THE BENEFITS OF TACKLING WORKLESSNESS AND LOW PAY

Paul Bivand and Dave Simmonds

This report explores the gains to government and to local economies of reducing worklessness and low pay, in terms of a reduced social security bill, increased economic activity and overall benefits to society.

The study is part of the Cities, Growth and Poverty research programme. It explores the extent to which local economies benefit from reducing worklessness as compared with the benefits to national government. This is a contribution to current debates on whether cities and localities could, if given the powers, effectively reduce poverty at local level.

- We estimate the benefit savings from people working at the Living Wage who are currently either out of work or working below the Living Wage.
- The report discusses a range of indirect impacts of reducing poverty on public service costs.
- We estimate the impacts of reducing worklessness and low pay on economic output for local economies and for the whole economy.
- The report identifies reasons why the impacts of reducing worklessness and low pay will differ between cities – a result of different patterns of wages, different patterns of part-time and full-time working and, particularly, different housing costs.
- We use the City of Leeds, and the wider Leeds City Region, as examples to show how savings differ from national estimates.
- We identify a range of activities that cities and localities could undertake to reduce worklessness and low pay.
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EXECUTIVE SUMMARY

This report examines the costs to government of worklessness and low pay, and explores what these costs look like at city level. Just as there are costs to government in supporting workless people and subsidising low pay, so there are benefits in reducing worklessness and improving pay. This report shows that the gains to government and to local economies are substantial, in terms of both a reduced social security bill and increased economic activity.

The report quantifies the impact of poverty reduction by reducing worklessness and increasing the number of people who are paid the Living Wage. In doing this we are updating and improving previous estimates of the costs of worklessness and identifying the benefits poverty reduction can bring to local economic growth.

We are using the Living Wage as a benchmark. It does not take everyone out of poverty – the extent to which it does so depends on the hours people work, their family circumstances and the availability of in-work benefits. We have been cautious in our estimates of the impact of the Living Wage. Other estimates may show greater impacts.

The costs of worklessness and low income have an impact on:

- public expenditure at local and national level;
- the wider economy at national and local level; and
- personal and household income.

Worklessness and poverty bring with them both ‘direct’ and ‘indirect’ costs. Direct costs are usually ‘cashable’, that is, there are immediate changes in public expenditure that can be easily measured. Indirect costs are more difficult to measure because this involves estimating the wider impact on society and the economy.

Most of the direct costs are paid by central rather than local government bodies, even if they are administered locally. Similarly, most of the direct
Cashable benefits to government of reducing poverty accrue to central rather than local bodies. Many of the indirect costs of (and benefits of reducing) poverty fall to local government — and the extent to which the potential benefits are realisable depends on how initiatives are designed and implemented.

As shown in Table 1, we estimate that for every £1 of public spending saved:

- 80p will accrue to central government to the Department for Work and Pensions (DWP) and HM Revenue & Customs (HMRC);
- 10p will accrue to the National Health Service (NHS) commissioners funded nationally;
- 7p will accrue to the local authority; and
- the remaining 3p will accrue to criminal justice services, fire services and social housing providers, many of which have local funding.

Table 1: The division of the impact on public finances between different public agencies

<table>
<thead>
<tr>
<th>Agency</th>
<th>Pence in £1 of public spending saved by agency</th>
</tr>
</thead>
<tbody>
<tr>
<td>Local authority</td>
<td>£0.07</td>
</tr>
<tr>
<td>NHS</td>
<td>£0.10</td>
</tr>
<tr>
<td>Police/criminal justice</td>
<td>£0.01</td>
</tr>
<tr>
<td>DWP</td>
<td>£0.78</td>
</tr>
<tr>
<td>HMRC</td>
<td>£0.03</td>
</tr>
<tr>
<td>Housing providers</td>
<td>£0.02</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>£1.00</strong></td>
</tr>
</tbody>
</table>

What has not been sufficiently recognised to date is the extent to which the nature and drivers of poverty vary at local level. The report shows there are differences at local level in the costs of worklessness and the impact on the local economy. Throughout this report we focus on Leeds to show how and why the costs and benefits vary. Improving our understanding of why costs vary at local level should lead to more effective ways for local policy-makers to reduce costs sustainably.

**Summary of impacts**

Tables 2, 3 and 4 summarise the results we have found. We show these in three blocks — the impact on government spending, the impact on the economy and the impact on individual incomes — because there are elements in each block that are the accounting equivalents of elements in other blocks. We are therefore trying to minimise double (or triple) counting of the same benefits. We have not added the three blocks together, and should not do so.

The impact on government spending is:

- Every time an out-of-work claimant moves into a job paid at the Living Wage, the government saves on average £6,897 annually; in Leeds it is slightly less at £6,800.
• When someone who is in employment moves up to the Living Wage, the government saves £265 annually; in Leeds it is £176.
• For all claimants (both in and out of work) the average saving is £3,658 annually; in Leeds it is £3,715.

These figures quickly add up to very large numbers once you take account of the number of people who are out of work. Figure 1 shows how the savings increase as more out-of-work claimants get work at the Living Wage.

**Figure 1: Annual gain to government from the out-of-work poor working at the Living Wage**

The increased economic output for the national and local economy of reducing poverty is:

• Every time an out-of-work claimant moves into work, there is an annual average increased economic output of £13,133 nationally; in Leeds this is £13,169.
• When someone who is in employment moves up to the Living Wage, there is annual increased economic output of £406; in Leeds this is £271.
• For all claimants (both in and out of work) the average annual boost to output is £7,065; in Leeds it is £7,363.

The gain to individuals’ disposable income is:

• Every time an out-of-work claimant moves into work, their average annual gain nationally is £6,514; in Leeds this is £6,604.
• When someone who is in employment moves up to the Living Wage, they gain £114 annually; in Leeds this is £74.
• For all claimants (both in and out of work) the average annual increase in net income is £3,462; in Leeds it is £3,665.
The low gains for people in employment below the Living Wage are because:

- Withdrawal rates for benefits and Tax Credits take 65–70p out of every additional £1 earned, even if people are below tax thresholds.
- Four out of five workers below the Living Wage work part-time, so the additional gross pay can be £500 or less a year (depending on hours).

Table 2: Annual per capita gains from out-of-work claimants moving into work at the Living Wage

<table>
<thead>
<tr>
<th>Subject</th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gain to government</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Benefit savings</td>
<td>£2,998</td>
<td>£2,494</td>
<td>£2,981</td>
</tr>
<tr>
<td>Administration savings(^1)</td>
<td>£646</td>
<td>£651</td>
<td>£648</td>
</tr>
<tr>
<td>Direct taxation</td>
<td>£1,959</td>
<td>£1,959</td>
<td>£1,959</td>
</tr>
<tr>
<td>Reduced health costs</td>
<td>£846</td>
<td>£766</td>
<td>£750</td>
</tr>
<tr>
<td>Reduced crime costs</td>
<td>£448</td>
<td>£410</td>
<td>£461</td>
</tr>
<tr>
<td>Total</td>
<td>£6,897</td>
<td>£6,280</td>
<td>£6,800</td>
</tr>
<tr>
<td>Gain to economy</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Direct increase in output</td>
<td>£13,133</td>
<td>£13,216</td>
<td>£13,169</td>
</tr>
<tr>
<td>Multiplier effects</td>
<td>£1,303</td>
<td>£1,427</td>
<td>£1,321</td>
</tr>
<tr>
<td>Total</td>
<td>£14,436</td>
<td>£14,643</td>
<td>£14,490</td>
</tr>
<tr>
<td>Gain to individual</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase in net incomes</td>
<td>£6,514</td>
<td>£7,137</td>
<td>£6,604</td>
</tr>
<tr>
<td>Total</td>
<td>£6,514</td>
<td>£7,137</td>
<td>£6,604</td>
</tr>
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</table>

Table 3: Annual per capita gains from in-work claimants receiving the Living Wage

<table>
<thead>
<tr>
<th>Subject</th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gain to government</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Benefit savings and direct taxation</td>
<td>£265</td>
<td>£244</td>
<td>£176</td>
</tr>
<tr>
<td>Administration savings</td>
<td>£0</td>
<td>£0</td>
<td>£0</td>
</tr>
<tr>
<td>Total</td>
<td>£265</td>
<td>£244</td>
<td>£176</td>
</tr>
<tr>
<td>Gain to economy</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Direct increase in output</td>
<td>£406</td>
<td>£373</td>
<td>£271</td>
</tr>
<tr>
<td>Multiplier effects</td>
<td>£23</td>
<td>£21</td>
<td>£15</td>
</tr>
<tr>
<td>Total</td>
<td>£428</td>
<td>£394</td>
<td>£286</td>
</tr>
<tr>
<td>Gain to individual</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase in net incomes</td>
<td>£114</td>
<td>£105</td>
<td>£74</td>
</tr>
<tr>
<td>Total</td>
<td>£114</td>
<td>£105</td>
<td>£74</td>
</tr>
</tbody>
</table>
Table 4: Annual per capita gains from claimants (both in and out of work) receiving the Living Wage

<table>
<thead>
<tr>
<th>Subject</th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Gain to government</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Benefit savings</td>
<td>£1,695</td>
<td>£1,404</td>
<td>£1,719</td>
</tr>
<tr>
<td>Administration savings</td>
<td>£261</td>
<td>£237</td>
<td>£253</td>
</tr>
<tr>
<td>Direct taxation</td>
<td>£1,025</td>
<td>£1,010</td>
<td>£1,077</td>
</tr>
<tr>
<td>Reduced health costs</td>
<td>£443</td>
<td>£395</td>
<td>£412</td>
</tr>
<tr>
<td>Reduced crime costs</td>
<td>£234</td>
<td>£211</td>
<td>£254</td>
</tr>
<tr>
<td>Total</td>
<td>£3,658</td>
<td>£3,257</td>
<td>£3,715</td>
</tr>
<tr>
<td>Gain to economy</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Direct increase in output</td>
<td>£7,065</td>
<td>£6,994</td>
<td>£7,363</td>
</tr>
<tr>
<td>Multiplier effects</td>
<td>£692</td>
<td>£746</td>
<td>£733</td>
</tr>
<tr>
<td>Total</td>
<td>£7,757</td>
<td>£7,740</td>
<td>£8,096</td>
</tr>
<tr>
<td>Gain to individual</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Increase in net incomes</td>
<td>£3,462</td>
<td>£3,730</td>
<td>£3,665</td>
</tr>
<tr>
<td>Total</td>
<td>£3,462</td>
<td>£3,730</td>
<td>£3,665</td>
</tr>
</tbody>
</table>

We have included in the tables the benefits of reduced health service use and of reduced crime. We have not included a range of the wider costs of poverty where the evidence for the financial benefits of reducing poverty is less well developed. These include:

- impacts on housing services;
- impacts on education services;
- impacts on personal social services; and
- impacts on local environmental services.

We expect that there will be benefits from reducing poverty in these areas but have not been able to put robust numbers on the benefit. The areas include many services that are delivered by local authorities, so these additional benefits could add to the local authority benefit from reducing poverty.

Local policy-making

Investing in tackling the causes of poverty needs to be seen as an integral part of investing to boost local economic growth. What does this mean for cities attempting to reduce poverty? The main steps should be to:

- Develop a sound evidence base – identify the key influences that move people in and out of poverty.
- Proof local policies for their impact on poverty levels – identify the costs and benefits of reducing poverty to inform the strategic decisions cities need to take.
- Adopt a cost–benefit approach – this helps to identify the elements that are needed in a city strategy to increase growth and reduce poverty, especially in the context of reduced local government spending.
- Review the policy choices – there are a number of approaches to poverty reduction that can be adopted within local economic strategies, and they can be justified in terms of the wider economic and fiscal benefits.
When reviewing local policies we have found that the main reasons for local variations in costs and benefits are:

- the nature of the local economy – the types of jobs and industries;
- wage levels – especially for entry-level jobs;
- the different patterns of worklessness – especially the number of people on health-related benefits;
- the balance between in- and out-of-work benefit recipients – areas with high levels of in-work poverty will gain the most from increasing pay levels; and
- housing costs and tenure – the level of rents varies considerably between areas and between different types of housing.

Examples of policy objectives that could be pursued at local level are:

- Increase the proportion of higher paid jobs by attracting those sectors and occupations that pay more.
- Improve pay rates in low-paid jobs by actively encouraging employers to adopt the Living Wage.
- Improve opportunities for people to increase their working hours by improving affordable childcare and other social care.
- Provide sufficient part-time jobs for those people who want or need to work part-time.
- Support high-performing employment and training programmes that increase the employability of the local workforce.
- Provide an education and skills training system that can deliver the qualifications for local people that are needed by current and future employers.
- Promote in-work progression – encourage employers to train workers and encourage individuals to invest in their skills.
- Adopt a housing strategy that ensures there is a sufficient supply of affordable housing.
- Develop focused actions for people in entrenched poverty.
- Establish a local support services framework for the welfare system that helps people escape poverty and insecure employment.

Greater Manchester’s New Economy economic think-tank has developed a cost–benefit analysis (CBA) tool (New Economy, 2013), which has been adopted by central government and published as supplementary guidance to HM Treasury’s Green Book (HM Treasury, 2014a). The advantage of a CBA tool is that it brings together the range of assumptions that local policy-makers have to make in planning a new intervention, and includes the best available evidence on financial impacts.

At present there is little incentive to cities to invest in measures to reduce worklessness and poverty because the vast majority of savings accrue to central government.

There is no clear incentive for local partners to tackle poverty as part of local growth strategies or to make the most efficient and effective choices given local circumstances. Successful and innovative city poverty reduction strategies could be rewarded by local areas retaining some of the benefits savings, thereby incentivising local partners to invest more resources, time and energy in promoting balanced and inclusive economic growth.
1 INTRODUCTION

This report is part of a series of projects supported by the Joseph Rowntree Foundation (JRF) programme, Cities, Growth and Poverty. The purpose of the programme is to encourage cities and city regions to see poverty reduction as a key part of their local growth proposals.

This report primarily looks at the costs of poverty on a city scale, and examines the benefits to city economic growth of tackling poverty. The report is a means to better understand the vital connections between reducing poverty, growing the local economy and encouraging more inclusive growth. The analysis in this report provides new estimates for how much we spend on people in poverty and the additional economic growth that could be generated with active policies to reduce poverty.

