Ending child poverty in a changing economy

Findings
Informing change

February 2009

Despite tough times ahead, there is still political consensus around the goal to end child poverty. Based on new projections taking account of the recession, the Joseph Rowntree Foundation has updated its assessment of what it will take to meet the government targets to halve child poverty by 2010 and eradicate it by 2020.

Key points

- Projections based on current policies suggest that child poverty will fall from 2.9 million to 2.3 million by 2010 – 600,000 short of the target.
- Two effects of the recession largely cancel each other out. Some children will enter poverty as their parents lose their jobs. Others, with low-paid parents, could move out of relative poverty, as Child Benefit and tax credits rise faster than average earnings.
- In a recession, planned welfare-to-work measures may not bring the previously projected large increase in the number of lone parents with jobs.
- In a recession, children are more likely to experience severe poverty, making it more costly per child to cut poverty.
- To meet its target for 2010, the Government would have to invest an estimated £4.2 billion a year in benefits and tax credits above its present plans. The allocation of an additional £2 billion since 2006 has been offset by an unexpected rise in child poverty between 2004 and 2007 and the increased costs of the recession.
- By 2020, without new policies to help low-income families, child poverty is projected to rise to 3.1 million.
- While the recession brings an increased short-term need for financial support, getting people back into sustainable jobs is central to the longer-term strategy. Policies need to take account of job quality and sustainability in order to provide a satisfactory solution to child poverty.

The research

By Donald Hirsch, Loughborough University, based on new research by the Institute of Fiscal Studies and the Institute for Economic and Social Research, University of Essex

Background

Over the past decade the Government has put a strong emphasis on its mission to wipe out child poverty in a generation, first announced in March 1999. The aim is to halve child poverty between the financial years 1998/9 and 2010/11 and to eradicate it in the following decade. While the vision of having no child poverty remains distant, the 2010 target is looming.

In 2006, the Joseph Rowntree Foundation (JRF), in partnership with the Institute for Fiscal Studies (IFS) and a range of leading experts, estimated that to reach the 2010 target would require a rise in tax credits costing about £4.3 billion a year, alongside the successful implementation of planned policies to raise the number of parents in employment (Hirsch 2006, *What will it take to end child poverty?*). Without extra resources, the study projected only a small reduction in child poverty by 2010 and a further small reduction by 2020, in each case achieving only a fraction of the fall required.

Since 2006, three important things have changed that make it desirable to reassess these projections:

- After six years of decline, the level of child poverty has started to rise again, showing a slight increase in the surveys published in 2007 and 2008.
- The Government has partially risen to the challenge of putting in more resources, announcing a total of around £2 billion in extra benefits and tax credits targeted at child poverty in the 2007 and 2008 Budgets, taking effect between 2008 and 2010.
- The recession that started in the second half of 2008 will change patterns of employment and earnings and affect economic projections.

