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The economics of Universal Credit

Introduction

Universal Credit (UC) is the most ambitious welfare reform policy since the formation of the welfare state. In January 2006, a green paper by the Department for Work and Pensions (DWP) suggested a 'single system of benefits for all people of working age' would have the advantages of simplifying redistributive welfare payments to better meet the needs of people in work, and provide a comprehensive safety net for those out of work. UC strategies seek to create incentives to encourage employment activity, and financial independence.

The mechanics, logistics, advantages and challenges were widely considered before the programme was formally rolled out in 2010, the start of what has now been a decade of austerity. Despite cross-party and inter-agency engagement, collaboration and support – all of which underpin Government's commitment to social welfare – rolling out UC and systematising its implementation have been marred by operational issues, institutional setbacks, and a general sense of mistrust by claimants fearing being left without dependable means of support.

The source of the systemic imbalance UV tries to redress, with respect to poverty, socio-economic inequality, stable employment, and other factors which would, in fact, encourage financial independence, cannot be isolated from the wider, and more complex economic contradictions in which the UC is situated. Therefore, it is not yet possible to qualify the success, or failure, of UC using purely economic data, growth differentials or labour market statistics. Some of these data sets are robust, from an economic growth perspective, yet disguise staggering levels of income inequity and poverty that plague a measurable demographic, especially the elderly, and especially children. Whilst it would be short-sighted to qualify UC as a failure, it does bear noting that its ultimate success would be signalled in the sustained levelling-up of individuals and households that are on, or fall below, the poverty line.

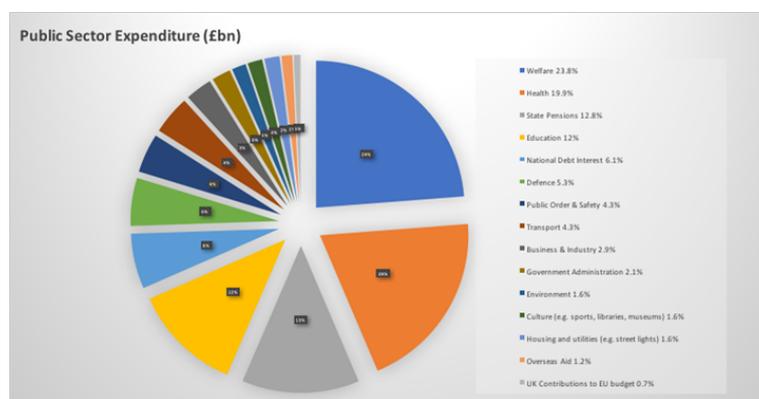
- I. Were the original objectives and assumptions the right ones? How should they change?

At the most fundamental level, UC's bold and radical *raison d'être* belies the true complexity of the systems it seeks to replace. UC came about as a functional, and largely technocratic, concern for the management of benefits and tax

credits, that would deliver income support promptly and reliably. Simplification, however, does not account for the contingencies of why people claim benefits.

With significant cuts in public sector spending over the period UC has been semi-operational, it is all too tempting to overlook Government's commitment to redistributive efforts, which amount to 40% of GDP. In 2019, £850 billion was allocated to public services, social security payments and capital investments. Yet, this level of investment runs counterfactual to the realities that see low-income households budgeting 'pennies' and earmarking irregular income streams to offset the cost of living.

Public Expenditure Statistical Analyses (PESA) for 2018¹



The biggest driver of poverty is not a lack of material possessions². It is the inability to cultivate human capital and strengthen systems of social provisioning and social cohesion which develop the resilience of societies to cope in times of stress³. Lack of inclusive economic participation, limited scopes for livelihoods, job insecurity and low wages result in poverty. Consider other intangible goods which may help lift an individual out of poverty: education, and access to health, care and information all enable resilience with which to weather periods of economic volatility, market failures and political uncertainty. From this perspective, UC is only a normative element of policy reform and not yet an effective mechanism for social welfare or economic justice.

¹ HM Treasury (2019). *Public Expenditure: Statistical Analyses 2019*. (24 January 2019) <https://www.gov.uk/government/publications/how-public-spending-was-calculated-in-your-tax-summary/how-public-spending-was-calculated-in-your-tax-summary>

² Greenhill, R., Carter, P., Hoy, C., & Manuel, M. (2015). *Financing the future: How international public finance should fund a global social compact to eradicate poverty*. (London: ODI).