Throughout this report we use the example of Leeds and the wider Leeds City Region to demonstrate the costs of poverty to cities and the potential economic and social gains in reducing poverty. JRF is working closely with Leeds City Council and Leeds City Region through the Cities, Growth and Poverty programme.

All major political parties regard work as the best way out of poverty, with paid work being seen as a better way to reduce poverty than simply transferring income and wealth from richer to poorer sections of society. Income transfers have a role, but ‘making work pay’ is common to all political parties. Proposals for devolving some of the functions relating to economic growth to Local Enterprise Partnerships (LEPs) and city regions (through City Deals) have been implemented by the Coalition Government and there are proposals from all the major political parties to go further.

In this report, we have concentrated on the benefits of decreasing poverty by reducing worklessness, increasing the number of people in work and increasing the Minimum Wage. The report identifies the impact of worklessness and low income on:

- public expenditure at the local and national level;
- individuals’ personal and household income; and
- the wider economy, at the national and local level.
While more people in work will increase economic output, and hence economic growth, this does not automatically mean that fewer people will be in poverty. As the increasing number of people who are both in employment and in poverty shows, simply getting people into work will not always reduce poverty. There are now more people suffering in-work poverty than out-of-work poverty.

This can happen for two main reasons. First, the Minimum Wage is too low to prevent those who earn it from being in poverty. Second, government takes a large share of any earned income through benefit tapers, taxes and National Insurance (NI). In this report we examine only the impact of increasing the Minimum Wage to the Living Wage, but we recognise that the introduction of Universal Credit will make it easier and simpler for governments to adjust how much they recoup from the pay of people on low incomes.

In reducing the costs of poverty, social security benefits are the largest and most certain element that can be quantified. While there is a national benefits system with standard rates, there are still differences at local level in the average cost per claimant. The reasons for this include different balances between unemployed Jobseeker’s Allowance and Employment and Support Allowance claimants and, more significantly, housing costs reflected in Housing Benefit payments.

There are also other public services, such as health services, where there is some evidence that levels of poverty affect the level of spending. This serves to reinforce the variation in costs between different local areas. However, exactly how cities are able to address the causes of poverty is not straightforward. This report shows how cost–benefit analysis (CBA) can be used to assess the impact of local investment in new interventions. CBA ensures the hard questions are asked but it also gives some hard (quantified) answers in terms of the financial, economic and individual cost benefits.
In this chapter we consider the direct and indirect costs of worklessness and poverty at national and local level. Social security spending is the largest and most easily identifiable direct cost to public services of poverty and represents largely ‘cashable’ savings. This is because benefit payments are demand driven – they stop and start according to people’s circumstances and their entitlements. Detailed data on benefits can be used to calculate costs, but with each dataset there are issues of measurement that need to be taken into account.

Later in this chapter we consider the indirect costs, which can cover a wide range of public services where local demand for those services may increase or decrease because of levels of poverty. An example is the demand for health services, where there is a well-established link between health problems and worklessness. However, cost savings in health services are not usually automatically cashable in the same way as for benefits payments – a number of related factors influence the speed and extent to which spending can adjust.

Welfare reform is leading to reduced household incomes (Inclusion, 2013) for claimants and additional costs for local government. The purpose of this study has not been to track and quantify all the short- or long-term impacts of welfare reform. However, these costs are real and a wider study is needed to identify this additional spending. The additional costs are within the context of what will be an estimated 30% reduction in local government spending between 2008 and 2015 (Hastings, et al., 2013). Coping with this
Reduction is one important reason why a better understanding of the costs and benefits of poverty reduction is important.

**Benefit savings from reducing poverty**

While there is detailed data on benefit spending, we have had to simplify some of the complexities of the benefit system to estimate the average out-of-work benefit spending, and in-work spending. Our approach to measurement is summarised in Appendix 1. We have tried to use the latest figures available – so DWP benefit figures are November 2013 while HMRC are for 2012–13. These are represented as 2013.

Figure 2 shows national social security spending by beneficiary (the cost of Housing Benefit has been included in the total for each group). More than half (55%) of all national social security spending is for pensioners and therefore not included in the analysis in this report. Out-of-work benefits account for 23% of the national social security bill, while in-work benefits amount to a smaller 14%. Compared with the national picture, spending in Leeds is lower for pensioners (51%), higher for those out of work (27%) and slightly higher for those in work (15%).

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**Figure 2: National social security spending by beneficiary group, 2013**

- **Pensioner**: £98 billion (55%)
- **Working age, out of work**: £41 billion (23%)
- **Working age, in work**: £25 billion (14%)
- **Disabled (DLA)**: £14 billion (8%)

Sources: Department for Work and Pensions (DWP) Tabulation Tool, DWP Stat-Xplore, HM Revenue & Customs (HMRC) Tax Credit statistics

Note: DLA: Disability Living Allowance.

**Spending on working-age benefits**

Working-age benefits come from a range of sources:

- out-of-work benefits (Department for Work and Pensions, DWP);
- in-work benefits (HM Revenue & Customs, HMRC);
- local authority administered benefits; and
- Council Tax reduction.

The detail associated with these is essential to the measurement of the costs and benefits, and there is a description of the issues in Appendix 1.
Figures 3 and 4 show the breakdown of benefit spending nationally and in Leeds respectively for 2013. Nearly half the working-age out-of-work spending is for Housing Benefit and Child Tax Credits.

**Figure 3: National out-of-work social security spending by benefit, 2013**

Sources: DWP Tabulation Tool, DWP Stat-Xplore, HMRC Tax Credit statistics, November 2013

**Figure 4: Leeds benefit spending for out-of-work claimants, 2013**

Sources: DWP Tabulation Tool, DWP Stat-Xplore, HMRC Tax Credit statistics, November 2013
The social security cost for out-of-work claimants in Leeds, on its own, exceeds £550 million a year. Leeds spends proportionately more on Jobseeker’s Allowance claimants than the national average. This difference is one of the reasons why there are local variations in the costs and benefits of poverty reduction – see Chapter 5 for further explanation of these variations.

Some people who claim out-of-work benefits may also do some paid work. This is notably the case for Employment and Support Allowance claimants where the ‘permitted work’ rules encourage some work. Universal Credit will change the definition of ‘in work’ and ‘out of work’ so that people on benefits who work less than 16 hours a week will be counted as in work, but may be required to look for further work in the future.

Figure 5 shows the 2013 pattern for in-work benefits in Leeds where the total spending is over £300 million a year. Leeds has 14% of in-work benefit spending on Housing Benefit, which is lower than the national average of 19%. This is largely because Leeds rent levels are lower than those in London and the South East, so Leeds workers have less need of Housing Benefit support.

Figure 5: Leeds spending for claimants who are in work, 2013

Taking both out-of-work and in-work benefits together, it is possible to estimate the total benefit spending for working-age claimants. Table 5 summarises the spending at national level, and in Leeds City Region2 and the City of Leeds.
Table 5: Benefit spending for working-age claimants, 2013

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£25,005,100,000</td>
<td>£1,313,400,000</td>
<td>£303,800,000</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£40,858,200,000</td>
<td>£1,857,800,000</td>
<td>£557,900,000</td>
</tr>
<tr>
<td>Total</td>
<td>£65,863,300,000</td>
<td>£3,171,200,000</td>
<td>£861,700,000</td>
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<tr>
<td>Benefit spending</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>per claimant</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In-work poor</td>
<td>£6,131</td>
<td>£5,882</td>
<td>£5,922</td>
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<tr>
<td>Out-of-work poor</td>
<td>£9,129</td>
<td>£7,819</td>
<td>£8,902</td>
</tr>
<tr>
<td>Average (weighted)</td>
<td>£7,700</td>
<td>£6,880</td>
<td>£7,561</td>
</tr>
</tbody>
</table>

Table 5 also illustrates the difference in pattern of spending between the national average spend per working-age claimant and Leeds City Region and the City of Leeds.

These figures are based on 59,000 out-of-work benefit claimants in Leeds. We estimate that there are 49,000 workers in Leeds paid below the Living Wage, 80% of whom work part-time.

However, some 13% of total in-work Tax Credit spending is for families with incomes over the Living Wage (one adult working full-time, one part-time). These payments are likely to represent reimbursement of payments for childcare through the Childcare Tax Credit and/or high rents through Housing Benefit. There could be a case for disregarding them when assessing poverty levels, but we have still included them in all figures to reflect true spending on benefits.

The potential impact of the Living Wage

Table 6 shows the possible savings to government every time an employee’s wages are increased to the Living Wage or an unemployed person moves into a Living Wage job.

For those already in work this gives average per capita in-work claimant savings in the range of £176 for the City of Leeds to £265 for the country. This is relatively low because people will continue to receive some in-work benefits when paid the Living Wage. The large difference in savings between Leeds and national figures is because there is a lower proportion of full-time workers in Leeds below the Living Wage compared with the national average.

Table 6: Benefit savings from paying at the Living Wage, based on 2013 figures

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£1,081,200,000</td>
<td>£54,400,000</td>
<td>£9,100,000</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£13,418,400,000</td>
<td>£592,600,000</td>
<td>£186,800,000</td>
</tr>
<tr>
<td>Total</td>
<td>£14,499,500,000</td>
<td>£647,100,000</td>
<td>£195,900,000</td>
</tr>
<tr>
<td>Benefit saving</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>per claimant</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In-work poor</td>
<td>£265</td>
<td>£244</td>
<td>£176</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£2,998</td>
<td>£2,494</td>
<td>£2,981</td>
</tr>
<tr>
<td>Average (weighted)</td>
<td>£1,695</td>
<td>£1,404</td>
<td>£1,719</td>
</tr>
</tbody>
</table>
For unemployed people there are benefit savings in the range of £2,500 to £2,900 per out-of-work claimant every time an unemployed person moves into a full-time Living Wage job. See Chapter 5 for explanations of why the average savings vary from place to place. In addition, government receives tax and NI income, and has lower administration costs. These are estimated below.

These savings quickly add up to substantial spending reductions for government. Figure 6 shows the relationship between the number of unemployed claimants moving into a Living Wage job and the total savings by government. For example, if unemployment were reduced in Leeds by 20,000 (or 34%), the government would save an estimated £60 million. In the extreme example of all those claiming out-of-work benefits moving into a full-time Living Wage job, the Exchequer would save £13 billion; £177 million of this would come from the City of Leeds and £593 million from the region.

Table 6 also shows the amount that is being spent on supporting people in jobs that pay below the Living Wage. In the hypothetical example of all employers paying the Living Wage, nationally just over £1 billion would be saved and £9 million in the City of Leeds. These savings would all accrue to central government; while local campaigns for the Living Wage will benefit the local economy through increases in the spending power of local residents, it is the Exchequer that directly benefits. (For a detailed analysis of the potential impact of the Living Wage, see Lawton and Pennycook, 2013.)
Impact of paying the Living Wage on tax receipts

One of the direct costs of worklessness is the loss of potential tax and NI revenue from employees and employers. Table 7 shows that the Treasury gains an average of £1,959 in tax and NI for every unemployed person moving into a full-time Living Wage job. If they worked part-time at the Living Wage, the Treasury would get zero because the Living Wage at average part-time hours is below tax thresholds for income tax and NI.

Table 7: Annual tax and National Insurance gain

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>Not available</td>
<td>Not available</td>
<td>Not available</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£8,767,600,000</td>
<td>£465,500,000</td>
<td>£122,800,000</td>
</tr>
<tr>
<td>Total</td>
<td>£8,767,600,000</td>
<td>£465,500,000</td>
<td>£122,800,000</td>
</tr>
<tr>
<td>Per-claimant tax and NI gain</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In-work poor</td>
<td>Not available</td>
<td>Not available</td>
<td>Not available</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£1,959</td>
<td>£1,959</td>
<td>£1,959</td>
</tr>
<tr>
<td>Average (weighted)</td>
<td>£1,025</td>
<td>£1,010</td>
<td>£1,077</td>
</tr>
</tbody>
</table>

The larger the number of unemployed people who move into full-time employment, the greater the additional revenue. Figure 7 shows the relationship between the gain to the Treasury and the numbers moving into work. For these purposes we have assumed that people move into full- or part-time work in the same proportion as the Leeds workforce – 70% full-time and 30% part-time. This could be adjusted to reflect that part-time work is more prevalent at the low end of the labour market, which would have the effect of reducing the tax gain.

Figure 7: Tax and National Insurance gains to HM Treasury from the out-of-work poor working at the Living Wage

Repeating the examples from above, if 20,000 unemployed people in Leeds moved into a full-time Living Wage job, the Treasury would gain £39 million.
At the extreme end, if all the out-of-work benefit claimants in Leeds worked full-time at the Living Wage, the Treasury would gain an extra £123 million in direct taxes and NI.

There would also be increased tax receipts (such as VAT and fuel duty) from the possible additional spending of people who are in work at the Living Wage. However, we have not incorporated any estimates for this in our calculations in this report. If we had been able to estimate the increased spending on VAT-able items and fuel, and the resulting tax take, our estimates of the Treasury benefit from people being in work at the Living Wage would only rise.

The cost of benefit administration
The cost of administering social security is significant. In March 2013 DWP had over 90,000 staff, all but a small proportion of whom were involved in administering social security. DWP also paid local authorities to administer Housing Benefit and Council Tax Support. Table 8 below summarises the costs of administration.

In total the operational cost of supporting City of Leeds claimants is £648 per claimant, or £38 million a year. For Leeds City Region, it amounts to £148 million a year, including the cost of Housing Benefit administration. This total is composed of DWP costs, local authority benefit administration and HMRC costs, as described below.

DWP programme and operational costs
In 2012/13 DWP spent £2.63 billion on programmes for the unemployed and on ‘operational delivery’ for working-age claimants. In addition it spent £466 million on support for local authorities – largely Housing Benefit administration costs.

The DWP operational delivery spending includes administration for the Disability Living Allowance and the transition to Personal Independence Payments, and administration of the State Pension. However, the bulk of the cost covers the main working-age benefits, where claimants have a greater engagement with Jobcentre Plus. DWP annual accounts under the last government identified that 64% of administration costs were for people of working age, 4.6% for disabled, and the remainder for pensioners, central administration and children (largely child support). We have not been able to separate out the DWP operational cost between out-of-work and in-work claimants.

The average figure for DWP costs is £486 per annum for every claimant. In Leeds this represents £34.9 million of spending incurred by DWP for Leeds claimants.