New projections for 2010 and 2020 based on present policies

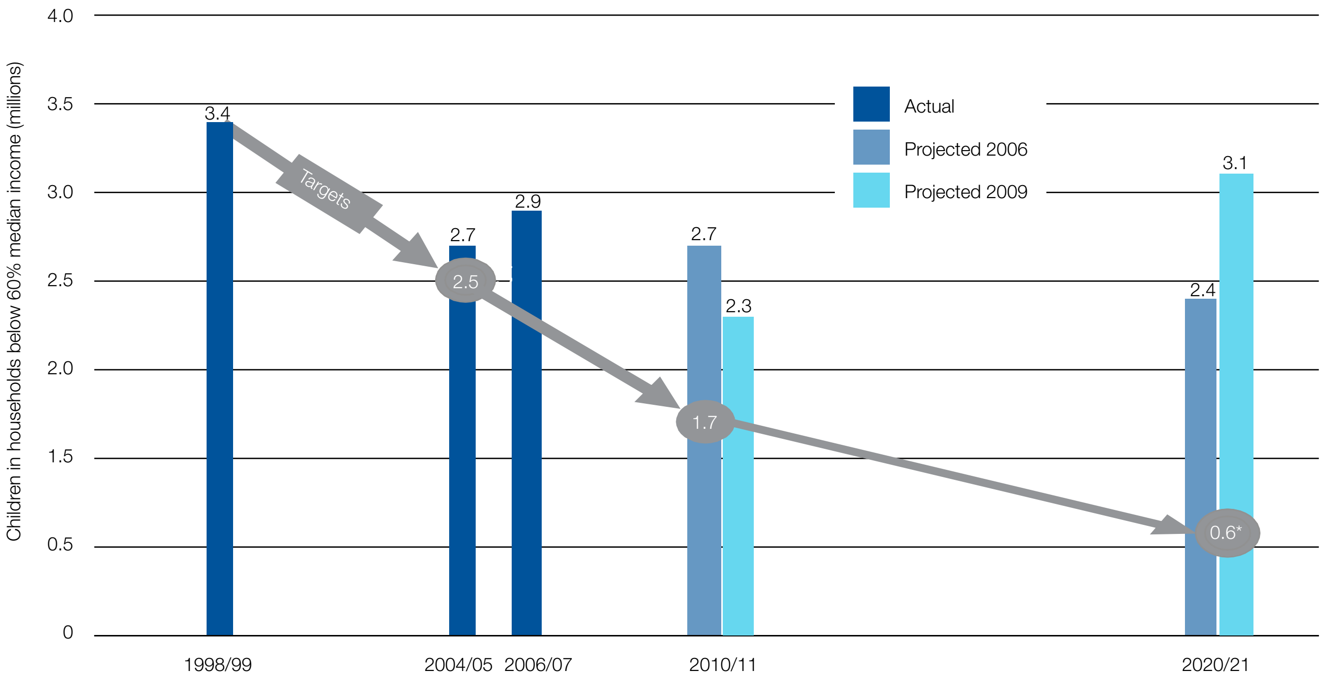
The Institute for Fiscal Studies, with the University of Essex, has produced revised projections of future levels of child poverty, based on reasonable assumptions about changes in employment, earnings and demography, along with the projected effects of announced policies for levels of benefits, tax credits and taxation. They give an indication of what any government's policies need still to achieve in order to meet stated targets. The projections draw on information about individuals and households collected in 2006/7, with assumptions about future trends in employment and earnings. The central projection assumes that:

- inflation-adjusted earnings will stay the same until 2010 and grow by 2 per cent a year thereafter;
- the recession will cause employment to be lower than previously forecast;
- the employment rate of lone parents will be the same in 2010 as it was in 2006 (previously it was projected to rise sharply). This is due to recession counteracting the effect of new welfare-to-work measures to get lone parents into work.

An alternative projection assumes a 'bad recession', under which earnings fall in real terms by 1 per cent to 2010 and the fall in employment is twice as high as in the central projection.

The central projection is for child poverty to fall from 2.9 million in 2006/7 to 2.3 million in 2010/11, which is half the fall required to meet the 2010 target of 1.7 million children in poverty. The fall is mainly attributable to the 2007 and 2008 Budgets, which were estimated to take 500,000 children out of poverty. Under a bad recession scenario, the projection is for a similar number of children to be in poverty, but with more of them in families without work.

Figure 1: Reduction in child poverty 1998–2021 – Targets and projections under present policies



* Note: It is not technically possible to achieve a zero poverty rate, since there are always some families with temporary dips in income. The target of 'eradication' by 2020 is here interpreted as a child poverty rate of 5%, the lowest ever recorded in any European country.

Figure 1 shows that, while the Government only narrowly missed its 2004 target of cutting child poverty by a quarter, present policies will not come close to cutting it by half in 2010. Since JRF's 2006 report, announcements of higher benefits and tax credits have reduced the projected 2010 shortfall, but not by the full half million children expected to escape poverty due to these measures, because of the offsetting effect of recent rises in child poverty.

