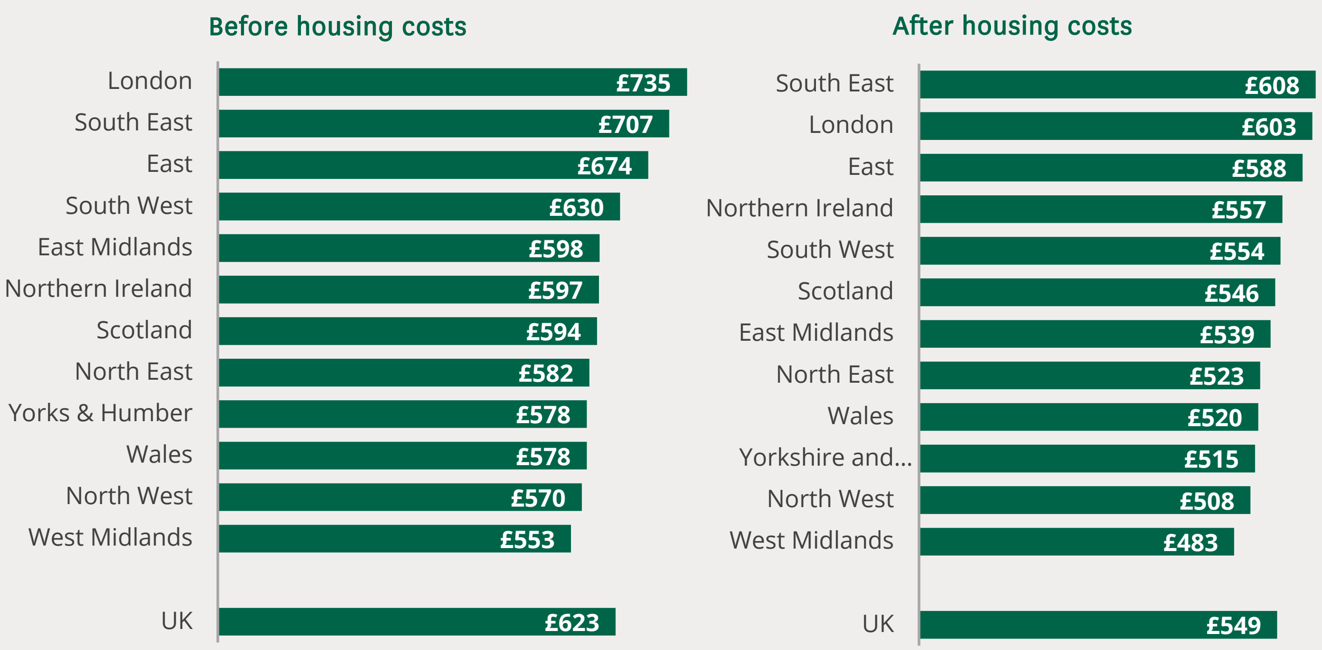
5 Income inequality between regions and countries in the UK

Median disposable incomes differ between UK regions and countries. In the three-year period 2020/21 to 2022/23, the West Midlands had the lowest median weekly household income before housing costs, at £553. London had the highest, at £735. The UK median disposable income for this period was £623.

After housing costs, the West Midlands still had the lowest median weekly income, at £483, while the South East had the highest, at £608. High housing costs in London means that after housing costs, incomes in London are lower than in the South East.

Median weekly income in UK countries and regions

2021/22 to 2022/23, in equivalised 2022/23 prices



Source: DWP, Households Below Average Income, 2022/23, Table 2.5ts

6 Income inequality between ethnic groups

There is significant income inequality between ethnic groups in the UK. In the Family Resources Survey, the ethnic group of a household is based on the ethnic group of the household reference person. This is usually the person in whose name the accommodation is owned or rented, or the person in the household with the highest income.[39]

6.1 Median incomes

The chart below shows in 2020/21 to 2022/23, people from Pakistani and Bangladeshi ethnic groups had the lowest median incomes, while people from White, Chinese, and Indian ethnic groups had the highest.