Local authority benefit administration costs
The Audit Commission (2014) has calculated that local authorities spent £827 million in 2012/13 on benefit administration and received £466 million from DWP as a subsidy. This left a difference of £361 million for local authorities to find from elsewhere.

Leeds City Council receives just over £5 million annually from DWP for the administration of benefits. Our estimate for the share of the total for working-age claimants is £2.65 million, based on the proportion of working-age claimants to pensioner claimants. This will be an underestimate as changes in claimant circumstances (which incur administration cost) are more likely for working-age claimants. In addition we have estimated Leeds’ share of the additional £361 million spent on administration by councils.

Taken together, this gives £83 per annum spent on administration by Leeds City Council for every claimant.
In addition, Leeds City Council administers the claims for free school meals. The cost to schools of managing the delivery of free school meals is likely to be significantly greater than the cost of administering claims. The introduction of free school meals for all infant schoolchildren will reduce the administration cost for Leeds City Council and for schools.

**HMRC administration**

HMRC estimates its administration spending on Tax Credits as 1.55% of Tax Credit spending (HMRC, 2013) or about £80 per claimant. The difference between DWP and HMRC is because, unlike Jobcentres, HMRC has little face-to-face contact.

**Table 8: The costs of administering the social security system**

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>DWP operational cost</td>
<td>£2,630,056,590</td>
<td>£130,143,327</td>
<td>£34,878,526</td>
</tr>
<tr>
<td>Cost per claimant year</td>
<td>£486</td>
<td>£486</td>
<td>£486</td>
</tr>
<tr>
<td>Housing Benefit</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>operational cost for</td>
<td>£453,888,270</td>
<td>£14,615,478</td>
<td>£4,406,597</td>
</tr>
<tr>
<td>working-age claimants</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Cost per claimant year</td>
<td>£83</td>
<td>£83</td>
<td>£83</td>
</tr>
<tr>
<td>HMRC Tax Credits</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>operational cost</td>
<td>£314,639,144</td>
<td>£18,275,681</td>
<td>£4,060,831</td>
</tr>
<tr>
<td>Cost per claimant year</td>
<td>£77</td>
<td>£82</td>
<td>£79</td>
</tr>
<tr>
<td><strong>Total operational cost</strong></td>
<td>£2,944,695,734</td>
<td>£148,419,008</td>
<td>£38,939,357</td>
</tr>
<tr>
<td>Total cost per out-of-</td>
<td>£646</td>
<td>£651</td>
<td>£648</td>
</tr>
<tr>
<td>work claimant year</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total cost per claimant</td>
<td>£261</td>
<td>£237</td>
<td>£253</td>
</tr>
<tr>
<td>year (in work or out of</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>work)</td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

**Passported benefits**

We have not included in our estimates the additional costs of passported benefits, given the complexity of the range of such benefits and how they apply in different households. These are ‘in kind’ benefits for people who meet means-tested or benefit tests. They include free school meals (administered by local authorities), free prescriptions and other National Health Service (NHS) benefits, a range of utility schemes, Legal Aid, and, in some cases, fee remission for some further education courses.

The common feature of these schemes is that a claim for a DWP income-based benefit establishes eligibility. However, for some passported benefits there are additional income-based schemes that may be applicable to people in low-income work.

If people move into low-income work from being on benefits, they lose automatic DWP-certificated eligibility for each passported benefit. Claimants commonly believe that eligibility is defined by DWP, while the other income-based schemes are less well understood. For example, in the case of NHS prescriptions, there are ‘season tickets’ that enable low-income people with a regular need for prescriptions to receive a substantial discount.
A 2012 review of passported benefits by the Social Security Advisory Committee (DWP, 2012a) showed both the complexity and the ‘cash’ value that some families can receive from these benefits. This can be as much as 10% of the value of the primary benefit payments. As such, passported benefits are a direct cost. There are identifiable savings when people cease to be eligible, with a potentially large impact on the gains when moving into low-paid work. More detailed research will be needed on how these sums impact on the figures given in this report.

**Indirect impacts on public service costs**

One cost of poverty is the additional call it makes on public services. However, assessing the additional costs of public services is fraught with complexity. We have reviewed past research (see Appendices 2 and 3) that attempts to identify benefits and costs from people who move into work or out of work. DWP’s main review, produced by Daniel Fujiwara (2010), has been built on by DWP itself (DWP, 2011) and expanded with updated information in the project by Greater Manchester’s New Economy to develop a CBA tool (New Economy, 2013). Uses of this tool have been highlighted by the National Audit Office (NAO, 2013) and it is being used by Whole Place Community Budgets.

Some of these costs impact on the local authority, some on other local public services such as Health Service Trusts, the police and fire services, and some on nationally controlled services. These are all (to varying extents) partners in Whole Place Community Budgeting processes. The extent to which the costs of poverty are borne by the local authority depends on the local configuration of services — that is, the proportion of schools that are academies (or free schools), and whether the local authority is the residual service provider when academies or their equivalents in other fields do not provide service to the poorest.

**Measurable indirect impacts**

**Health services**

The benefit to reducing health service costs from people moving into work was calculated by Fujiwara (2010) at £508 per additional job year for programmes other than those for Employment and Support Allowance claimants (or others with health problems) and £1,016 for Employment and Support Allowance claimants. The savings are primarily the result of a reduction in GP consultation costs.

These estimates produce the following annual savings if all the benefit claimants are in work.

<table>
<thead>
<tr>
<th>Table 9: Health savings from reducing poverty</th>
</tr>
</thead>
<tbody>
<tr>
<td>National</td>
</tr>
<tr>
<td>----------</td>
</tr>
<tr>
<td>Jobseeker’s Allowance and Income Support claimants</td>
</tr>
<tr>
<td>Employment and Support Allowance claimants</td>
</tr>
<tr>
<td><strong>Total</strong></td>
</tr>
<tr>
<td>Savings per out-of-work claimant year</td>
</tr>
<tr>
<td>Savings per claimant (in work or out of work), annual</td>
</tr>
</tbody>
</table>
Police and criminal justice services
Fujiwara (2010) finds that the impact of people moving into work on the costs of crime to public services varies according to age and gender. The evidence is strongest for acquisitive crime such as theft and burglary, where a range of studies show a relationship between crime and the income level of the individual. The New Economy CBA tool (see Chapter 6) divides the fiscal benefit of reduced crime between police, other criminal justice organisations, housing and local authorities. This division can be important in demonstrating the gains to partners in engaging in poverty reduction activities.

Table 10: Savings from reduced crime

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Savings from reduced crime</td>
<td>£1,793,000,000</td>
<td>£95,100,000</td>
<td>£25,700,000</td>
</tr>
<tr>
<td>Savings per out-of-work claimant year</td>
<td>£401</td>
<td>£400</td>
<td>£410</td>
</tr>
<tr>
<td>Savings per claimant (in work or out of work), annual</td>
<td>£210</td>
<td>£206</td>
<td>£225</td>
</tr>
</tbody>
</table>

Other uncosted impacts
There are other costs that can be attributed to levels of poverty, which we have not included in this analysis. A JRF commissioned report, Coping with the cuts (Hastings, et al., 2013), categorised the sorts of services that are more likely to be used by poor communities. These are:

- very pro-poor – Housing Benefit (administration); homelessness; other housing general fund spend; children’s social care; Citizens Advice; and police; and
- pro-poor – crime and community safety; social care for older people and other adult groups, including home care; fire and rescue; primary and special education; other education; public transport (bus); and school transport.

In general, it is intuitive to acknowledge that there are links between the demand for these services and the level of poverty. However, quantifying the costs that are linked to poverty is more difficult because of the range of different influences on demand. Nonetheless it is important to recognise the strain poverty places on local services whether they are funded through local government or not.

There is an emerging evidence base to quantify the impact of poverty reduction in some services, examples of which are outlined below.

Impacts on housing services
Social housing has increasingly been aimed at people in poverty. Public services concerning housing, both local authority homelessness services and those of social housing providers, are highly associated with people being in poverty. However, whether the costs of social housing and homelessness will change with poverty reduction is more complex.

Impacts on education services
Bramley and Watkins (2008) present evidence that poverty affects education outcomes (and therefore lifelong incomes). The relationship between deprivation and the cost of education has been recognised in education funding formulae, both previously through local authority
Impacts on national and local government spending

education funding and currently through the Pupil Premium paid to schools. New Economy (2014) raises the possibility that increased school readiness (at age 5) can produce fiscal, economic and social benefits, but does not at this stage have evidence to give values to this possibility.

Impacts on local authority personal social services
Bramley and Watkins (2008) point out that the use of children’s social services is strongly associated with poverty. New Economy (2014) points to adult social service costs associated with mental health and residential social services.

Impacts on local environmental services
Bramley and Watkins (2008) find an association between street cleaning and other local environmental services, and poverty. These services are largely delivered by local authorities, though delivery may be shared with social housing providers in some cases. It is likely that the impacts of a poverty reduction programme on these issues would follow the age and gender pattern that we have reported relating to acquisitive crime, and also the elements discussed under education services.
3 IMPACTS ON THE ECONOMY

In this chapter we consider the impacts on the economy in terms of the economic output lost as a result of worklessness and low pay, the impacts on spending power and the multiplier impact of increases in spending.

The costs to the economy are largely based on the output, wages and spending that have been forgone because of worklessness and low incomes. Therefore, our estimates are based on the economic loss compared with what would happen if more people were in work and earning the Living Wage.

Impacts on economic output

The underlying assumption is that an employee will produce output equivalent to the cost of their employment (this will include employer NI contributions and contributions to pensions). Using this assumption we can calculate the additional economic output that would be generated by increasing the numbers in work and moving to the Living Wage.

However, this additional economic output will be an under-estimate because individuals receiving the Living Wage can be expected to spend more on consumption which then leads to additional economic output in shops, restaurants, consumer goods sectors and so on. This is the basis for the 'induced multiplier effect'.

Multiplier effects are controversial among economists. One reason for this is that estimates under different economic models produce quite different results. HM Treasury’s guidance, The Green Book: Appraisal and evaluation in central government (HM Treasury, 2014a, p. 54), discusses the use of multipliers in the wider context of estimating net or additional impacts of projects and programmes. It refers to guidance on additionality produced by English Partnerships in 2001 and updated in 2008 (English Partnerships, 2008), which gives specific advice on the values and how to apply multipliers. Similar guidance was also produced for the Department for Business, Innovation and Skills (DBIS) in 2009 (HM Treasury, 2009).
However, work on CBA for DWP by Fujiwara (see Appendix 2) recommends not using multipliers when assessing employment programmes. Fujiwara argues that in the absence of detailed information on spending patterns it is difficult to conclude whether the multiplier impacts of policies have a positive or negative impact on the economy. He therefore recommends against the use of multipliers.

For the purposes of this exercise we have taken the view that it is correct to apply an induced multiplier because in practice we would anticipate that additional spending in the economy is likely, on balance, to have a positive rather than a negative impact. Hence the overall impact of a reduction in poverty caused by raising to the Living Wage should include some account of multiplier effects.

**How much extra output would there be?**

For the City of Leeds, we estimate that there will be an additional output of £839 million each year (see Table 11). Most of this relates to the additional output from out-of-work people moving into employment – £13,169 per claimant getting work.

This primarily comprises wages, together with mandated employer contributions to NI and the new auto-enrolment pensions. The additional employer costs are very low for existing workers earning below the Living Wage as most are part-time workers, and our calculations for people starting part-time work at the Living Wage show very low mandatory labour cost.

In this calculation we make no distinction between new employees being employed in the private or public sector. In both cases employees earn their keep through cost-effective production of goods and services.

**Table 11: Increased output if people were earning the Living Wage**

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£1,654,500,000</td>
<td>£83,300,000</td>
<td>£13,900,000</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£58,779,600,000</td>
<td>£3,140,100,000</td>
<td>£825,300,000</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>£60,434,100,000</strong></td>
<td><strong>£3,223,400,000</strong></td>
<td><strong>£839,200,000</strong></td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Additional output per claimant</th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£406</td>
<td>£373</td>
<td>£271</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£13,133</td>
<td>£13,216</td>
<td>£13,169</td>
</tr>
<tr>
<td><strong>Average (weighted)</strong></td>
<td><strong>£7,065</strong></td>
<td><strong>£6,994</strong></td>
<td><strong>£7,363</strong></td>
</tr>
</tbody>
</table>

**Impact of increased spending: the multiplier effect**

Shifting workless people into employment and moving low-paid workers onto the Living Wage puts money in the pockets of workers, most of which will be spent in the local economy. The impact on individuals’ incomes is discussed in Chapter 4. The estimates are discussed in different sections to avoid double counting wages and employer output. Here we calculate the multiplier effect on local economic output.

Research (summarised in Lawton and Pennycook, 2013, pp. 33–34) has shown that raising the Minimum Wage boosts productivity which will help drive local economic growth.

Table 15 in Chapter 4 shows the net gain to individuals – this is the additional amount in people’s pockets when moving from benefits or increasing from the Minimum to the Living Wage.
We have applied an ‘income multiplier’ to this additional spending. The HM Treasury Green Book (HM Treasury, 2014a) estimates the multiplier effect as 1.2 – this means that for every £1 of additional net income a further 20p of economic output is generated. Table 12 sets out the results.

For example, most people moving into work will spend more on transport. This transport cost is a necessary expense and is additional spending. The additional traffic caused produces an increase in demand for a range of transport services, including petrol sales, bus ticket sales and so on. This is counted as additional economic output. Transport services may require additional workers to service the additional demand. The same principle applies to suppliers of other goods and services.

We have not included a ‘supply linkage multiplier’ in these estimates. Where cities have a defined programme to tackle poverty, with costs and spending profiles, it is more appropriate to include a multiplier. However, here we are concentrating on the impact of a reduction in poverty and not the process for how the reduction came about.

### Table 12: Multiplier effects of additional individual income

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£92,660,000</td>
<td>£4,679,913</td>
<td>£759,913</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£6,345,992,174</td>
<td>£344,583,840</td>
<td>£90,172,778</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>£6,438,652,174</td>
<td>£349,263,753</td>
<td>£90,932,691</td>
</tr>
<tr>
<td>Per-claimant multiplier effect</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In-work poor</td>
<td>£23</td>
<td>£21</td>
<td>£15</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£1,418</td>
<td>£1,450</td>
<td>£1,439</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>£753</td>
<td>£758</td>
<td>£798</td>
</tr>
</tbody>
</table>
Another important dimension in assessing the economic and financial benefits of tackling poverty is the impact on individuals and society in general. In this chapter we look at the direct impact on the income of individuals. It is also important to recognise that there are less tangible but equally important well-being benefits. Recent developments in how this wider society impact is measured means that we can estimate some values for Leeds.