³ Abhijit V. Banerjee and Esther Duflo (2019). *Good Economics for Hard Times: Better Answers to our Biggest Problems* (London: Allen Lane)

The demand for public policy, that is sensitive to these intersectional dynamics, is, unfortunately never optimal. There are several reasons for this, but foremost is that Government policy is rarely set out as 'a clear strategy for what they want the system to achieve'⁴ thus forestalling public scrutiny – or evaluation – into the fairness, or viability of the proposed programme.

Reversing nearly 10 years of austerity in a climate of economic uncertainty marked by low wages, rising rents and cost of living and significant cuts to social security, the long-term view is that a reduction for income inequality depends on the ability of Government to raise public monies with which to fund public services, in conjunction with the benefits system. To separate one from the other would potentially distort policy outcomes because individuals, households, communities and businesses are exposed to economic and political changes at different stages over the time they contribute to, and benefit, from the system.

Simply put, without money to support UC, in terms of resources, technical expertise and case handling, and without an understanding of the dynamics of poverty within this ostensibly prosperous economy, it is difficult to set the system on the path of its original purpose.

The new year has already witnessed delays to the full roll-out of UC, with much of the current evidence as published by the Institute for Fiscal Studies⁵ and the Institute for Government⁶, contextualising the business case summaries published by the Department for Work and Pensions since 2018⁷, to better reflect the complexity and scope of the socio-economic, cultural and psychological consequences of such a large-scale welfare reform on individuals and households⁸.

II. What have been the positive and negative economic effects of Universal Credit?

UC introduced features that differed from previous benefit schemes: fully digitised service, largely unavailable to households without Internet data or computer access; paying monthly, in arrears, rather than prospectively, a feature which impacts directly on the saving and budgeting strategies of claimants, who are paid either weekly, or fortnightly, or on those with precarious job situations; increased conditionality; and reduced amounts paid to some

⁴ Gemma Tetlow and Joe Marshall (2019). Taxing Times: The need to reform the UK tax system', Institute for Government

⁵ Mike Brewer, Robert Joyce, Tom Waters and Joseph Woods (2019). 'Universal credit and its impact on household incomes: the long and the short of it', *Institute for Fiscal Studies*, April.

⁶ Nicholas Timmins, (2016). 'Universal Credit: from disaster to recovery', *Institute for Government*. September.

⁷ 2018 is a significant year as Universal Credit was introduced, nation-wide for all unemployed people. At the end of 2018, 1.6 million people were on UC..As an example, see: Department for Work and Pensions, (2018). 'Universal Credit Programme Full Business Case Summary', June.

⁸ Sophie Wickham, Lee Bentley, Tanith Rose, Margaret Whitehead, David Taylor-Robinson, Ben Barr (2020). 'Effects on mental health of a UK welfare reform, Universal Credit: a longitudinal controlled study', *Lancet Public Health* 2020; 5: e157–64.

claimant groups, the logic and logistics of which have proven to be cumbersome to untangle⁹.

The cultural shift introduced by UC contrasted hugely with rules that in almost all cases dis-incentivised working below a certain amount of hours weekly. Under UC, in theory, any amount of work would pay as long as the claimant had an 'interest' in doing more work or earning more. This flawed assumption is behind the introduction of the claimant commitment, which requires an individual to spend up to 35 hours a week looking for work, or face more stringent sanctions.

This conditionality fails to take into account the various factors that keep people formally unemployed in the first place, such as care duties and work in the home. The role of the state is fundamentally recast: the state and the taxpayer now have an interest in requiring those in less than full-time employment to do more work, or earn more, in order to manage the overall burden of benefits and reform on the public purse, not simply to establish a more equitable system of income redistribution.¹⁰ *In-work conditionality* assumes people have choices: in working more hours; in job opportunities; for employment security; or in earning higher wages. Situations where claimants who lose out on benefits if they are judged to be earning less than they could, or are seen to be making less than a 'reasonable effort' to work, are one of the most intractable paradoxes of UC.

UC is meant to encourage independence through higher earnings and less reliance on benefits, but this conditionality is dependent upon the health of the labour market – which incidentally ignores the value of care work to the economy¹¹ – and qualifies human activity hierarchically, on the basis of value and productivity, without the full weight of how biases bear upon auxiliary assumptions and their applications in policy prescriptions. It is also dependent upon the provision, quality and sustainability of public goods, such as health, education, transport, police, early years education and provision for elderly care. UC, by and large, has bred mistrust in the state system¹², in large part due to a critical blindness to the complexity of living in favour of transactional simplicity.