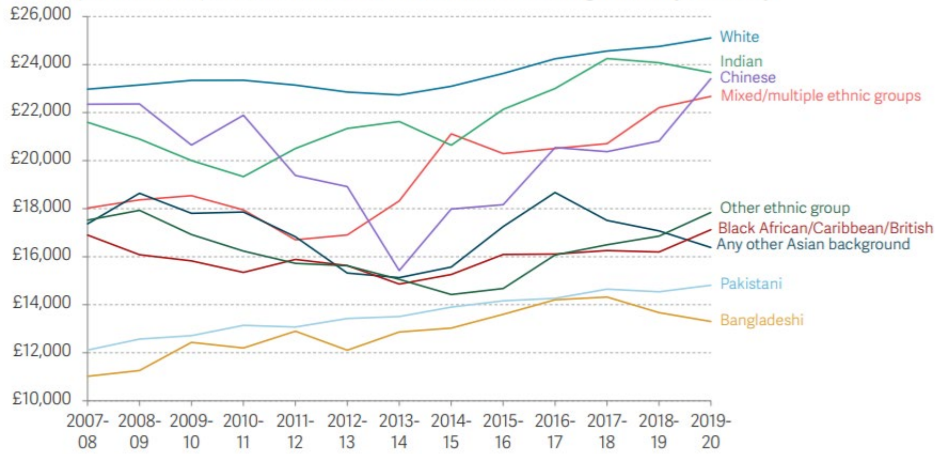
Source: DWP, Households Below Average Income, via Stat-Xplore

[39] The household reference person is the member of the household in whose name the accommodation is owned or rented, or is otherwise responsible for the accommodation. In households with joint householders the person with the highest income is taken as the household reference person.

The Resolution Foundation measured median incomes after housing costs by ethnic group in 2021 and found that income gaps are prevalent and persistent. As shown in the chart below, incomes for Pakistani and Bangladeshi households have increased in recent years, but incomes in these households are still more than 40% lower than incomes of White households.[40]

FIGURE 16: **Large income gaps between different ethnic groups have persisted over time**

Three-year average (year ending) of median real (CPI-adjusted to 2020-21 prices) equivalised disposable household income, after housing costs, by ethnicity



NOTES: GB before 2002-03.
SOURCE: RF analysis of DWP, Households Below Average Income.

Source: Resolution Foundation, The Living Standards Audit 2021, 1 July 2021

6.2 Income distribution

As well as a difference in median incomes, there is also a disparity between the proportion of people in different ethnic groups at the top and bottom of the income distribution.

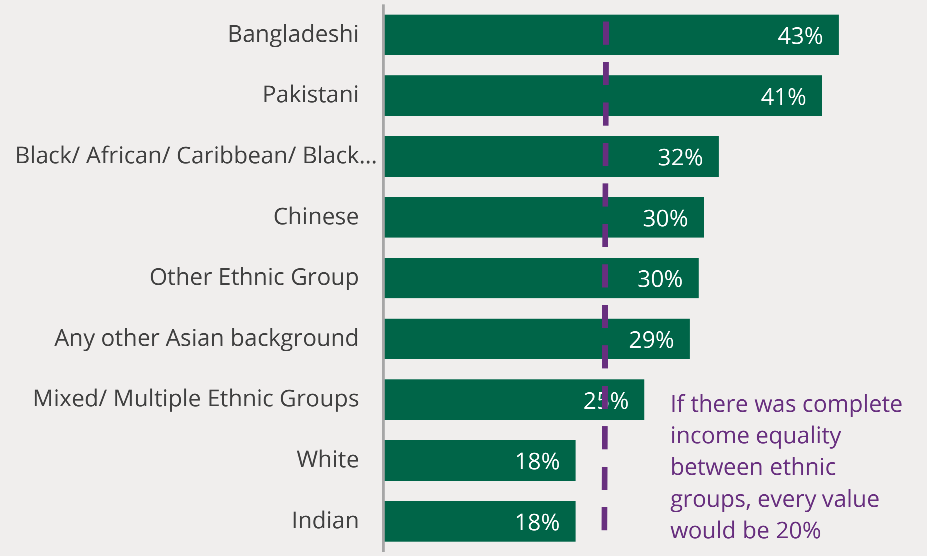
The charts below show the percentage of people in each ethnic group who were in the bottom fifth and the top fifth of all incomes in the years 2020/21 to 2022/23.