Impacts on individual incomes

What is the impact if people earn the Living Wage?
An out-of-work person moving into a full-time Living Wage job in Leeds would, on average, have an additional gross annual income of £12,437 or £7,194 net of taxation — their take-home pay. For people who are already in work, the average gains of the Living Wage are substantially less at £251 gross and just £74 net of taxation.

The low level of gain for in-work people may cause surprise and is largely because:

- 75–80% of workers below the Living Wage work part-time (varying by area), and
- the ‘effective tax rate’, counting the withdrawal of Tax Credits, Housing Benefit and Council Tax Support, together with tax and NI payments, is between 65% and 70% in most cases.

Therefore, the impact of the Living Wage on gross pay depends on hours and the worker’s original pay rate. We estimate that the Living Wage would increase pay per hour for the median part-time worker who was paid below...
The benefits of tackling worklessness and low pay

Table 13 shows the change in individual incomes for three sample cases (which do not sum to the averages calculated earlier), showing how benefit withdrawal impacts particularly on workers who are already claiming in-work benefits.

<table>
<thead>
<tr>
<th>Table 13: Effect of taxes and benefit withdrawal on the impact of the Living Wage on net incomes</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Out of work</strong></td>
</tr>
<tr>
<td><strong>Before Living Wage</strong></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
</tr>
<tr>
<td></td>
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<tr>
<td></td>
</tr>
<tr>
<td><strong>Now in work Still in work (part-time) Still in work (part-time)</strong></td>
</tr>
<tr>
<td><strong>Income taxes/NI</strong></td>
</tr>
<tr>
<td><strong>Out-of-work benefits</strong></td>
</tr>
<tr>
<td><strong>Housing Benefit</strong></td>
</tr>
<tr>
<td><strong>Tax Credits</strong></td>
</tr>
<tr>
<td><strong>Total</strong></td>
</tr>
<tr>
<td><strong>Change</strong></td>
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<td></td>
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<td></td>
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</tr>
</tbody>
</table>

We have chosen the 20th percentile of part-time pay because around 40% of part-time workers earn less than the Living Wage. The 20th percentile of part-time pay is thus close to the median (half earn more, half less) of part-time workers below the Living Wage. The 20th percentile is thus close to the ‘typical’ wage for part-timers below the Living Wage.
The increase in gross pay is low, around 14%, because of the difference between the actual wage and the Living Wage. Government then recoups 70% of the increased gross pay in benefit withdrawals, leaving 30% of the 14% to the worker.

The 70% benefit withdrawal rate reduces to 65% under Universal Credit, but higher rates of benefit withdrawal for Council Tax Support may eliminate this advantage (see Bushe, et al., 2014).

In the extreme example, if all the out-of-work benefit claimants in Leeds were working full-time at the Living Wage, their net wages would add nearly £445 million annually to the City of Leeds economy (see Table 14). We have assumed that 70% work full-time and the rest part-time, the current proportions of Leeds employees.

Table 14: Additional gross earnings if the Living Wage were the minimum income

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£1,544,500,000</td>
<td>£77,800,000</td>
<td>£12,900,000</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£55,505,200,000</td>
<td>£2,966,000,000</td>
<td>£779,400,000</td>
</tr>
<tr>
<td>Total</td>
<td>£57,049,700,000</td>
<td>£3,043,800,000</td>
<td>£792,300,000</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Additional earnings per claimant</th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£379</td>
<td>£348</td>
<td>£251</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£12,402</td>
<td>£12,483</td>
<td>£12,437</td>
</tr>
<tr>
<td>Average (weighted)</td>
<td>£6,669</td>
<td>£6,604</td>
<td>£6,952</td>
</tr>
</tbody>
</table>

However, the tax and benefit system claws back around 38–39% of the additional income from people who move into work at the Living Wage (through benefit savings and additional taxes). This is known as the ‘participation tax rate’.

For those in work, we need to add the additional income for those currently earning below the Living Wage. Raising everyone to the Living Wage would affect 58,000 people in Leeds.

Between 75 and 80% are part-time workers, showing that the Minimum Wage labour market in Leeds is dominated by part-time work. Without any increase in hours worked, raising these wages to the Living Wage would add:

- £13 million to the gross earnings of current Leeds workers;5
- £78 million for Leeds City Region;
- £1.5 billion for workers nationally.

However, this is a gain in gross wages. Tapers within the in-work benefit system, together with taxes and NI, will reclaim approximately 70% of the increase in gross wages for HM Treasury.

The gains to individual incomes net of tax and benefit reductions form the basis for the estimates in Table 15 and of the multiplier effect included in Chapter 3.
Table 15: Net gains to individual incomes

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£463,300,000</td>
<td>£23,399,567</td>
<td>£3,799,567</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£31,729,960,870</td>
<td>£1,722,919,200</td>
<td>£450,863,890</td>
</tr>
<tr>
<td>Total</td>
<td>£32,193,260,870</td>
<td>£1,746,318,767</td>
<td>£454,663,457</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£114</td>
<td>£105</td>
<td>£74</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£7,090</td>
<td>£7,251</td>
<td>£7,194</td>
</tr>
<tr>
<td>Total</td>
<td>£3,763</td>
<td>£3,789</td>
<td>£3,989</td>
</tr>
</tbody>
</table>

The estimates for the net gain to individual incomes on moving from benefits to work are over £7,000 per year. This is an average figure, and figures will vary according to family and housing circumstances.

The participation tax rate, which measures the increase in net income on moving from benefits to work, is 38–39%. This is broadly consistent with earlier estimates of the extent to which the initial gain on starting work is clawed back by tax payments and benefit losses.

However, the net gains for the in-work poor are smaller because the combined effects of benefit withdrawal and increasing tax reduces gains by the ‘marginal deduction rate’. We have used an average marginal deduction rate of 70%, related to the current benefit system. Universal Credit is planned to reduce this to 65%. However, actual marginal deduction rates vary substantially according to family circumstances.

The gains to individual incomes for the in-work poor are small because 75% (in Leeds) of the individuals affected are part-time and the additional pay for the hours worked (where we have assumed no change) produces a small total. The tax and NI payments from these part-time workers will be zero. If fuller information were available on the earnings of in-work claimants, it is feasible that better estimates of gains to in-work claimants could be made.

Well-being benefits

It is more difficult to measure the concept of the costs and benefits to society of poverty. Economists view the issue of social cost through the prism of models based on the idea that the marginal utility (value) of income declines with increasing income levels. For example, a £10,000 increase is worth more to the person who has just £10,000 a year than to the person who already has £100,000.

The acceptance of this basic idea among economists partly explains why they tend to support raising Minimum Wages up to a point at which economic models suggest there could be a negative effect on employment numbers (see, for example, DeLong, 2014). In other words, this is the point at which the gain in income for some is offset by the loss of income for others. The history of the National Minimum Wage in the UK has involved much debate about the point at which negative effects on employment numbers might emerge, with little or no evidence that they have done so to date.

Our working assumption in this report is that increasing earnings to the Living Wage does not have a detrimental effect on employment levels. This is because we are quantifying the benefits that could accrue from reductions...
Impacts on individuals and well-being in worklessness and low pay with all in work paid at the Living Wage. Box 1 discusses some of the recent evidence as to the possible employment effects of the Living Wage.

If employment were to be reduced by moving all employees to the Living Wage, this effect would reduce the gains we have identified. However, we have already been cautious in excluding some other likely gains (for example, passported benefits).

The DWP social CBA review (Fujiwara, 2010) recommended a formula to estimate the well-being benefit of people moving into work (and hence the cost of not doing so). Fujiwara called this the ‘redistributive costs and benefits’, which, in summary, are the notional value of additional earnings to low-income people compared with the same increase for higher paid people. While this concept is intangible and non-cashable, it does have a direct bearing on people’s overall well-being.

Box 1: The Living Wage and employment

The Living Wage is not a statutory floor for wages. This report, in assessing the impact of all employees being paid the Living Wage, assumes that the Living Wage remains voluntary for employers. This combination would probably require a set of policies to increase the skills and productivity of low-paid workers so that employers would be voluntarily prepared to employ them at least at the Living Wage. In the absence of such policies there would be a risk either that not all employers would be willing to pay the Living Wage or that a legislative requirement that they do so would lead to some losses of employment.

The recent final report of the Living Wage Commission (2014) rejected a statutory Living Wage on the grounds that ‘the unintended consequences of taking this route now would be likely to outweigh the potential benefits’. The report quoted research undertaken by the National Institute for Economic and Social Research (NIESR) (Riley, 2013), which suggested that a compulsory Living Wage could result in a net loss of 160,000 jobs in the economy. Within this overall figure it was expected that there would be a loss of employment among young people aged under 30 years of around 300,000, compensated in part by an increase in employment among those aged 30 plus as employers replaced some younger workers with more experienced ones.

The NIESR research stresses that its results do not take account of all factors. Paying a Living Wage might increase labour productivity (e.g. via a reduction in absenteeism, or an increase in employee motivation), which could in part offset the potentially adverse employment demand effects of a Living Wage. On the other hand, the NIESR work does not take account of any potential scale effects where the cost increases with a Living Wage lead to a rise in the prices charged by companies. This potentially results in a fall in demand for their products, leading them to reduce the scale of their operations. Another factor that could add to the overall employment losses associated with the Living Wage would be if the wages of employees paid above the Living Wage also rose as employers sought to restore wage differentials compared with the directly affected low-paid workers.

The Living Wage Commission final report also notes the findings of a study by the Resolution Foundation/Institute for Public Policy Research.
The benefits of tackling worklessness and low pay

DWP used the formula in its assessment of the impact of the Future Jobs Fund (DWP, 2012b) where the well-being benefit of people getting work was assessed as £2,400 per participant. This was one element of an overall ‘society’ assessment of the Future Jobs Fund by Fujiwara, which was valued at a benefit of £7,750 per participant.

In the case of the Future Jobs Fund, the cost to the Exchequer was negative, but the benefits to participants, employers and society were strongly positive. This underlines how a fiscal analysis, while important in making the case to HM Treasury, may miss out key benefits to society. However, large estimates of the well-being or redistributive benefits based on complex formulae make it difficult to apply when looking at the costs and benefits of financing anti-poverty programmes locally because the estimated benefit is non-cashable.

If we were to apply the Fujiwara formula to Leeds, it generates an average additional well-being of £6,000 (see Table 16). However, this is not real additional income but the estimated additional value that low-income people will benefit by.

<table>
<thead>
<tr>
<th></th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>In-work poor</td>
<td>£694,950,000</td>
<td>£35,099,351</td>
<td>£5,699,351</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£47,594,941,305</td>
<td>£2,584,378,800</td>
<td>£676,295,835</td>
</tr>
<tr>
<td>Total</td>
<td>£48,289,891,305</td>
<td>£2,619,478,151</td>
<td>£681,995,186</td>
</tr>
<tr>
<td>Welfare weight per claimant</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>In-work poor</td>
<td>£170</td>
<td>£157</td>
<td>£111</td>
</tr>
<tr>
<td>Out-of-work poor</td>
<td>£10,634</td>
<td>£10,877</td>
<td>£10,791</td>
</tr>
<tr>
<td>Average (weighted)</td>
<td>£5,645</td>
<td>£5,683</td>
<td>£5,984</td>
</tr>
</tbody>
</table>

We have not included the well-being or redistributive benefits in our summary total, given that we have focused on identifiable and cashable costs and benefits. However, well-being benefits should ideally be taken into account by local areas when assessing the overall impact poverty reduction can make.
5 WHAT CAUSES DIFFERENCES IN THE IMPACT OF POVERTY REDUCTION LOCALLY?

The existing composition of the workforce and the current state of the local economy will affect the nature and degree of poverty. The level of activity in the local economy affects the number and type of jobs, while the composition by occupation and sector, as well as the level of unemployment, affects earnings levels. All these factors impact on the scale and nature of poverty at local level and need to be understood if local areas are assessing the costs and benefits of tackling poverty locally.

This sort of analysis will also have implications for local strategies (especially economic growth strategies) if they are to have an impact on poverty levels. The causes of local variations can help point to the interventions that local partners can make in order to narrow differences. Some causes are likely to be beyond the direct control of local agencies where they may only be able to encourage a long-term shift in the nature of the labour market.

**Different patterns of worklessness affect poverty**

The level of poverty in any one area will vary by both the extent and nature of worklessness and the level of wages of people who are in work. ‘Worklessness’ is composed of those who say they are:

- unemployed and claiming Jobseeker’s Allowance;
- unemployed and not claiming any benefits;
• currently not actively seeking work because they are claiming a health and disability benefit or have caring responsibilities; and
• inactive in the labour market and not claiming any state benefits.

The proportions of these groups vary substantially across the country and within city regions. For example, in Leeds City Region, Barnsley has the highest claim rate at 15.5% compared with 5.4% in Harrogate, and Leeds City at 12.1%. However, Bradford has an employment rate at 66.5% compared with 68.2% in Leeds. The differences include a higher inactivity rate in Bradford. The differences between Bradford and Leeds include a higher Leeds proportion who are students and economically inactive, and higher Bradford proportions looking after family or home and retired below age 64.

These different proportions can make substantial differences to the costs and benefits in a local area, as well as the strategy and actions a local area would deploy in reducing poverty.

**Different patterns of workless benefit claimants**

The overall benefit claim rate is not the whole picture and the breakdown between the different types of benefits is also important. Higher proportions of Employment Support Allowance (and Incapacity Benefit) claimants means potentially higher fiscal gains when reducing numbers, but it is also harder to secure these gains.

Table 17 shows that Leeds has proportionately more Jobseeker’s Allowance claimants and fewer Employment Support Allowance claimants compared with the national average. However, there will be significant variations below the local authority level, which should influence poverty reduction strategies and how local resources are targeted.