One of UC's greatest strengths is its apolitical ideology (narrow assumptions notwithstanding) at the level of principle, and the cross-party effort dedicated to

⁹ Monique Rotik and Luke Perry (2011). 'Perceptions of welfare reform and Universal Credit', Department for Work and Pensions, Research Report 778.

¹⁰ For further information see:

Wright S, Dwyer P, Jones K, Mcneill J, Scullion L, Stewart (2018). 'Welfare conditionality, sanctions, support, and behaviour change'. Final findings: Universal Credit', *Economic and Social Research Council*

Fletcher, D. R. and Wright, S. (2020) 'Special Issue: International perspectives on the theories and practices of welfare conditionality', in *Social Policy & Administration*, 54(2): 185-326.

¹¹ The estimated value of unpaid care to the UK economy stands at £411 billion. Office for National Statistics (2018) Household Satellite Account, UK: 2015-2016.

¹² 'Universal Credit: Inside the Welfare State', BBC, February 2020.

its implementation. Conversely, its greatest weakness is being removed from the economic reality of its target demographic, and the human cost to living through a protracted period of fiscal retrenchment.

III. What effect has fiscal retrenchment had on the ability of Universal Credit to successfully deliver its objectives?

'Official denials notwithstanding, it is obvious to anyone who opens their eyes'

Philip Alston, May 2019

The UN Special Rapporteur on Poverty Report on the United Kingdom

The report provides evidence of:

- ✚ Despite economic prosperity, one fifth of its population (14 million people) live in poverty. Four million of those are more than 50 % below the poverty line and 1.5 million experienced destitution in 2017, unable to afford basic essentials.
 - ✚ Following drastic changes in government economic policy beginning in 2010, the two preceding decades of progress in tackling child and pensioner poverty have begun to unravel and poverty is again on the rise.
 - ✚ The number of people in in-work poverty who are working is 3.8 million, or more than 25% of all the people living in poverty, that is 1 in 8 workers overall
 - ✚ And over the last 10 years, the number of workers in poverty has grown by a million - up by a third.
 - ✚ The remainder of people in in-work poverty are 2.6 million children and one million non-working adults, nearly three quarters of them are women.
 - ✚ Of these 1 million non-working adults, 91% live with dependents
 - ✚ Relative child poverty rates are expected to increase, to reach close to 40%
- Sharp increases in the number of food banks, homelessness and rough sleeping
 - For certain groups, life expectancy has fallen
 - A 'decimation' of the legal aid system
 - Alienation of low-income persons from the justice system
 - Denial of benefits to persons with disabilities, or of being pushed into unsuitable work
 - Lack of organised care for persons with mental illnesses
 - Policing services are down to 'skeletal proportions'
 - A shrinking of community, youth and refuge centres
 - Single-parent households, especially single mothers, 'struggling to cope in very difficult circumstances'

'For almost one in every two children to be poor in twenty-first century Britain would not just be a disgrace, but a social calamity and an economic disaster rolled into one'

Austerity measures have decimated public services, which has led to increased levels of poverty¹³. Yet, Gross Domestic Product per capita in 2019 rose by 6.5% to US\$42,580, making the UK the fifth largest economy in the world in terms of GDP¹⁴. The unemployment rate is the lowest in 40 years, and there are 3.3

¹³ The devastating consequences of austerity were laid bare in a 2019 report by the United Nations Special Rapporteur on Poverty. It says poverty in the UK is the result of ideological and political choices. The social safety nets have been 'deliberately removed and replaced with a harsh and uncaring ethos', Philip Alston UN Special Rapporteur on Poverty, May 2019
Human Rights Council Forty-first session
24 June–12 July 2019 Agenda item 3
Promotion and protection of all human rights, civil, political, economic, social and cultural rights, including the right to development
Visit to the United Kingdom of Great Britain and Northern Ireland
Report of the Special Rapporteur on extreme poverty and human rights, April 2019
[<https://undocs.org/A/HRC/41/39/Add.1>]

million more people in work than in 2010. This is partly due to growth in the workforce over time, and only because 2010 represented a low point following the global recession¹⁵.