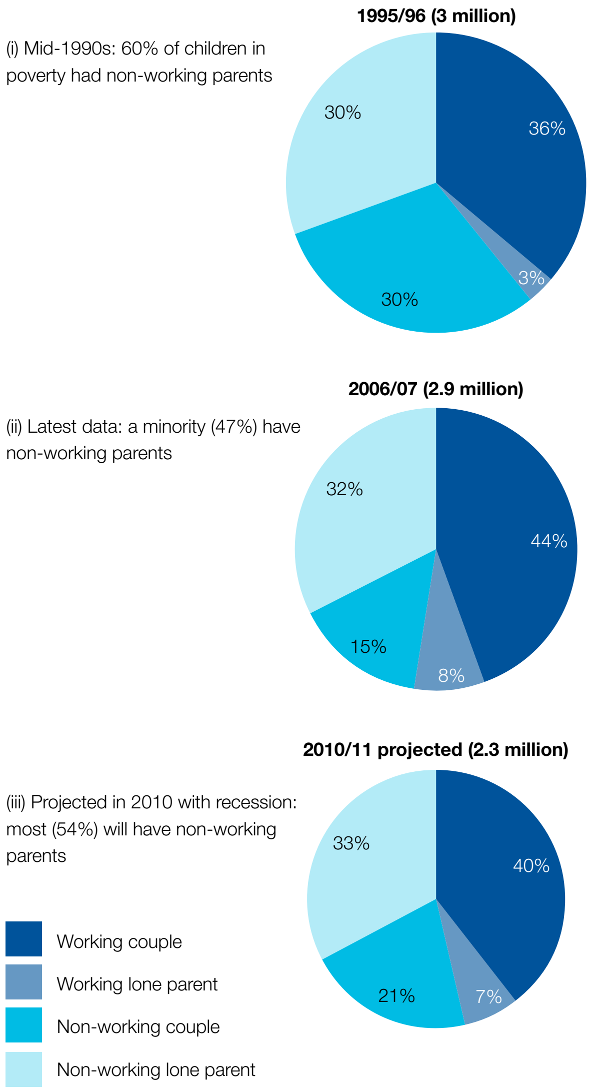
In 2020, the projection shows child poverty rising again to 3.1 million under the central assumptions, even though these include an increase in lone parent employment from 56 per cent to 70 per cent. This figure must be treated with caution, but it illustrates the potential fragility of the gains made in the current decade; many of those taken out of poverty by the latest measures will remain very close to the poverty line and may fall below it again. This is particularly likely if, when economic growth restarts, benefits and some tax credits continue to be uprated only in line with prices and not earnings, causing families on low incomes to fall behind.

The 2020 projection shows that, even with highly successful welfare-to-work policies, it would be possible for child poverty to rise rather than fall in the next decade, unless other measures are taken. New policies need to improve the generosity of benefits and tax credits and how they are uprated, and help provide good jobs for working parents that combine reasonable pay with flexibility. The Joseph Rowntree Foundation recently produced a series of reports showing a range of areas where bold measures will be required (see www.jrf.org.uk/publications/what-needed-end-child-poverty-2020).

What difference does a recession make?

There is no clearly predictable relationship between economic growth rates and relative poverty rates. Even though the worst off can often fall behind in a boom, prosperity creates resources that can be used for redistribution, as happened in 1998–2003. In a bust, families on low incomes can have mixed fortunes relative to others. Some become much worse off,

Figure 2: The changing face of child poverty



especially those who lose their jobs. Among those who stay in work, incomes compared with the median may not do badly if the average is stable or falling. In the past two recessions there has been no obvious trend in the level of child poverty.

Over the next two years, real earnings are likely to be flat or falling at every level. If this affects people on low earnings in the same way as people on average earnings, it will not in itself affect relative poverty. However, with benefits and tax credits today making up a much greater proportion of the incomes of low earning families than they did in the past, and with guarantees that these tax credits will either rise or maintain their value in real terms, it is more likely that working families on low incomes will see a rise in their incomes relative to the median income during a recession. At the same time, if the number of out-of-work households with children increases as a result of lower employment rates, this is likely to add to the child poverty total.

Modelling these effects of recession, the IFS research shows that they roughly cancel each other out, and suggests that the projected child poverty rate will not be strongly affected by the severity of the recession. However, while recession may not much affect headline child poverty figures, it will mean that a higher proportion of children in poverty will be in families that do not work.

Changing balance between in-work and out-of-work poverty

Over the last decade, the number of children with parents with ‘in-work poverty’ has grown as a proportion of all children in poverty. In 1995/6, the proportion of children in poverty whose families were out of work reached a high of 60 per cent. Yet the latest poverty figures show that the majority of children in poverty now have working parents. Over this period, the risk of out-of-work poverty for children with two parents halved.

The current projections show a partial reversal of this by 2010, with 54 per cent of children in poverty being in non-working families (see Figure 2). In the context of an overall projected fall in the number of children in poverty, due to rises in benefits and tax credits, the number of children in poverty with working parents is projected to fall by 20–30 per cent between 2006/7 and 2010/11. However, the number in poverty without working parents is projected to fall by only 5 to 10 per cent.

The projections show a particularly sharp fall in poverty rates among children in families where one parent works full-time and the other does not work. One in five such families were in poverty in 2006/7, but by 2010 this risk is projected to fall to 11 per cent. A substantial number of couples depending on a single low wage are projected to become relatively better off because their child benefit and tax credits are rising while the recession hits other people's incomes.

