

Chapter One



Stagnation nation

Chapter summary

- The UK economy has huge strengths, from high employment to world class universities.

- But, having grown more quickly than most advanced economies from the 1990s to the mid-2000s, the UK has been in relative decline ever since: the average productivity gap with France, Germany and the US nearly doubled, to 16 per cent, between 2008 and 2019.

- Slow growth is the cause of Britain's flatlining wages: real wages grew by an average of 33 per cent a decade from 1970 to 2007, but this fell to below zero in the 2010s. By 2018 typical household incomes were 16 per cent lower in the UK than in Germany and 9 per cent lower than in France, having been higher in 2007.

- Having surged during the 1980s, and remained consistently high ever since, income inequality in the UK was higher than any other large European country in 2018. Inequality between places is high and persistent too.

- This is stagnation: the toxic combination of low growth and high inequality. It is ruinous for low-to-middle income Britons. Low-income households in the UK are 22 per cent poorer than their counterparts in France, meaning their living standards are £3,800 a year lower than their French equivalents'.

- The young have also lost out: 8 million younger workers have never worked in an economy with sustained average wage rises, and those born in the early 1980s were almost half as likely to own a home as those born in the early 1950s at age 30.

- Stagnation leaves public services struggling, even as the tax burden rises: taxes are on course to reach their highest share of GDP since the 1940s.

The country wrestling with today's cost of living crisis, like the people, places, and firms experiencing it, has a history. Understanding where that has left the UK is the purpose of this chapter. Alongside many strengths, it argues that the Britain of the 2020s risks being defined by the combination of sustained low growth and longer-lasting high inequality. Each brings challenges, but a prolonged period of the two together risks continued stagnation, which should be the priority of policy makers to reverse.

Britain has many advantages and its economy has many strengths

The UK is a privileged and prosperous country in a global context. Having been one of the world's richest countries for several centuries, our national incomes now average 6 per cent above the typical Organisation for Economic Co-operation and Development (OECD) country and our employment rate is high. Setting up a company is easy in the UK, and the adoption of technology among the population is generally swift.

The UK also has many strengths. It is a world leader in service exports,¹ with world-class universities and a research system to match.² Furthermore, a preoccupation with financial services can obscure wider, and faster-growing, sectors such as gaming and TV production. The UK is highly innovative in some important growth areas, with the value of the life sciences and pharmaceuticals sectors being demonstrated once again during the pandemic. It also has a degree of soft power derived from the cultural and educational exports that the widely-used English language supports.³

In uncertain geopolitical times, the UK's membership of NATO and its geographic location on offshore European islands afford a relatively high degree of security. Our geography may be insular, but it is not remote: our location and time zone afford a high degree of integration with the dense North Atlantic systems of trade, travel, and security, compared, for example, to Australia or New Zealand. In the context of both climate change and the steps necessary to limit it, the UK is less vulnerable than many other countries to the

1 J De Lyon et al., [Enduring strengths: Analysing the UK's current and potential economic strengths, and what they mean for its economic strategy, at the start of the decisive decade](#), Resolution Foundation, April 2022.

2 Department for Business, Energy & Industrial Strategy, [International comparison of the UK Research Base, 2019: Accompanying note](#), July 2019.

3 British Council, [Global Perceptions Survey 2021](#), December 2021.

effects of global warming⁴ and has relatively high meteorological potential to generate renewable electricity.⁵

But we are in a period of relative decline

Recognition of the UK's enduring, relatively privileged position should not prevent an honest assessment of where we find ourselves today, as we are well into a period of relative decline. The OECD forecasts that the UK economy will not grow at all in 2023: a worse performance than any G20 country bar Russia.⁶

While predictions of such significant future underperformance are uncertain, our recent experience of it is painfully concrete. Yes, Britain is a secure member of the family of high-income nations, but it is a long way from the top of this group and the gap has been widening. To use a football analogy, we are not yet in danger of relegation from the top division, but we are increasingly a long way from qualifying for the Champions League.