**Table 17: Numbers and proportions of workless claimants**

<table>
<thead>
<tr>
<th>Claimants of DWP benefits</th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jobseeker’s Allowance</td>
<td>1,132,550</td>
<td>68,630</td>
<td>19,800</td>
</tr>
<tr>
<td>Employment and Support Allowance and incapacity benefits</td>
<td>2,448,360</td>
<td>121,100</td>
<td>30,410</td>
</tr>
<tr>
<td>Lone parent (Income Support)</td>
<td>484,980</td>
<td>24,520</td>
<td>6,930</td>
</tr>
<tr>
<td>Others on income-related benefit</td>
<td>142,240</td>
<td>8,020</td>
<td>2,110</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>4,208,130</td>
<td>222,280</td>
<td>59,250</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Percentages of claimants</th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Jobseeker’s Allowance</td>
<td>27%</td>
<td>31%</td>
<td>33%</td>
</tr>
<tr>
<td>Employment and Support Allowance and incapacity benefits</td>
<td>58%</td>
<td>54%</td>
<td>51%</td>
</tr>
<tr>
<td>Lone parent (Income Support)</td>
<td>12%</td>
<td>11%</td>
<td>12%</td>
</tr>
<tr>
<td>Others on income-related benefit</td>
<td>3%</td>
<td>4%</td>
<td>4%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>100%</td>
<td>100%</td>
<td>100%</td>
</tr>
</tbody>
</table>

Finally, the number of students in a local area can also make a significant impact given that they will be included in the workless totals but would not necessarily be included in poverty reduction strategies.
**Different wage patterns affect poverty**

There are more people in poverty nationally who are in work than out of work. Patterns of pay differ by the nature of local economies, the split between full- and part-time workers, and the nature of the industry sectors and occupations. Different patterns of poverty arise from low wages and the level of opportunities for low-wage families being able to get out of poverty on a single full-time wage.

Pay for full-time workers in England averaged £27,375 in April 2013 (£13.00 per hour). This is the ‘median’ average (half way up or down the earnings ladder) as opposed to the ‘mean’ average, which can be distorted by the presence of high earners. Part-time workers are, on average, paid lower per hour than full-time workers. The median average hourly pay for part-timers was £8.06 an hour.

In general local economies can be characterised on a spectrum from ‘low skills equilibrium’ to ‘high skills equilibrium’ – with a similar spectrum of pay levels (OECD, 2012). The differences will lead to significant variations in the costs and benefits, critically in the gain to work for individuals and the value of increased output.

**How do wage differences affect Leeds?**

Leeds itself has pay levels that are relatively close to the England average, though not at the top end. However, other parts of the City Region have lower earnings. Leeds full-timers are paid (at median) 4.3% below the England level. West Yorkshire full-timers (which includes Leeds) are paid 9.3% below England, and North Yorkshire 8.6% below England. For part-timers, Leeds and West Yorkshire workers have hourly pay above the England figure, while North Yorkshire are 7.2% lower.

Figure 8 shows the distribution of hourly earnings for full-timers and part-timers in England, Leeds, North Yorkshire county and the former West Yorkshire county, for 2013. The central box shows earnings for the central half of employees. The lines above and below extend to the points at which 10% earn above that level, and the point at which 10% earn below that level. The central cross-bar in the box is the median.

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**Figure 8: Range of hourly earnings for full-time and part-time workers**

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In general local economies can be characterised on a spectrum from ‘low skills equilibrium’ to ‘high skills equilibrium’.
For full-time workers, just over 10% are paid below the Living Wage. However, for part-time workers the pattern is very different. Around 40% are paid below the Living Wage. From these figures, we can estimate how many workers in Leeds are paid below the Living Wage, and how much in extra wages it would take to lift them over the Living Wage.

**Different housing costs affect poverty**

People’s largest spending item is usually their housing cost. Housing costs vary between housing tenures and between areas. Rents in local council properties are usually lowest, followed by Housing Association properties on social rent and affordable rent properties. The most expensive are private rented properties.

Housing costs vary dramatically both between and within city regions. Within the Leeds City Region, average Housing Benefit awards for the out of work (where, before the bedroom tax, many claims were paid at 100% of rent) vary by 37% from £71 a week in Barnsley to £97 a week in Harrogate. These figures are for working-age claimants.

**Policy choices**

Flowing from an analysis of local variations, there are a number of approaches that could be adopted within local economic strategies. These are more likely to tackle poverty and can be justified in terms of the wider economic and fiscal benefits. Examples of policy objectives that could be pursued at local level are:

- Increase the proportion of higher paid jobs by attracting those sectors and occupations that pay more.
- Improve pay rates in low-paid jobs by actively encouraging employers to adopt the Living Wage.
- Improve opportunities for people to increase their working hours by improving affordable childcare and other social care.
- Provide sufficient part-time jobs for those people who want or need to work part-time.
- Support high-performing employment and training programmes that increase the employability of the local workforce.
- Provide an education and skills training system that can deliver the qualifications for local people that are needed by current and future employers.
- Promote in-work progression – encourage employers to train workers and encourage individuals to invest in their skills.
- Adopt a housing strategy that ensures there is a sufficient supply of affordable housing.
- Develop focused actions for people in entrenched poverty.
- Establish a local support services framework for the welfare system that helps people escape poverty and insecure employment.
In this chapter we look in more detail at the costs and benefits when assessing measures to reduce poverty in cities. For local policy-makers there will clearly be a trade-off between cost and effectiveness of local anti-poverty measures. However, at present there is little evidence as to what the trade-off may be and how to assess the costs and benefits of approaches. Here we focus in particular on the use of the New Economy CBA tool, described in detail below.

The advantage of a CBA tool is that it brings together the range of assumptions that local policy-makers have to make in planning a new intervention, and includes the best available evidence on financial impacts. The CBA tool ensures the hard questions are asked but it also gives some hard (quantifiable) answers in terms of the financial, economic and individual cost benefits.

The New Economy model and its uses
The New Economy CBA tool has been adopted by central government and published as supplementary guidance (HM Treasury, 2014b) to HM Treasury’s Green Book. Local authorities are increasingly using the tool. For example, the current phase of Whole Place Community Budgets are required to use it by the Cabinet Office in the development of their business plans. It uses a unit cost database for its default costs and fiscal
The benefits of tackling worklessness and low pay

benefits, though users can use it flexibly to add their own costs. Its use in practice is described in detail in a National Audit Office report (NAO, 2013). Commenting on the model, the NAO report concluded that:

• data on costs and benefits should draw on the best available evidence and compare costs and benefits on a like-with-like basis; and
• in keeping with economic decision-making principles, future costs and benefits should be reduced or ‘discounted’ to reflect their lower value compared with present-day costs and benefits.

The New Economy model comes as an Excel spreadsheet tool, with an accompanying technical specification that contains evidence on previous initiatives and how the various issues link together. In Box 2 we have used the model to develop a worked example for Leeds City.

Box 2: An illustrative worked example for Leeds

We used the New Economy tool to test what the fiscal impact might be for a new programme for the City of Leeds designed to improve the number of people finding work.

We have based the example on a total of 20,000 workless participants over three years. The purpose would be to realise the gains identified in the earlier examples of fiscal gains in Chapter 2. The basic proposition to test is whether the New Economy model shows there are fiscal and economic returns to additional expenditure to provide further employment support for one year for workless claimants.

The main inputs required by the tool are:

• the counterfactual – what would have happened anyway without the programme;
• performance gain – the additional impact the programme will have;
• cost – the actual costs of running the programme.

Counterfactual: according to our analysis of the Labour Force Survey, 48% of unemployed people in Leeds would normally have started work over the course of a year, and 11.5% of the economically inactive would normally have done the same. Estimates for the unemployed concentrating only on long-term unemployment would be much lower, but in this case we are considering the entire unemployed population, whether short- or long-term unemployed.

Performance gain: the performance assumption for unemployed people finding a job increases from 48.4% to 60% and for economically inactive people finding work increases from 11.5% to 17%.

Costs: the costs are based on an average £750 per participant for one year. This compares with £1,180, which is the estimated per participant cost for the two-year Work Programme (Inclusion, 2014).

In addition, there is a wide range of other factors in the model that can be varied, such as the nature of beneficiaries that then have an impact on the nature of the fiscal gains. Wherever feasible we have made assumptions that are in line with the profile of the Leeds population.
Table 18 reproduces the table that is generated by the model.

Table 18: Fiscal benefit–cost ratio – Leeds City employment programme (price base 2014)

<table>
<thead>
<tr>
<th>Overall fiscal CBA</th>
<th>Financial year</th>
<th>Net present value</th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Actual costs</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Costs</td>
<td>6,660,000</td>
<td>5,940,000</td>
<td>5,400,000</td>
</tr>
<tr>
<td>Discounted costs</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Costs</td>
<td>6,660,000</td>
<td>5,732,100</td>
<td>5,028,615</td>
</tr>
<tr>
<td>Benefits</td>
<td>4,692,757</td>
<td>3,553,829</td>
<td>3,747,794</td>
</tr>
</tbody>
</table>

The table shows that a three-year programme (2014 to 2016) would pay for itself after five years with a benefit–cost ratio of 1.19 (or a £1.20 return for every £1 spent).

What happens when you change performance?
If we change only the performance assumption, and nothing else, we can produce a chart (see Figure 9) comparing the benefit–cost ratio with the performance assumption – which is shown as the percentage above deadweight (the jobs that would have been gained anyway). This shows the relationship between improved performance and the return on investment, or benefit–cost ratio.

A key feature of the CBA is whether users expect improvements to be sustained. In this analysis, we have assumed that 90% of those who start work are in work in the following year, with a further drop in the next year. This is based on Work Programme providers’ expectations for job outcomes and sustainment payments made at the time they bid. The subsequent state of the economy, increases in job flexibility (such as zero-hour contracts) and bidder over-optimism may mean that this profile is also over-optimistic.

Figure 9: Leeds programme – how the benefit–cost ratio changes with performance
While our illustrative worked example produces a return to the taxpayer, all of these assumptions can be subject to much debate. However, we believe the assumptions in the model are based on sufficient evidence and the right level of expectations. For example, DWP has used an assumption of programmes achieving 25% over normal job-finding rates, based on evaluations of previous programmes. Whether or not this was realistic is an active question in relation to the Work Programme.

The focus of the Work Programme on in-work sustainment has proved difficult for providers as they had little evidence on which to base their delivery models. However, the learning experience from the Work Programme leads us to believe that future programmes will be better able to keep people in work rather than churn them round a low-pay/no-pay cycle.

The key challenge is whether cities can design and deliver programmes that help people into work more effectively than central government.

The New Economy CBA model calculates a separate economic CBA which measures the wider economic impact of the programme through the increased wages of people moving into work.

Table 19: Economic benefit–cost ratio – Leeds City employment programme

<table>
<thead>
<tr>
<th>Economic CBA</th>
<th>Financial year</th>
<th>Net present value</th>
</tr>
</thead>
<tbody>
<tr>
<td>Actual costs</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Costs</td>
<td>5,550,000</td>
<td>4,950,000</td>
</tr>
<tr>
<td>Benefits</td>
<td>8,559,292</td>
<td>6,717,056</td>
</tr>
<tr>
<td>Discounted costs</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Costs</td>
<td>5,550,000</td>
<td>4,776,750</td>
</tr>
<tr>
<td>Benefits</td>
<td>8,559,292</td>
<td>6,481,959</td>
</tr>
<tr>
<td>Economic benefit–cost ratio</td>
<td>2.61</td>
<td></td>
</tr>
</tbody>
</table>

This shows a far stronger impact, with an economic benefit–cost ratio of £2.61 for every £1 invested. This estimate is broadly comparable to, for example, the DWP impact assessment of the Future Jobs Fund (DWP, 2012b). In that analysis, it yields a very positive total impact on participants, employers and the Exchequer combined, and one that is more than three times as large as the impact on net participant incomes.

Who do the gains accrue to?
The model gives a high-level apportionment of the gains between the different agencies:

- 77% of the fiscal benefit accrues to DWP in benefit savings. This includes Housing Benefit savings which, in national accounts terms, come under DWP’s Annually Managed Expenditure.
- Most of the rest of the savings accrue to the NHS (10%) as savings in health costs.
- HMRC savings (3%) are reductions in Child Tax Credit as income rises.
- 7% of the savings accrue to the local authority.

This shows that the majority of the direct cashable gains go to central government. Local authorities receive 7% of direct gains (see Table 20) although this does not take into account all the wider and indirect costs.
of poverty and the strain it places on local services, which are outlined in Chapter 2.

**Table 20: Gains to different agencies**

<table>
<thead>
<tr>
<th>Agency</th>
<th>Gain (£)</th>
</tr>
</thead>
<tbody>
<tr>
<td>Local authority</td>
<td>£0.07</td>
</tr>
<tr>
<td>NHS</td>
<td>£0.10</td>
</tr>
<tr>
<td>Police/Criminal justice</td>
<td>£0.01</td>
</tr>
<tr>
<td>DWP</td>
<td>£0.78</td>
</tr>
<tr>
<td>HMRC</td>
<td>£0.03</td>
</tr>
<tr>
<td>Housing providers</td>
<td>£0.02</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>£1.00</strong></td>
</tr>
</tbody>
</table>

**Other issues**

In using such models it is important to be aware of a range of issues that are central to the design, implementation and assessment of anti-poverty and worklessness initiatives.

**Forecasts are likely to be wrong, but remain useful**

Cost–benefit methods are part of an appraisal process that necessarily involves predicting the future. However, the future is proverbially uncertain. The useful nature of forecasts comes from the process one goes through to make the forecasts. Understanding the processes by which people flow in and out of poverty not only helps with improving forecasts, but helps with designing programmes too.

**Deadweight – would people have exited poverty without your help?**

‘Deadweight’ loss is a feature of employment programmes. It occurs if, following the introduction of a particular initiative aimed at reducing worklessness, the intended outcome (i.e. reduced worklessness) would have occurred in the absence of that intervention. The labour market is dynamic; people move in and out of work all the time and deadweight will vary with the state of the economy.

**Churn – people move in and out of work, and in and out of poverty**

For Jobseeker’s Allowance, which is the benefit that has the largest churn, the total number of new claimants a year is around 3 million. The headline change in claimants is the difference between inflow and outflow numbers, which is usually between 3 and 4 million a year. Successful anti-poverty strategies have to recognise that people move out of poverty anyway, but they may be replaced by other people becoming poor. The issue in tackling poverty is not just increasing the exit rate from poverty, but also reducing the entrance rate.