43% of people from a Bangladeshi ethnic group were in the bottom fifth of incomes, compared to 18% of people from an Indian or White ethnic group.

[40] Resolution Foundation, The Living Standards Audit 2021, 1 July 2021

Percentage of individuals in the bottom fifth of incomes

By ethnic group of the head of the households 2020/21 to 2022/23

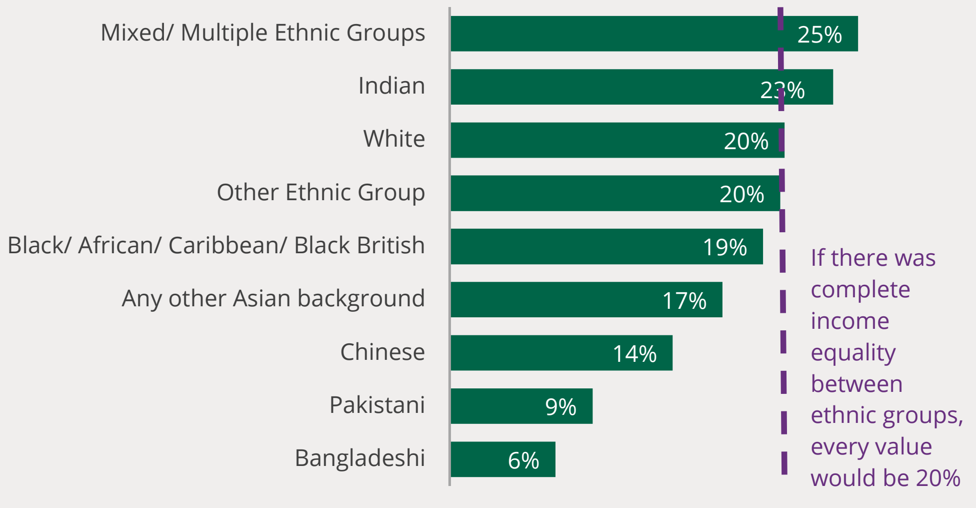


Source: DWP, Households Below Average Income, via Stat-Xplore

At the other end of the income distribution, only 6% of people from a Bangladeshi ethnic group were in the top fifth of incomes, compared to 25% of people from Mixed/multiple ethnic groups, 23% of people from an Indian ethnic group.

Percentage of individuals in the top fifth of incomes

By ethnic group of the head of the household, 2020/21 to 2022/23



Source: DWP, Households Below Average Income, via Stat-Xplore

7 Income inequality by disability status

Families where a member is disabled have significantly lower median incomes than families where nobody is disabled.

The chart below shows that in 2020/21 to 2022/23, households with a disabled family member had an income of £549 before housing costs, £134 less than households with no disabled members. After housing costs, households with a disabled family member had an income of £478, £125 less than households with no disabled members.

Median income by disability status

By disability status of the family, 2020/21 to 2022/23 (2022/23 prices)