In this picture, the 'losers' are likely to be affected more strongly than those who gain. Those children who enter poverty in the next year or two because their parents lose their jobs may fall into severe poverty. On the other hand, those children who stop being in relative poverty, as the median income falls, may not feel that their circumstances have changed much. This is confirmed by a separate projection of the level of deprivation, measured by looking at how many children in low-income families lack basic necessities. Following the increases in tax credits announced in 2007 and 2008, the number of children deprived of necessities is projected to fall by only about a third as much as the number of children in families below the income poverty line.

Overall it is possible that recession will bring a net increase in children's hardship even though it does not raise the child poverty total. This is likely to raise the cost of tackling child poverty, since it is more expensive to lift children out of severe poverty.

Can redistribution still achieve the 2010 target?

In order for child poverty to be half as much in 2010/11 as it was in 1998/9, a further 600,000 children would need to be lifted out of poverty. This is a similar amount to the number that the Treasury estimates that it has already taken out of poverty by increases in tax credits and benefits announced in 2007 and 2008, which cost about £2 billion. In principle, any further measures introduced in April 2010 could repeat this by raising tax credits and/or benefits further.

In practice, these calculations show that to do so will cost a lot more than a further £2 billion a year. They suggest that to get 600,000 children out of poverty in 2010 would cost £4.2 billion a year. This would raise the child element of the child tax credit by £12.50 a week more than planned.

The estimated cost of taking a child out of poverty has risen since the 2006 projections, from £4,300 to £6,900. Part of this is due to inflation, as prices are about 7 per cent higher now than in mid-2006. Also, a technical change to improve the accuracy of these calculations has had the effect of raising the projected cost of meeting the target.

Some real changes are also making it more expensive per child to reach the targets. In particular, a detailed profile of family incomes shows that there are now projected to be far fewer children in families slightly below the poverty line than previously forecast – many more will find themselves deeper in poverty as a result of increased unemployment in a recession. This means that fewer could escape poverty with just a small boost in income. Moving parents back into jobs, to raise them closer to or above the poverty line, will need to play a major part in combating child poverty in the medium term. In the short term, extra public resources will be needed to cover the cost of reducing child poverty to the planned level, during the downturn.

Conclusion and policy implications

These projections show that under existing policies, about 1.1 million fewer children will be in poverty in 2010 than in 1998. However, this will fall 600,000 short of the goal to halve child poverty. Achieving only two-thirds of the targeted reduction for 2010 will make it difficult to meet the more ambitious goals for 2020.

The recession will not greatly affect child poverty numbers, but it will worsen the profile of child poverty. Proportionately fewer of the children in poverty will have parents in work, and more will be in severe poverty, meaning that both the level of hardship experienced and the cost of reducing child poverty will be greater.

If these greater levels of hardship are allowed to take root, the knock-on costs of child poverty experienced during the recession could be serious and long-lasting. Previous JRF research on the cost of child poverty suggested that over the long term, child poverty is costing at least £25 billion a year in extra spending, lost taxes and lost GDP. If during the recession the Government were to cut back spending on child poverty, evidence shows that this would continue to affect these children's prospects throughout their lives, and the consequences would be costly for society as a whole.

While this suggests a case for increased spending to alleviate child poverty directly during the downturn, it also underlines the importance of developing more fundamental solutions over a longer period. As the economy recovers, getting parents into jobs will be particularly important. However, as JRF's recent analysis has shown, a wider focus than reducing 'worklessness' is needed, to include:

- developing parents' skills and enabling them to get jobs that can be combined with family life;
- providing truly affordable childcare that meets children's and parents' needs; and
- ensuring that benefit levels provide a solid foundation for families seeking to improve their lives.

Earnings, job quality and sustainability also need to improve. Success in reducing worklessness in the last decade did not necessarily lift families out of poverty.

The challenge in a difficult recession will be to continue implementing such long-term improvements in order to build upon progress already made in reducing child poverty.

About the project

This research to update and revise child poverty projections was undertaken by the Institute for Fiscal Studies (IFS), together with Professor Holly Sutherland of the University of Essex. It repeated the modelling exercise carried out by the JRF and IFS in 2006, using the most recent data available.

For further information

The full report, **Micro-simulating child poverty in 2010 and 2020**, by M. Brewer, J. Browne, R. Joyce and H. Sutherland, is published by the Institute for Fiscal Studies. It is available as a free PDF at www.ifs.org.uk/comms/comm108.pdf

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