**Substitution – are you helping some groups at the expense of others, and did you mean to?**

Programmes that are targeted on particular disadvantaged groups may succeed in helping them at the expense of some other group who would otherwise have got the jobs in question. It is a feature of employer behaviour that they may prefer to use employees who are assisted through a programme because they are cheaper, or because there is help from the
programme to manage the employee’s behaviour, rather than have their
own supervision and management in place. A key question for designers of
initiatives is what the consequences of helping a target group might be, and
whether any negative consequences on other groups are acceptable.

**Displacement – are you helping some firms at the expense of others?**
Interventions in the economy distort the market, which is what they are
designed to do. However, it is possible to distort the market in ways that
were not intended. An example of this may be the use of wage subsidy
schemes, which benefit some employers at the expense of others who may
already be supporting employment programmes, placing some employers at
a disadvantage to others.

**Are you being over-optimistic?**
Potential bidders are naturally optimistic and one of the more difficult issues
for programme bidders and commissioners to deal with is that people believe
they can improve on previous attempts. In the commissioning framework,
this is known as over-bidding. When developing programmes within the
public services, it is known as ‘optimism bias’. Where a project is wholly new
(a relatively rare occurrence), project designers can convince themselves that
it will work just because this is what the theory suggests. One way to address
this over-optimism is to undertake some scenario analysis to assess how
the costs and benefits of the proposed interventions change if plausible but
more pessimistic assumptions are adopted.

**Leakage – are you helping the areas you meant to help?**
In projects that are intended to help particular deprived areas within cities,
it is difficult to ensure that the help goes to the areas intended. One of the
characteristics of many deprived areas in cities is a high degree of population
movement. This has been an issue with some skills interventions targeted
in areas with low qualifications. Those who have been upskilled get jobs
outside the area and sometimes need to move away from the city, only to be
replaced by other low-skilled individuals.
7 CONCLUSIONS

This review of the costs and benefits of tackling poverty shows that claimants, government and society all gain by reducing poverty. Understanding the nature and drivers of poverty in any single local economy is the critical starting point for effective decisions on how cities can intervene to help increase incomes and reduce poverty.

Impacts on national and local government spending

There are substantial savings to government from people who are out of work moving into work at the Living Wage. We estimate the savings at £6,897 per person nationally.

The savings vary between areas because of:

- different rent levels affecting Housing Benefit savings;
- different patterns of ill-health benefits affecting reduced health costs;
- and
different age and gender patterns of claimants affecting crime costs.

The savings in Leeds City Region as a whole are 9% lower than nationally, but are still £6,280 per person. Leeds City is only 1% lower than the national average, so has much larger savings than the average of the rest of the Leeds City Region.

In addition, there will be savings from other areas of public services where evidence of the positive impact of moving to work at the Living Wage is not yet robust. These include impacts on housing services, education services, personal social services and local environmental services.
Table 21: Annual per capita gains to government (national and local) from out-of-work claimants moving into work at the Living Wage

<table>
<thead>
<tr>
<th>Subject</th>
<th>National</th>
<th>Leeds City Region</th>
<th>City of Leeds</th>
</tr>
</thead>
<tbody>
<tr>
<td>Benefit savings</td>
<td>£2,998</td>
<td>£2,494</td>
<td>£2,981</td>
</tr>
<tr>
<td>Administration savings†</td>
<td>£646</td>
<td>£651</td>
<td>£648</td>
</tr>
<tr>
<td>Direct taxation</td>
<td>£1,959</td>
<td>£1,959</td>
<td>£1,959</td>
</tr>
<tr>
<td>Reduced health costs</td>
<td>£846</td>
<td>£766</td>
<td>£750</td>
</tr>
<tr>
<td>Reduced crime costs</td>
<td>£448</td>
<td>£410</td>
<td>£461</td>
</tr>
<tr>
<td>Total</td>
<td>£6,897</td>
<td>£6,280</td>
<td>£6,800</td>
</tr>
</tbody>
</table>

Most of the direct costs of poverty are paid by central, rather than local, government bodies, even if some benefits are administered locally. Similarly, most of the direct cashable benefits to government of reducing poverty accrue to central rather than local bodies.

We have counted benefits and health services as centrally funded (apart from unfunded Housing Benefit administration), while crime costs are partially locally funded.

Many of the indirect costs of (and benefits of reducing) poverty fall to local government – and the extent to which the potential benefits are realisable depends on how initiatives are designed and implemented. Differences in who benefits mean that local authorities have a lower incentive than may be desirable to reduce poverty for their residents. Central government receives the great majority of the savings, while local authority benefits are either small or do not have robust estimates.

**Impacts on individual incomes**

The impacts on incomes of people starting work and getting the Living Wage are large and positive, on average.

Our estimates of the impact of the Living Wage on existing low-paid workers are much smaller. We have been cautious in making our estimates, and the small size of the effects primarily follows from our caution.

There are several relevant factors. In Leeds, we know that 10% of full-time workers were paid at the Living Wage or below, but we do not know how much below and did not want to assume they were paid at one of the National Minimum Wage range rates.

Of Leeds workers paid below the Living Wage, 62% work part-time. Substantial numbers are paid below the adult National Minimum Wage. We assume that these are on youth or apprenticeship rates, but still below the Living Wage. We have not assumed that part-time workers increase their hours when they start getting the Living Wage. If they are on low hours, the extra income they get is smaller.

Because of our caution, based on the lack of evidence at local level, the impacts on individual incomes we show for moving existing workers to the Living Wage are more likely to be on the low side than on the high side.

**Impacts on local economies**

Local economies stand to gain an average of £13,133 in additional economic output every time a claimant moves into a Living Wage job. This is the
benefit that the local economy gets, but it may not be visible locally as large employers count their turnover and profits at head offices.

Investing in tackling the causes of poverty needs to be seen as an integral part of investing to boost local economic growth. Alleviating the effects of poverty and managing the demand for local services will remain important, but there is a clear economic case for long-term strategies to reduce poverty.

With economic growth and employment now picking up, the question remains whether all will benefit. Increasing the number of jobs does not always mean that more people move out of poverty, nor will it reduce substantially the need for government to financially support low-income households. The shift to more people in poverty and in work demonstrates this. Encouraging a more balanced or inclusive growth will mean that policymakers (at all levels) need to scrutinise how this can be delivered.

In pursuing local economic policies for growth, the aim of poverty reduction should be integral. What has not been sufficiently recognised to date is the extent to which the nature and drivers of poverty vary at local level. This report has shown that the drivers behind the amount that is spent on relieving poverty at city level include:

- the characteristics of social security claimants;
- the average level of wages; and
- the nature of the housing market.

What has not been sufficiently recognised to date is the extent to which the nature and drivers of poverty vary at local level.

What does this mean for cities attempting to reduce poverty?

Developing a sound evidence base
First and foremost, cities need a sound evidence base of spending on social security. The evidence base also needs to identify the key influences that move people in and out of poverty.

Proofing local policies for their impact on poverty levels
Identifying the costs and benefits to cities of reducing poverty is feasible (at a sufficient level of detail) to inform the strategic decisions cities need to take about the nature of investment that is needed. The investment will include people, infrastructure and support services.

Adopting a cost–benefit approach
A cost–benefit approach helps make it clearer what elements are needed in a city strategy to increase growth and reduce poverty. In the context of reduced local government spending and the need to prioritise expenditure, a cost–benefit approach provides the basis for an investment appraisal that looks more holistically at the wider economic benefits of poverty reduction.

Review the policy choices
A number of approaches to poverty reduction can be adopted within local economic strategies and can be justified in terms of the wider economic and fiscal benefits. We have found that the main reasons for local variations in the costs and benefits are:

- the nature of the local economy – the types of jobs and industries;
- local wage levels – especially for entry-level jobs;
- the different patterns of worklessness, especially the number of people receiving health-related benefits;
• the balance between in- and out-of-work benefit recipients – areas with high levels of in-work poverty will gain the most from increasing pay levels; and
• housing costs and tenure – the level of rents vary considerably between areas and between different types of housing.

Policy choices
Examples of policy objectives that could be pursued at local level are:

• Increase the proportion of higher paid jobs by attracting those sectors and occupations that pay more.
• Improve pay rates in low-paid jobs by actively encouraging employers to adopt the Living Wage.
• Improve opportunities for people to increase their working hours by improving affordable childcare and other social care.
• Provide sufficient part-time jobs for those people who want or need to work part-time.
• Support high-performing employment and training programmes that increase the employability of the local workforce.
• Provide an education and skills training system that can deliver the qualifications for local people that are needed by current and future employers.
• Promote in-work progression – encourage employers to train workers and encourage individuals to invest in their skills.
• Adopt a housing strategy that ensures there is a sufficient supply of affordable housing.
• Develop focused actions for people in entrenched poverty.
• Establish a local support services framework for the welfare system that helps people escape poverty and insecure employment.

Who benefits?
At city level the immediate financial gains of reducing poverty are not always apparent. This is because most of the direct financial benefits accrue to national government rather than to the local area. There is no clear incentive for local partners to tackle poverty as part of local growth strategies or to make the most efficient and effective choices given local circumstances.

Even in a top-down approach of incentivising local activity, successful and innovative city poverty reduction strategies could be rewarded by local areas retaining some of the benefits savings, thereby incentivising local partners to invest more resources, time and energy in promoting a balanced and inclusive economic growth.

Designing strategies is one thing, but designing and delivering successful actions which are cost effective is quite another. A more rigorous approach using CBA may help local partners to identify their existing costs and redesign local services – as is happening in City Deals and Whole Place Community Budgets.

Finally, the pursuit of economic growth and poverty reduction is not just about a balance sheet approach to decision-making. It will also need leadership at local level to take some radical steps for which there may not always be sufficient evidence.
Executive summary
1. The administration savings are the savings in the cost of delivering benefits and jobsearch activation by Jobcentre Plus, Housing Benefit (and Council Tax Support), and Tax Credits, plus the cost of delivering programmes such as the Work Programme.

Chapter 2
2. The Leeds City Region is composed of the City of Leeds, Barnsley, Bradford, Calderdale, Craven, Harrogate, Kirklees, Selby, Wakefield and the City of York. It thus comprises the former West Yorkshire Metropolitan County plus substantial parts of North Yorkshire, and Barnsley from South Yorkshire.

3. The Fujiwara analysis is based on the economic cost of crime, using Home Office (now Ministry of Justice) analysis of the economic costs of crime.

Chapter 3
4. The other form of multiplier is the indirect multiplier, which measures the impact of purchases by businesses through their supply chains. These are not relevant to our argument here.

Chapter 4
5. This is based on residents of the area data from the Annual Survey of Hours and Earnings 2013 (ONS, 2013). This will under-report those below the NI threshold, and excludes self-employed people. The figures are therefore conservative estimates.

Chapter 5
6. Unfortunately, this means median figures for areas such as the Leeds City Region are difficult. We have therefore shown the former West Yorkshire and the county of North Yorkshire, for which figures are available. A considerable part of North Yorkshire is outside the Leeds City Region.

Chapter 6
7. New Economy provides research, strategy and policy development on behalf of the Greater Manchester Combined Authority and its partner bodies. The methodology builds on HM Treasury appraisal guidance and was developed with input from central government analysts.

Chapter 7
8. The administration savings are the savings in the cost of delivering benefits and jobsearch activation by Jobcentre Plus, Housing Benefit (and Council Tax Support), and Tax Credits, plus the cost of delivering programmes such as the Work Programme.
REFERENCES

[All URLs accessed 9 September 2014]


APPENDIX 1: DESCRIPTION OF WORKING-AGE BENEFITS AND MEASUREMENT ISSUES

DWP benefits

DWP benefits include: Jobseeker’s Allowance for unemployed people; Employment and Support Allowance (for those unable to work for health reasons) and its predecessors Incapacity Benefit and Severe Disablement Allowance; Income Support, which is paid to lone-parent claimants with a youngest child under the age of five and a number of smaller groups with no other means of support; and Disability Living Allowance (being replaced by the Personal Independence Payment), which, unlike the others, is not related to whether or not a person is in work.

There are a number of other benefits with smaller impact. The most significant of these is Carer’s Allowance, paid to those caring for a person with high care needs recognised by the Disability Living Allowance. This is often supplemented by Income Support as the level of benefit is low.

Issues with measurement

DWP publishes statistics on numbers of benefit claimants and the average level of claim at city (local authority) level quarterly, although with a delay of six months.

These statistics are based on administrative figures, so measure 100% of claimants. However, people who do not claim are not counted. If people claimed their full entitlement, claimant numbers and spending would be higher. Some people who are unemployed do not claim the benefits available, as the evidence from DWP and HMRC (reviewed by Finn and Goodship, 2014) shows. For Jobseeker’s Allowance 30–40% of potential spending is not taken up.
Approach adopted in this report
In this report we have counted benefit savings from DWP benefits offset against increases in HMRC Tax Credits when people move into low-wage work.

We have not counted any benefit savings in relation to disability benefits (Disability Living Allowance and Personal Independence Payment) as these were initially intended to cover some of the additional costs arising from disability. While disability benefits are included in welfare benefits in total,

we do not assume that the costs of disability reduce when people move into work.

HMRC benefits

The HMRC benefits we have considered are Working Tax Credits and Child Tax Credits. HMRC is also responsible for paying Child Benefit, but for people on low wages or out of work there is no difference in Child Benefit eligibility.

Measurement issues

HMRC publishes local-authority-level statistics on Working and Child Tax Credits as snapshots of current claims twice a year, in April and December, and a fuller annual release of finalised claims after they have reconciled the claims for a full tax year. This is published a year in arrears, so the figures for the year to March 2013 will have been published at the end of May 2014.

The approach taken in this report

People who are out of work and have children will be eligible for Child Tax Credit. We have identified the HMRC figures for out-of-work Tax Credits at local level within the total benefits estimates.

When people move into work at the Minimum or Living Wage they should be eligible for the Working Tax Credit and, depending on income and family circumstances, their Child Tax Credit will be tapered (reduced).

In our calculations we have assumed that people move into work at the average level of in-work Tax Credits for their area. We considered whether or not to adjust the average level of Tax Credits because some Tax Credit recipients earn at higher levels. However, part of the impact of the Coalition’s welfare reforms has been to reduce Tax Credit eligibility for in-work families to those on much lower incomes than were eligible previously.