Source: DWP, Households Below Average Income, via Stat-Xplore

8 International comparisons

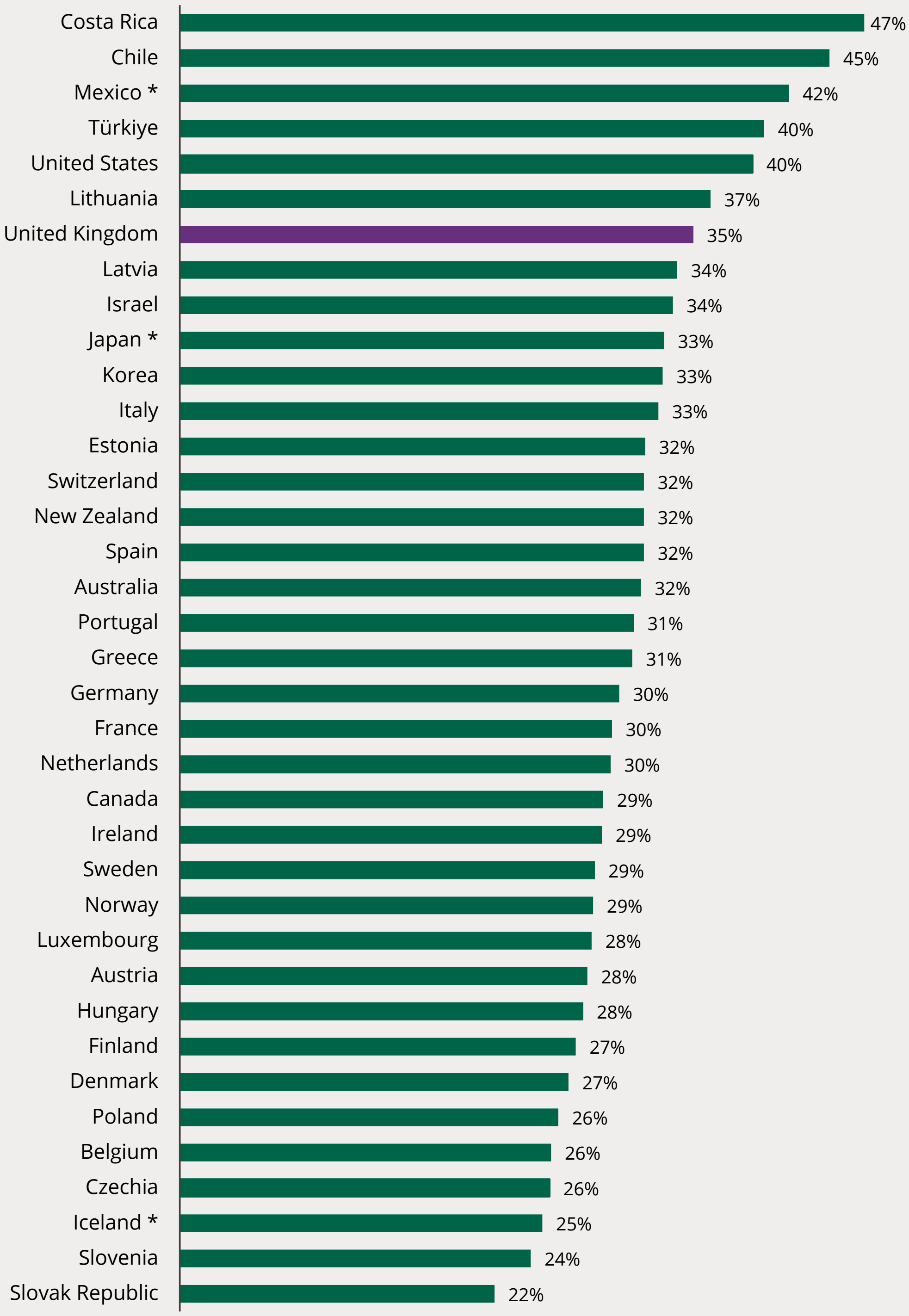
Comparable data on income inequality in different countries is published by OECD.

8.1 OECD data

OECD data indicates the UK had a higher level of income inequality than most European OECD members based on the Gini coefficient for disposable income, but a lower level than the US.

Gini coefficient for equivalised disposable income (OECD)