It is reasonable, albeit ambitious, to compare productivity in the UK with the US – the most productive large country in the world – along with the most productive large European economies (France and Germany). On this measure (see Figure 3) the broad picture has been of the UK converging from about two-thirds of US productivity towards about 80 per cent since 1970. The UK also made up ground with France and Germany from the early 1990s, after these countries had converged closer to US productivity levels earlier in the second half of the 20th century. But that phase of UK catch up came to an end in the mid-2000s and the UK's relative performance has been declining ever since.

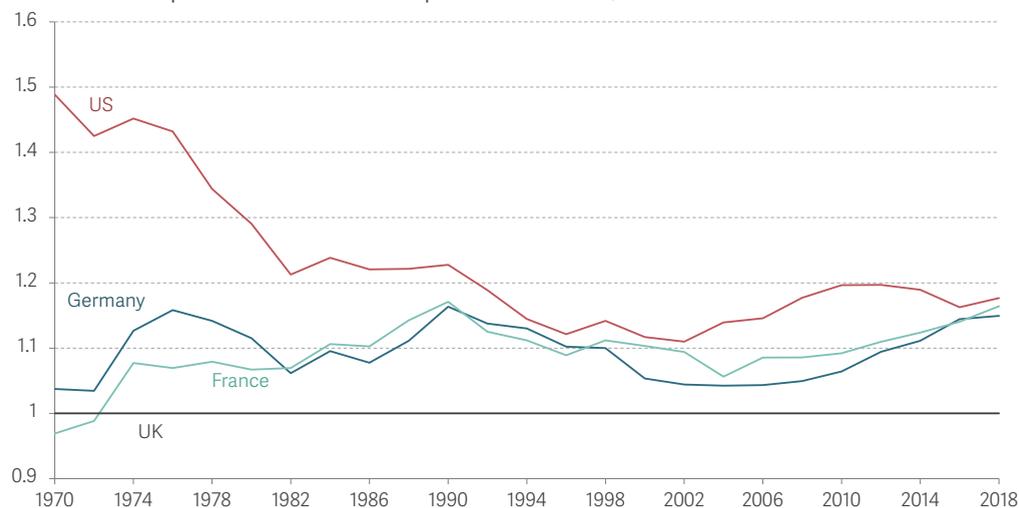
4 www.gain.nd.edu/our-work/country-index, accessed 14 June 2022; D Eckstein, V Künzel & L Schäfer, [Global Climate Risk Index 2021: Who suffers most from extreme weather events? Weather-related loss events in 2019 and 2000-2019](#), Germanwatch, January 2021.

5 Department for Business, Energy & Industrial Strategy, [Energy white paper: Powering our net zero future](#), December 2020.

6 OECD, [Economic Outlook](#), June 2022.

Figure 3: UK productivity has fallen further behind France, Germany, and the US since the early 2000s

Ratio of GDP per hour worked compared to the UK, current PPP



Notes: Data shown is two-year rolling averages. Purchasing power parity (PPP) is used to compare labour productivity between countries. PPP is a theoretical exchange rate in which you can buy the same amount of goods and services in every country. These data are current PPP rather than constant prices measured in a base year. Current PPP is the correct measure when comparing relative levels. See Feenstra, R et al., *The Next Generation of the Penn World Table*, *American Economic Review*, 105(10), 3150-3182, 2015.

Source: Analysis of OECD, Level of GDP per capita and productivity dataset.

While productivity growth slowed in most countries around or after the crisis, the UK's slowdown was exceptionally severe. In the 12 years following the crisis, labour productivity grew by only 0.4 per cent per year in the UK, compared to an average of 0.9 per cent among the 25 richest OECD countries (there are a number of different ways in which economic progress can be compared across countries over time, as Box 1 explores). As a result the UK's productivity gap with France, Germany and the US has widened by an average of 7 percentage points since 2008 to stand at 16 per cent in 2019. The gap relative to France and Germany has almost tripled from 6 to 16 per cent – this further decline being equivalent to an extra £3,700 in output per person.