IV. How has the world of work changed since the introduction of Universal Credit?

The table below shows the quarterly rate of growth in employment from 2014.¹⁶ At the start of 2014, only 5,000 cases are on UC. The original target had been set to 1 million claimants.



It is to be noted, 79% of the jobs that have been created since 2010 are full-time, and hence out of reach of full-time carers, in the absence of Government-funded provisions for early-years childcare, or elderly care. Full-time employment, however, is no guarantee against in-work poverty, which is a major and growing problem in this country. In fact, in-work poverty¹⁷ rates outstripped the growth in employment in 2018. Real regular pay and real total

¹⁴ Listed in US\$ as per Financial Times, *Country Economy: United Kingdom* <https://countryeconomy.com/gdp/uk>, as better indication of relative GDP in light of the currency fluctuations of 2018-2019.

¹⁵ Indeed, United Kingdom employment statistics mirror those experienced in recent years in many OECD countries

¹⁶ Office for National Statistics (2019). *Labour market economic commentary: Additional economic analysis of the latest UK labour market headline statistics and long-term trends for December 2019*

¹⁷ With poverty measured using household income, either all the people in a household are in poverty or none are. Extending this logic, all a household's members are in in-work poverty if the household is in poverty and at least one of its members is in paid work. On the latest numbers for 2014/15, 7.4 million people in the UK are in in-work poverty, which at 55 per cent of all those in poverty is a new record- 500,000 British workers have been swept into working poverty over the past five years- the number of people with a job but living below the breadline has risen faster than employment

pay registered at 0.2% lower than the downturn peak reached in February-April 2008 during the financial crisis. It is also evident that robust economic figures do not reflect reality¹⁸.

V. Does Universal Credit's design adequately reflect the reality of low-paid work?

In the world of work, high participation tax rates, and marginal tax rates for those in low-paid work are disincentives to start work in the first place. This is compounded by uncertainty in the workplace, care duties and work within the home.

Job Losses as Reported in the Press

February 2020

Lloyds, Virgin Money and Direct Line to cut 2,000 jobs 26 Feb 2020

Ted Baker to cut 160 roles after 'very challenging year' 26 Feb 2020

HSBC to close 27 more branches across UK this year 25 Feb 2020

HSBC to cut 35,000 jobs worldwide as profits plunge 18 Feb 2020

Beales to close 12 of its 23 department stores 7 Feb 2020

New John Lewis boss warns staff of store closures and job losses 6 Feb 2020

January 2020

BBC announces 450 jobs will go in newsroom shake-up 29 Jan 2020

Ryanair warns it could shut bases and cut jobs after 737 Max delays 28 Jan 2020

British Steel buyer will cut up to 500 jobs if takeover goes ahead 24 Jan 2020

Morrisons to cut 3,000 managers and take on more shop-floor staff 23 Jan 2020

Can the UK regional airline Flybe fly out of its troubles? 14 Jan 2020

High street crisis deepens as 3,150 staff lose jobs in a week 7 Jan 2020

August 2019

Morrisons shuts four supermarkets, putting 400 jobs at risk 22 Aug 2019

UK government agrees £300m rescue package for British Steel 9 Aug 2019

Sound of silence: will shipyard that built Titanic vanish into history? 9 Aug 2019

British Steel: Turkish pension fund likely to be preferred bidder 8 Aug 2019

Boohoo moves for Karen Millen and Coast but 1,100 jobs at risk 6 Aug 2019

Harland and Wolff expected to go into administration 5 Aug 2019

HSBC boss John Flint resigns 'by mutual agreement' 5 Aug 2019

July 2019

Ryanair says 900 jobs at risk because of 'excess pilots and cabin crew' 31 Jul 2019

Centrica boss to step down as energy firm posts first-half losses 30 Jul 2019

Nissan to axe 12,500 jobs worldwide but Sunderland appears safe 25 Jul 2019

Deutsche Bank posts worst quarterly loss in four years 24 Jul 2019

Waitrose to axe seven more stores putting 700 jobs at risk 18 Jul 2019

British Steel receiver warns sale will take time 5 Jul 2019

A quarter of UK betting shops could close, with 12,000 jobs at risk 4 Jul 2019

¹⁸ Pascale Bourquin, Agnes Norris Keiller and Tom Waters (2019). *The distributional impact of personal tax and benefit reforms, 2010 to 2019*, Institute for Fiscal Studies