We decided not to adjust the average in-work Tax Credit payment used, on the basis that the Tax Credit system provides a subsidy to childcare costs that could otherwise push families towards poverty. As childcare is a key part of a strategy that involves encouraging an increase in paid work by parents, we felt it would be illogical to exclude from our estimates people who may be slightly higher paid than the average.

A more sophisticated analysis would unpack the increase in childcare support needed, taking into account the population demographics of those in poverty, and the impact of Tax Credit (and, in future, Universal Credit) support for childcare.

We have estimated the Living Wage for a couple, assuming that one is in full-time work at average full-time hours, and that the other partner works part-time at the average hours of part-time workers. This produces a couple gross income of between £21,900 and £22,200 a year, varying by differences in the local patterns of working hours. HMRC produces figures
on the incomes used to taper payments. Using these figures, we estimate that about 13% of Tax Credit spending relates to households above such a couple Living Wage rate.

**Housing Benefit**

Housing Benefit is administered by local authorities for DWP. Local authorities carry out checks on eligibility and calculate the benefits.

The average Housing Benefit level paid to out-of-work working-age claimants in the Leeds City Region (covering a high proportion of rent, if not all) varies from £97 per week in Harrogate to £71 per week in Barnsley. This is a 37% difference in the rent level covered by Housing Benefit. There is a larger difference in the (tapered) amount paid for in-work claimants. The Harrogate in-work claimants are paid almost 50% more Housing Benefit than those in Barnsley.

If Housing Benefit did not make some attempt to equalise incomes after housing costs, these differences would make more of an impact on poverty. However, because in-work Housing Benefit is only partial, these housing cost differences do make a difference to disposable incomes.

Housing Benefit is administered differently for social housing and the private rented sector, where it is known as Local Housing Allowance. For the private rented sector, maximum acceptable rent levels are set by the Valuation Office Agency, which effectively sets the normal rent level for claimants within the Broad Rental Market Areas.

People who are claiming a DWP income-related benefit, which includes the income-related elements of all the main DWP benefits, have their Housing Benefit claims ‘certificated’ by DWP. This means that local authorities do not have to undertake means testing and therefore administration is cheaper. For other cases, whether claiming contribution-related benefits or in-work, the local authority undertakes a means test.

**Measurement issues**

DWP publishes information on Housing Benefit claims monthly. This is broken down by age group and by whether people are in work. The data covers Housing Benefit claims paid, and shows claimant numbers and average payments at local authority level. The DWP data also includes whether benefit has been reduced as a result of the Spare Room Subsidy or ‘bedroom tax’.

**The approach taken in this report**

We have taken a simplified approach of identifying the average Housing Benefit payment in Leeds for both in-work and out-of-work claimants. We have excluded pensioner Housing Benefit claims from the averages. A more sophisticated analysis would disaggregate in-work and out-of-work working-age claimants by more detailed housing tenure and bedroom number.

**Council Tax Support**

Local authorities are now responsible for both the funding and administration of Council Tax Support in England. This is a change from the earlier position when, as for Housing Benefit, local authorities administered...
Appendix 1: Description of working-age benefits and measurement issues

The Coalition also reduced it by 10%.

The Department for Communities and Local Government has a model Council Tax scheme, but authorities are free to vary this. The main requirement from central government is that pensioners continue to receive 100% Council Tax Support on the same basis as the previous DWP scheme. This means that the 10% reduction in budget is weighted onto working-age claimants.

JRF has supported the New Policy Institute to collect and publish information on local Council Tax Support schemes. This information is published at www.counciltaxsupport.org.

In Leeds, the average loss of support compared with the DWP system is £3.30 per week for those in work, and £3.90 a week for those out of work.

Measurement issues
Some statistics are available from DWP on the old Council Tax Benefit system, and from www.counciltaxsupport.org on the aggregate changes since then.

However, previous DWP Tax-Benefit Model Tables (DWP, 2010) show that in-work Council Tax Benefit was payable in many cases when the only worker in a family worked part-time, but was only payable to families with one full-time worker when they had large families. The changes to Council Tax Support have removed this theoretical eligibility in most cases. Therefore it is likely that, in Leeds, Council Tax Support claimants moving to full-time work at the Living Wage would extinguish eligibility for Council Tax Support under the new scheme. If they moved to part-time work they would continue to be eligible.
APPENDIX 2: PREVIOUS ESTIMATES OF COSTS AND BENEFITS

The cost of unemployment (1990–2001)

Our predecessor organisation, the Unemployment Unit, published a semi-regular series estimating the Exchequer cost of unemployment from 1990 to 2001.

The calculations were regularly quoted by local organisations seeking to build a case for developing local provision for the unemployed and inactive. The intention was to show that there were benefits from getting people into jobs, and that these could be substantial.

However, the focus was on costs and benefits to the public purse, the Exchequer, rather than the total economic costs and benefits. These wider subjects were covered in a series of macro-economic evaluations of provision such as that for the New Deals. However, even these excluded a range of benefits where there was an association between employment and the issue, such as crime reduction and health benefits.

The 2001 version of the calculation is shown in Table 22 (Unemployment Unit, 2001).

Table 22: Exchequer costs of unemployment

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Direct costs (millions)</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Benefits for claimant unemployed</td>
<td>£5,360</td>
<td>£5,010</td>
<td>£5,020</td>
</tr>
<tr>
<td>Benefits for ‘non-claimants’</td>
<td>£1,692</td>
<td>£1,784</td>
<td>£2,449</td>
</tr>
<tr>
<td>Administration costs</td>
<td>£904</td>
<td>£900</td>
<td>£896</td>
</tr>
<tr>
<td>Redundancy Fund (incl. admin)</td>
<td>£130</td>
<td>£166</td>
<td>£174</td>
</tr>
<tr>
<td>Total direct costs</td>
<td>£8,086</td>
<td>£7,860</td>
<td>£8,539</td>
</tr>
</tbody>
</table>

Table 22 continues on page 55
---|---|---|---|
**Foregone revenue**<br>PayE (net) per unemployed person | £2,692 | £2,869 | £2,889 |
Income Tax total (net) (millions) | £6,778 | £6,574 | £6,478 |
Ni per unemployed person | £1,678 | £1,699 | £1,682 |
Ni contributions total (millions) | £4,225 | £3,894 | £3,771 |
Indirect tax per unemployed person | £2,100 | £2,169 | £2,274 |
Indirect taxes total (millions) | £5,288 | £4,969 | £5,099 |
Total foregone revenue (millions) | £16,292 | £15,437 | £15,348 |
Foregone revenue per unemployed person | £6,470 | £6,737 | £6,846 |

---|---|---|---|
**‘Broad’ Labour Force Survey** | 2,518,083 | 2,291,531 | 2,242,000 |
Claimant count | 1,328,775 | 1,209,225 | 1,209,225 |
Total cost (millions) | £24,378 | £23,297 | £23,887 |
Total cost (billions) | £24.4 | £23.3 | £23.9 |
Total cost divided by all unemployed | - | - | - |
Cost per claimant | £11,280 | £11,760 | £11,880 |
Cost per ‘non’-claimant | £7,140 | £7,520 | £7,940 |

The calculation of the Exchequer cost showed that the costs to the government of people being unemployed were substantially greater than the direct benefit cost.

We did not persist with the series because there were changes to the tax and benefit system that made it difficult to produce estimates that were consistent. These included the introduction of the Working Families Tax Credit and later the Working Tax Credit which reduced the Exchequer benefit from a claimant starting work.

The 2001 article also included an assessment comparing the value of what we would now call ‘sustainment’ in work, in the context of different levels of investment in the human capital of the unemployed. This was done using a net present value of the Exchequer benefit of participants being in work as shown in Table 23.
While the scenarios were constructed, the concept that sustainment in work, higher pay and pay progression contribute to substantially increased returns, and can justify high-cost programmes, remains valid.

However, a major issue in persuading government of the value of investing in in-work sustainment has been that the official cost–benefit frameworks had not accepted that savings beyond a one-year horizon could be attributed to an employment programme.

This attitude changed in the Freud review of 2007.

**Table 23: The value of investing in human capital**

<table>
<thead>
<tr>
<th></th>
<th>High investment, high retention</th>
<th>High investment, high retention</th>
<th>Low investment, medium retention</th>
<th>Low investment, low retention</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Discount rate</strong></td>
<td>5%</td>
<td>5%</td>
<td>5%</td>
<td>5%</td>
</tr>
<tr>
<td>Year 1 spending</td>
<td>£15,000</td>
<td>£15,000</td>
<td>£3,000</td>
<td>£3,000</td>
</tr>
<tr>
<td>Year 2 return</td>
<td>£5,000</td>
<td>£5,000</td>
<td>£5,000</td>
<td>£5,000</td>
</tr>
<tr>
<td>Year 3 return</td>
<td>£5,200</td>
<td>£5,000</td>
<td>£5,000</td>
<td>£-</td>
</tr>
<tr>
<td>Year 4 return</td>
<td>£5,408</td>
<td>£5,000</td>
<td>£-</td>
<td>£-</td>
</tr>
<tr>
<td>Year 5 return</td>
<td>£5,624</td>
<td>£5,000</td>
<td>£-</td>
<td>£-</td>
</tr>
<tr>
<td>Year 6 return</td>
<td>£5,849</td>
<td>£5,000</td>
<td>£-</td>
<td>£-</td>
</tr>
<tr>
<td>Year 7 return</td>
<td>£6,083</td>
<td>£5,000</td>
<td>£5,000</td>
<td>£-</td>
</tr>
<tr>
<td>Year 8 return</td>
<td>£6,327</td>
<td>£5,000</td>
<td>£-</td>
<td>£-</td>
</tr>
<tr>
<td>Year 9 return</td>
<td>£6,580</td>
<td>£5,000</td>
<td>£-</td>
<td>£-</td>
</tr>
<tr>
<td>Year 10 return</td>
<td>£6,843</td>
<td>£5,000</td>
<td>£-</td>
<td>£-</td>
</tr>
<tr>
<td>Net present value</td>
<td>£25,010</td>
<td>£19,561</td>
<td>£12,067</td>
<td>£4,194</td>
</tr>
<tr>
<td>Annual pay increase</td>
<td>4%</td>
<td>0%</td>
<td>0%</td>
<td>0%</td>
</tr>
</tbody>
</table>

The table in the Freud review intended to justify these figures shows a different total for lone parents, of £3,800 rather than £4,400, with a
footnote that the Exchequer savings would be lower if the lone parent used Childcare Tax Credit.

These are comparisons of the Exchequer flows from benefits and taxes in the in-work and out-of-work cases, on a full-year basis. They take no account of the cost or likelihood of the person involved getting into work and staying in work.

Freud did argue that:

"The full annual Exchequer saving of getting a person on incapacity benefits into work is around £9,000. To the extent that the person would not have otherwise worked for many years, the saving to the State is a multiple of this figure. Once a person has been on incapacity benefits for a year, they are on average on benefit for eight years. So a genuine transformation into long term work for such an individual is worth a net present value of around £62,000, per person to the State."

This was calculated as the net present value of Exchequer savings from an Incapacity Benefit recipient staying in work for eight years, discounted at HM Treasury recommended rates.

The argument that savings could be multiplied if the jobs were sustained for extended periods was made.

The argument then flowed through into discussions between DWP and HM Treasury under both governments about the ‘DEL-AME switch’ – paying for current programmes out of benefit savings that were expected to accrue in the future.

Methodologies for estimating and incorporating the wider social and economic impacts of work in the CBA of employment programmes


The report exhaustively discusses a range of possible impacts on the costs and benefits of programmes. These included:

- in-work costs;
- non-market time;
- equilibrium effects in the labour market – substitution, displacement and wage effects;
- the social cost of Exchequer finance;
- the impacts of work and programmes on health;
- the impacts of work and programmes on crime rates;
- multiplier effects – of spending by both programme participants and programme staff;
- product market correctors – whether wages are likely to be an understatement of the impacts of our employment programmes on the economy; and
- welfare weights – the welfare impacts, given how costs and benefits are distributed across society.

The net result is a matrix of possible effects identified by whom they affect, as shown in Table 24.
### Table 24: Estimating costs and benefits of employment programmes: a DWP framework table

<table>
<thead>
<tr>
<th>Impact</th>
<th>Perspective</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Participants</td>
</tr>
<tr>
<td>Increase in output</td>
<td>N/A</td>
</tr>
<tr>
<td>Increase in wages</td>
<td>+</td>
</tr>
<tr>
<td>Programme payments to employers</td>
<td>N/A</td>
</tr>
<tr>
<td>Programme payments to providers</td>
<td>N/A</td>
</tr>
<tr>
<td>Reduction in DWP operational costs (net)</td>
<td>N/A</td>
</tr>
<tr>
<td>Reduction in benefits (net)</td>
<td>-</td>
</tr>
<tr>
<td>Increase in direct and indirect taxes</td>
<td>-</td>
</tr>
<tr>
<td>Increase in travel and childcare costs</td>
<td>-</td>
</tr>
<tr>
<td>Reduction in healthcare costs</td>
<td>N/A</td>
</tr>
<tr>
<td>Reduction in crime</td>
<td>N/A</td>
</tr>
<tr>
<td>Redistributive costs and benefits (welfare weight)</td>
<td>+</td>
</tr>
<tr>
<td>Social cost of Exchequer finance</td>
<td>N/A</td>
</tr>
<tr>
<td>Multiplier effects</td>
<td>N/A</td>
</tr>
</tbody>
</table>

Key: ‘+’ denotes a net benefit; ‘-’ denotes a net cost; ‘=’ denotes that benefits and costs balance to zero for society as a whole; ‘N/A’ denotes neither a cost nor a benefit.

The column for ‘society’ is the net result of all the other impacts, with the exception of the line for the social cost of Exchequer finance, where this is estimated to be the negative effect on the economy as a whole of distortions induced by additional taxes or borrowing required to fund a programme.

**A society perspective**

What is evident from the matrix is that many of the individual items that are important from an Exchequer point of view are netted off on a society view – so programme payments to employers are a cost to the employer and an equal inflow for employers. The same goes for benefit reductions between the Exchequer and individuals.

This means that when we are considering the issue from the point of view of contributions to growth, we can concentrate on those items that do not net off in the ‘society’ column.

**Output**

The value of output from a person moving from benefits to work can be estimated as the labour cost, comprising mainly wages and employer NI. In future, the mandated employer cost of auto-enrolled pensions can be included here.