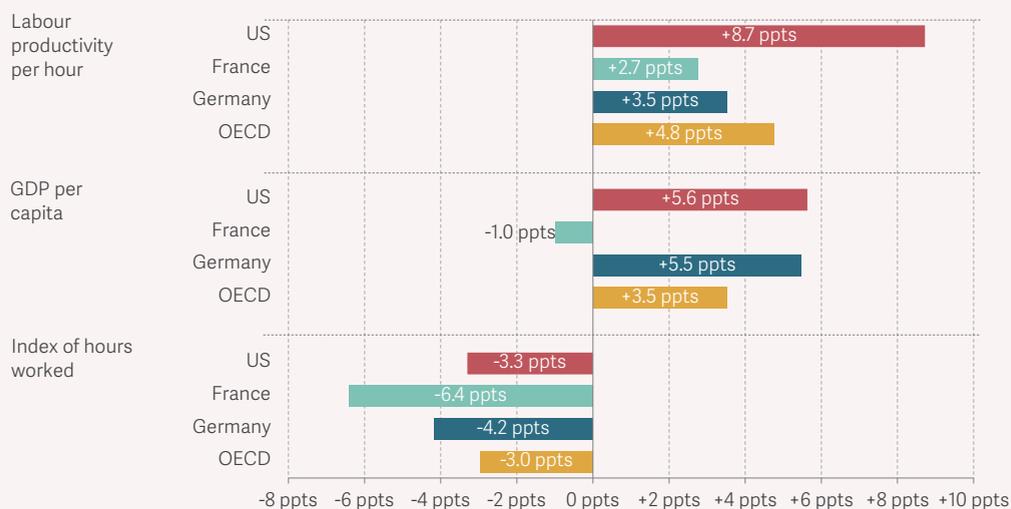
Box 1: Comparing the drivers of living standards across countries and over time

How the UK has fared relative to some key comparator countries across aggregate measures of economic performance since 2007 is set out in Figure 4. The first segment shows the extent of the UK's underperformance in labour productivity per hour (i.e. the same measure shown in Figure 3), with the gap between the UK and other countries increasing significantly in all cases. Productivity combines

with employment levels and the average numbers of hours worked in determining GDP per capita, relative changes in which are shown in the second segment of Figure 4. Here the extent of that underperformance is larger relative to Germany. On the eve of the financial crisis, GDP per capita in the UK was just 6 per cent lower than in Germany, but this gap had risen to 11 per cent by 2019.

Figure 4: The UK's relative decline since the financial crisis needs to be considered across a range of metrics

Change in the gap in labour productivity per hour and GDP per capita, and the relative change in hours worked, between the UK and selected advanced economies: 2007 to 2019



Notes: Total hours are expressed as an index = 100 in 2006. Ppts are percentage point changes. Labour productivity is measured at constant 2015 PPPs. This is the correct measure to use when analysing relative growth rates, rather than relative levels. R et al., The Next Generation of the Penn World Table, American Economic Review, 105(10), 3150-3182, 2015.

Source: Analysis of OECD, Level of GDP per capita and productivity dataset.

This difference reflects a larger rise in the total number of hours worked in the UK, which past research links to households supplying more labour to protect their incomes in the face of the deep productivity and wage stagnation in the UK.⁷ Since the financial crisis, hours worked have increased by 11.3 per cent in the UK, more than two-and-a-half times the rise in France (4.3 per cent) and significantly more than

the OECD as a whole (8.1 per cent).

But such large labour supply increases cannot go on forever, so provide only a temporary reprieve from the effect on household income growth of relative underperformance on productivity. In the long run it is relative productivity performances that drive changes in living standards, which is why that metric is the focus in this chapter.

These productivity gaps are pervasive across different sectors of the UK economy: we are not less productive simply because we have too little manufacturing or too many restaurants.⁸ Among other things, British firms – and therefore British workers – have too little capital to work with, explaining almost all of our productivity gap with France. In the 40 years to 2019, total fixed investment in the UK averaged 19 per cent of GDP, the lowest in the G7 and some 4 percentage points below the G7 average of 23 per cent.⁹ Business capital investment in the UK as a proportion of GDP (at 10 per cent in 2019) has consistently lagged behind France, Germany, and the US (13 per cent, on average), as has business investment in research and development (1.2 per cent versus an average of 2 per cent across these three countries in 2019).