December 2019

Jamie Oliver's Fifteen Cornwall closes with the loss of 100 jobs 12 Dec 2019
Brexit hits UK ski and holiday staff overseas 11 Dec 2019
Jessops jobs and stores in jeopardy after administrators called in 6 Dec 2019

November 2019

Mothercare to cease all UK trading with loss of 2,800 jobs 5 Nov 2019
Chinese giant Jingye is leading contender for British Steel buyout 3 Nov 2019

October 2019

Brexit watch Brexit uncertainty drives up job losses and holds back economy 25 Oct 2019
Thomas Cook: MPs to question PwC on possible conflict of interest 20 Oct 2019
Scottish department store Watt Brothers goes into administration 18 Oct 2019
UK's robust jobs market dented amid big fall in employment 15 Oct 2019
'Kindness can't pay the bills': what now for ex-Thomas Cook staff? 11 Oct 2019
UK edges towards recession as service sector sinks 3 Oct 2019
Waitrose boss Rob Collins steps down in £100m John Lewis cuts 1 Oct 2019

September 2019

Wrightbus in last-minute search for buyer to avoid collapse 22 Sep 2019
British American Tobacco cuts 2,300 jobs in shift towards vaping 12 Sep 2019

June 2019

Network Rail bids for parts of British Steel 30 Jun 2019
Ford to cut 12,000 jobs in Europe amid struggling car market 27 Jun 2019
Ted Baker warns on profits amid 'extremely difficult' conditions 11 Jun 2019
The Sun faces major job cuts as publisher seeks to slash costs 7 Jun 2019
'Body blow for area': Bridgend devastated by Ford factory closure 6 Jun 2019
Ford to close Bridgend factory by September 2020 6 Jun 2019
Aviva to axe 1,800 jobs as insurer cuts costs 6 Jun 2019

May 2019

Today in Focus What happens to a place when its steel industry collapses? 29 May 2019
CNN preparing to make cuts at London-based news operation 28 May 2019
The Society interview Andy Haldane: 'We have allowed the voluntary sector to wither' 22 May 2019
Ford to cut 7,000 jobs including more than 500 in UK 20 May 2019
Honda says it will close Swindon plant in 2021, ending workers' hopes 13 May 2019
TSB expected to cut at least 100 jobs at head office 9 May 2019
Bombardier puts Belfast wing-making plant up for sale 2 May 2019

Employment figures ought to be further qualified by the massive lay-offs across key industries, and by the closure of long-standing institutions that have, historically, provided some measure of job security. The prevalence of zero-contract hours, flexi-working and occasional employment which increasingly characterise the working lives of those struggling to make ends meet, are not safeguards against poverty.

Conclusion

Support for such large-scale welfare reform cannot be given reluctantly or half-heartedly, nor can it be subjected to political manoeuvring, or indiscriminate criticism. It requires concerted effort from all those involved in order to keep UC thriving and true to purpose. It also requires funding, and lack of public monies, despite Government commitment to social welfare, is the thorniest structural hurdle to the full implementation of UC.

Since 2010, and running parallel to austerity measures, the tax system in the United Kingdom has been undergoing piecemeal reform shifts with various degrees of success¹⁹, and a lot of distortion. Government's social welfare plans do not, currently, include a rise in the tax margin, or new taxes. While there is historical, and world-wide evidence to support the claim that high taxes do not discourage work, or initiative, or hinder economic growth²⁰, there is also evidence to suggest an increase in tax is unlikely to mean more money for Government to redistribute²¹.

Economists, for example, consider the progressivity of the tax and benefits system and judge policy on the basis of redistribution. Government finds itself in a predicament. One of the most pressing concerns are the moderate levels of intake of tax compared to rising public spending pressures. However, without raising taxes or increasing levels of borrowing, already at 80.6% of GDP²², the provision of public services will be further curtailed, and the success of UC could be jeopardised.

29 February 2020

¹⁹ IBID

²⁰Abhijit V. Banerjee and Esther Duflo (2019). *Good Economics for Hard Times: Better Answers to our Biggest Problems* (London: Allen Lane)

²¹ Jill Rutter, Bill Dodwell, Paul Johnson, George Crozier, John Cullinane, Alice Lilly and Euan McCarthy (2017). 'Better Budgets: Making Tax Policy Better', Institute for Government, Institute for Fiscal Studies and The Chartered Institute of Taxation, January.

²² Office for National Statistics, November 2019.