2021 or latest year



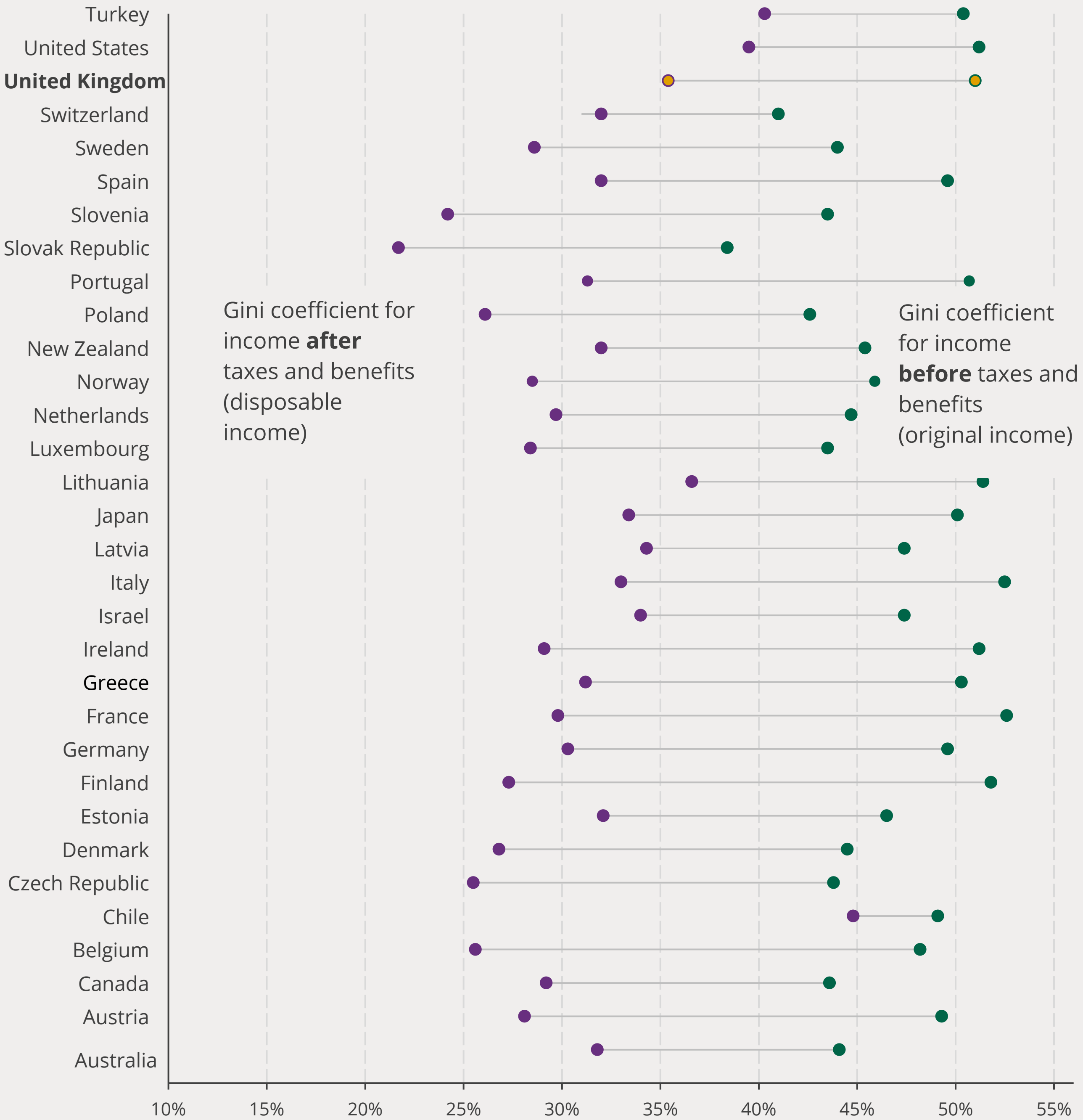
* Estimates for chile, Costa Rica and USA are for 2022, estimates for Germany, Australia, New Zealand, Switzerland, Israel, Turkey and Mexico are from 2020, the Denmark estimate is from 2019, the Japan estimate is from 2018 and the Iceland estimate is from 2017

Source: OECD stat, Income distribution database, accessed 12 April 2024

By comparing inequality in original incomes (before the effect of taxes and benefits) with inequality in disposable incomes (after taxes and benefits), we can get some indication of the extent to which different countries' tax and benefit systems redistribute income between households. The UK has a similar level of inequality in original income to Germany and France. However, in these countries there is less inequality in disposable incomes indicating a greater degree of redistribution.

The UK tax and benefit system redistributes income to a lesser extent than countries with similar inequality in original incomes

Gini coefficients for inequality in "original income" (before taxes and benefits) and "disposable income" (after taxes and benefits): higher values indicate greater inequality. 2021 or latest year



Source: OECD data, Income distribution and poverty, accessed 12 April 2024

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