**Multipliers**

Fujiwara recommends against the use of multiplier effects in the assessment of the costs and benefits of employment programmes. There are a number of points made. Firstly, the change in wages already picks up impacts on
Appendix 2: Previous estimates of costs and benefits

The individual (p. 50). If secondary markets were perfect, then all the gain to society would be reflected in the wage. However, as this is unlikely to be the case, Fujiwara suggests that there may be effects but they are not well-evidenced in the (pre-recession) economics research literature.

The more recent research by Olivier Blanchard and David Leigh of the International Monetary Fund (2013) and others identifies multiplier effects of government spending. They find that the multiplier effects at national and international level relate to the state of the economic cycle. The issue of whether or not multiplier effects vary with the state of the local labour market in cities and small areas is not resolved.

Fujiwara argues strongly against the continued use of multipliers from the Additionality Guide originally published in 2001 and subsequently updated (English Partnerships, 2008) with similar guidance produced for BIS in 2009 (HM Treasury, 2009). He argues that those recommendations were not based on the economics literature.

Redistributive costs and benefits (welfare or well-being)

Redistributive costs and benefits (the impact on society of costs and benefits being distributed across different income groups) are included in the major documents discussing costs and benefits, such as the Treasury Green Book (HM Treasury, 2014a) as well as the Fujiwara paper (2010).

Fujiwara prefers to call this a ‘welfare weight’, a recommendation that was not followed when the approach was used in the assessment of the impact of the Future Jobs Fund (DWP, 2012b).

Fujiwara discusses a wide range of recent economic research on the impacts on what economists term ‘welfare’ for different income groups in society. He concludes that the advice in the Treasury Green Book under-estimated the impacts on welfare, and recommended the use of a higher multiple of the net income gain to people moving from benefits to work.

Health impacts

Fujiwara makes the following recommendations for applying health impacts in CBA:

- Estimate the number of additional job years resulting from an employment programme.
- For non-Employment and Support Allowance programmes, multiply the number of additional job years by £508. This will provide an estimate of the expenditure savings accrued from the programme.
- For Employment and Support Allowance programmes, multiply the number of additional job years by £1,016. This will provide an estimate of the expenditure savings accrued from the programme.
- These estimates are derived from 2008 figures and, therefore, should be uprated by inflation where relevant.
- The analysis should be supplemented by a description of the caveats.

This was based on estimates of health costs and on ‘factory’ studies reporting on the health declines reported by people when factories closed and they were made redundant, regardless of their original health status.

The impact of crime

Fujiwara includes a detailed review of the evidence linking acquisitive crime and income levels.

The review provides evidence that the impact of employment programmes on crime relates to the age and gender structure of those helped, given that crime is disproportionately committed by young men.
Travel and childcare costs
These are included as costs that would not be incurred if the programme participant were not in work. The discussion of the evidence on childcare regards the relevant cost to include as a cost net of Tax Credit or other support.

What the Fujiwara paper does not do is account for the benefits of childcare. In terms of Sure Start Centres, it is at this stage, too early to estimate the impact of high-quality formal childcare on labour market outcomes of those children helped. However, the US literature on Head Start and Perry Pre-School indicates that childcare should not necessarily be considered as a cost item only – there may be benefits to the child in addition to enabling the parents to work.

The first full-scale use of the cost–benefit framework as recommended by Fujiwara was in the impact assessment of the Future Jobs Fund. This is discussed below.

Impact assessment of the Future Jobs Fund

The official impact assessment of the Future Jobs Fund (DWP, 2012b) was substantially more sophisticated than the estimates made in the Freud review. It used the Fujiwara framework and recommendations, with some limitations. Table 25 is drawn from the report.

Table 25: The estimated costs and benefits per participant of the Future Jobs Fund programme under baseline assumptions

<table>
<thead>
<tr>
<th>FJF programme impact</th>
<th>Participants</th>
<th>Employers</th>
<th>Exchequer</th>
<th>Society</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increase in output</td>
<td>0</td>
<td>+4,400</td>
<td>0</td>
<td>+4,400</td>
</tr>
<tr>
<td>Increase in wages</td>
<td>+4,300</td>
<td>-4,300</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>FJF employer payments</td>
<td>0</td>
<td>+6,850</td>
<td>-6,850</td>
<td>0</td>
</tr>
<tr>
<td>Reduction in operational costs</td>
<td>0</td>
<td>0</td>
<td>+900</td>
<td>+900</td>
</tr>
<tr>
<td>Reduction in benefits</td>
<td>-1,450</td>
<td>0</td>
<td>+1,450</td>
<td>0</td>
</tr>
<tr>
<td>Increase in taxes</td>
<td>-1,000</td>
<td>-100</td>
<td>+1,100</td>
<td>0</td>
</tr>
<tr>
<td>Increases in travel and childcare costs</td>
<td>-250</td>
<td>0</td>
<td>0</td>
<td>-250</td>
</tr>
<tr>
<td>Reduction in healthcare costs</td>
<td>0</td>
<td>0</td>
<td>+300</td>
<td>+300</td>
</tr>
<tr>
<td>Redistributive costs and benefits</td>
<td>+2,400</td>
<td>0</td>
<td>0</td>
<td>+2,400</td>
</tr>
<tr>
<td>Social cost of Exchequer Finance</td>
<td>0</td>
<td>0</td>
<td>0</td>
<td>0</td>
</tr>
<tr>
<td>Total programme impact</td>
<td>+4,000</td>
<td>+6,850</td>
<td>-3,100</td>
<td>+7,750</td>
</tr>
</tbody>
</table>

Key: ‘+’ denotes a net benefit; ‘–’ denotes a net cost; ‘0’ denotes neither a cost nor a benefit.

Source: (DWP, 2012b)
Note: Totals may not sum due to rounding.

The analysis showed that:

- The net benefit to participants was £4,000 per participant, based largely on the increase in wages net of taxes and benefits reduction and also the redistributive costs and benefits – the Fujiwara ‘welfare weight’.
• The net benefit to employers was £6,850, the value of the employer payment, as the value of output is equal to wages plus employer NI (the marginal productivity being equal to the labour cost).
• The net cost to the Exchequer was £3,100, with the employer payments offset substantially by reduction in DWP operational cost, benefit reductions and tax increases.
• The net cost to society is the sum of all of these.

In this analysis, the additional health benefit from working is calculated, but is almost completely offset by the increased costs of working in travel and childcare costs.

The major contributors to the benefit to society come from:

• the increase in output, which is assumed (as economists do by default) to be equal to the labour cost – wages plus employer NI payments;
• the redistributive costs and benefits; and
• the reduction in DWP operational cost of administering the welfare system.

**Impacts for this analysis**

A useful guide is produced by using the DWP impact assessment as a ‘worked example’ for estimating the costs to society of a person being out of work and on benefits in opposition to being in work.

We have to date concentrated on the ‘big-ticket’ elements that impact on society as a whole, and determined which of these can be used at local level.

The impacts on the Exchequer, in the cost–benefit matrix, have been estimated in the aggregate rather than in detail (see Table 26).

**Table 26: Estimating costs and benefits; whether local information is available and whether impacts are positive or negative (or not appropriate)**

<table>
<thead>
<tr>
<th>Impact</th>
<th>Participants</th>
<th>Employers</th>
<th>Providers</th>
<th>Exchequer</th>
<th>Society</th>
</tr>
</thead>
<tbody>
<tr>
<td>Increase in output</td>
<td>N/A</td>
<td>+ Local</td>
<td>N/A</td>
<td>N/A</td>
<td>+ Local</td>
</tr>
<tr>
<td>Increase in wages</td>
<td>+ Local</td>
<td>Local</td>
<td>N/A</td>
<td>N/A</td>
<td>=</td>
</tr>
<tr>
<td>Programme payments to employers</td>
<td>N/A</td>
<td>+</td>
<td>N/A</td>
<td>–</td>
<td>=</td>
</tr>
<tr>
<td>Programme payments to providers</td>
<td>N/A</td>
<td>N/A</td>
<td>+</td>
<td>–</td>
<td>=</td>
</tr>
<tr>
<td>Reduction in DWP operational costs (net)</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>+ National</td>
<td>+ National</td>
</tr>
<tr>
<td>Reduction in benefits (net)</td>
<td>– Local</td>
<td>N/A</td>
<td>N/A</td>
<td>+ Local</td>
<td>=</td>
</tr>
<tr>
<td>Increase in direct and indirect taxes</td>
<td>– Direct: Local</td>
<td>– Direct: Local</td>
<td>–</td>
<td>+</td>
<td>=</td>
</tr>
<tr>
<td>Increase in travel and childcare costs</td>
<td>– National (no local data yet available)</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>– National (no local data yet available)</td>
</tr>
<tr>
<td>Reduction in healthcare costs</td>
<td>N/A</td>
<td>N/A</td>
<td>N/A</td>
<td>+</td>
<td>+ National</td>
</tr>
</tbody>
</table>

*Table 26 continues on page 62*
We have assembled sources for estimating the key elements of this sort of analysis at local authority level. These are:

- Earnings: mean and median earnings are available at local authority level for full-time employees, part-time employees and all employees. We have based our estimates on people moving from local earnings figures that are below the Living Wage (or are out of work) to the Living Wage. DWP (and, using the DWP data, the New Economy model) use higher estimates for this.
- Employer NI: can be calculated on the basis of the resulting earnings calculation, using announced rates.
- Output: this is assumed to be equivalent to the labour cost elements of gross wages plus employer NI.
- Reduction in DWP administration cost. The unit cost figure as given in the Future Jobs Fund report can be updated by published DWP productivity estimates.
- Income Tax and employee NI has been calculated based on earnings (above) and published rates.
- Benefit savings have been calculated for each local authority based on statistics for caseload and payments for each out-of-work benefit, and for Housing Benefit, where we have calculated the difference between in-work and out-of-work Housing Benefit at local authority level, net of HMRC Tax Credits. In each case the most up-to-date data has been used, but these relate to various dates. The HMRC data is the earliest, being based on finalised assessments for 2012–13. Subsequent reductions in the value of Tax Credits will reduce the impact. Housing Benefit figures are current, and show the impact of the Housing Benefit cap in that there are a number of London authorities where average in-work Housing Benefit is higher than out-of-work Housing Benefit, the opposite to the effect in other parts of the country.
- Net economic benefit per individual is the average wage net of taxes and NI less the benefit saving net of in-work benefits.
- This enables a calculation of the redistributive effect of an out-of-work individual on benefits moving into work at local authority level.
- We can assume that the health benefits of moving into work are similar to those in the Future Jobs Fund impact report.
- We have so far done this at aggregate level.
- Remaining to do is to separate impacts for part-timers (assuming that lone parents move into part-time work).

We have also used the median earnings for 2012 in our calculations, for people working in the area. There are a number of local authorities where mean earnings are available but not medians, so we intend to use the mean for these areas.
APPENDIX 3: THE MANCHESTER NEW ECONOMY COST–BENEFIT MODEL

The Manchester New Economy cost–benefit model attempts to place a value on three different types of benefits (or outcomes) associated with delivering a specific service or intervention within a project area. These are:

- Fiscal benefits: savings to the taxpayer that are due to a specific project – for instance, reduced benefit costs (Jobseeker’s Allowance, Employment and Support Allowance and Income Support for Lone Parents), health service, police or education costs.
- Economic benefits: gains that accrue to individuals – for instance, increased earnings, or to the whole economy – for instance, increased gross value added as a result of more people being employed.
- Social benefits: gains that accrue to society – for instance, improved health and well-being or increased satisfaction with the community.

The model’s analysis timeframe is a five-year assessment of costs and benefits which has been chosen to reflect the need to identify short-term savings of a project to the public sector.

The key output from the model is the benefit–cost ratio (BCR). The BCR measure is a ratio of the monetised value of the outcomes of the project (the benefits) to the cost of implementing the project and provides an indication of the return on investment achieved by the project. A BCR<1 indicates that the project has cost more than it has achieved and therefore is not economically beneficial and should be considered for decommissioning. A BCR of 1 is the breakeven point at which the benefits achieved exactly match the costs incurred. It could be argued that any scheme which has a benefit–cost ratio >1 should therefore be progressed.

For the Leeds example we have used the total cohort of those claiming out-of-work benefits split by those claiming Jobseeker’s Allowance, those claiming Employment and Support Allowance and those lone parents claiming Income Support. The analysis is broken down into the impact on a number of specific outcomes.

The outcomes we have included are:

- reduced number of individuals claiming;
- increased number of people holding Level 2 and Level 3 skills;
• reduced number of adults with mental health problems;
• reduction in re-offending;
• reduced housing evictions;
• reduced number of children in care;
• reduced drug abuse and alcohol dependency;
• reduced truancy; and
• increased well-being of adults and children.

We have estimated the total population that are likely to benefit from the above outcomes for the Leeds City Area. The overall cohort comes from DWP statistics by benefit claimed. To this cohort we have applied proportions for various groups from various sources, for example:

• qualification levels of those out of work in Leeds and the number of children in workless families from the Census;
• those with mental health issues claiming Employment and Support Allowance from DWP;
• eviction rates in Leeds from Shelter;
• local re-offending rates from West Yorkshire police;
• truancy rates from the Department for Education; and
• drug and alcohol abuse rates from the NHS.

The model then takes these cohorts and asks for impact rates and deadweight calculations. Deadweight proportions (what would have happened anyway) were sourced by Inclusion, again through various sources, and a uniform percentage increase was applied to these deadweight calculations to produce impact rates.

The Manchester model takes the additional impacts above deadweight and applies them to fiscal, economic and social benefit gains in monetary terms – these are embedded in the model and have been collected by Manchester New Economy. They are based on national averages and collected from a variety of sources. (Some figures are based on academic papers from the past, which have then been uprated to present values using inflators.)

Set against the cost of the intervention, the model arrives at the BCRs described above. The model makes further adjustments to take into account optimistic bias. It makes additional calculations of monetary fiscal values from better health and reduction in crime (on top of those related to simple savings to the Exchequer through welfare benefit savings) from moving people into work.

The model is restrictive in that it does not allow for detailed breakdowns. If, for example, the intervention is specifically about reducing crime, the benefits gained from just dealing with young men engaged in a particular type of crime cannot be calculated. Rather it gives the user an overall saving for all groups, based on a national average rather than a rate for the local area.
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**Paul Bivand** is Associate Director of Analysis and Statistics at Inclusion. He has 30 years of experience in policy research in the employment and skills field.

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