In contrast to our firms' lack of capital, the UK scores well on some aggregate measures of human capital, relative both to the past and to some other countries.¹⁰ But there remain major shortcomings and inequalities in skills (see Box 2).

7 T Bell & L Gardiner, *Feel poor, work more: Explaining the UK's record employment*, Resolution Foundation, November 2019. See also J P Pessoa & J Van Reenen, *The UK Productivity and Jobs Puzzle: Does the Answer Lie in Wage Flexibility?*, *Economic Journal*, 124: pages 433-452, 2014.

8 J Oliveira-Cunha et al., *Business time: How ready are UK firms for the decisive decade?*, Resolution Foundation, May 2021.

9 Source: analysis of OECD data. This is calculated as simple averages of the ratio of total gross fixed capital formation (GFCF) to GDP, in current prices.

10 B Égert, C de La Maisonnette & D Turner, *A new macroeconomic measure of human capital exploiting PISA and PIAAC: Linking education policies to productivity*, OECD Economics Department Working Papers No. 1709, April 2022.

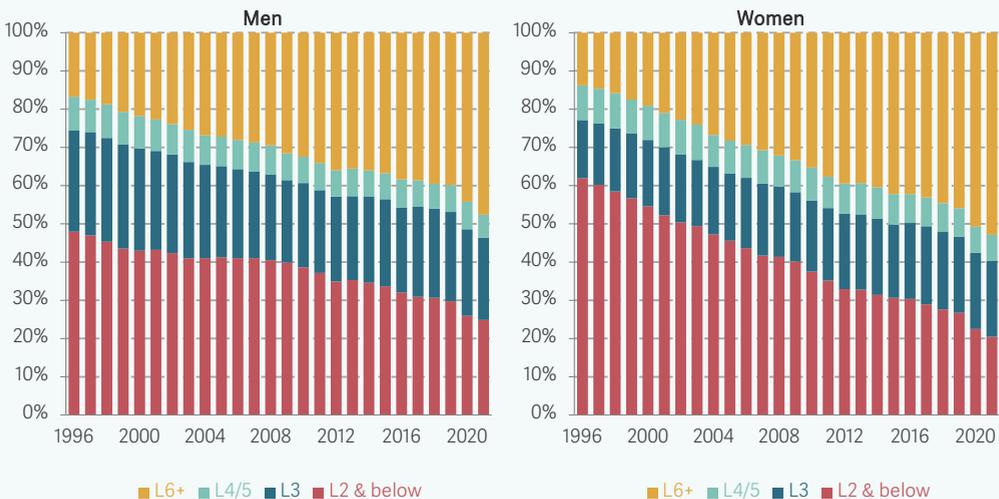
Box 2: Human capital in the UK

Significant gains in educational attainment over recent decades mean that whereas in 1996 roughly half of young men, and significantly more than half of young women, would enter their mid-20s with at most GCSE-equivalent qualifications, fewer than one-in-three do today (Figure 5). The

proportion of young women with a degree has more than doubled over this period. But the pace of improvement has slowed – during the late 1990s, the average annual increase in the proportion of 25-34-year-olds with degrees was 7 per cent, but by 2017-2019 this had fallen to 3 per cent.¹¹

Figure 5: The proportion of younger men and women with lower-level qualifications has roughly halved since the mid-1990s

Highest qualification held among 25-34-year-olds: UK



Notes: Below Level 2 includes qualifications classed as ‘other’ in the ONS Labour Force Survey. Level 2 is equivalent to GCSE-level qualifications, Level 3 is equivalent to A-level, Level 4/5 refer to sub-degree higher education courses, and Level 6+ refers to degree-equivalent qualifications and higher.

Source: Analysis of ONS, Labour Force Survey.

The distribution of human capital in the UK is highly unequal, with our school system’s focus on

binary English and maths exam results at 16, earlier specialisation, and a significant class gap in

11 Analysis of ONS, Labour Force Survey.

higher education (HE) participation posing major challenges.¹² Worryingly, OECD surveys show that the gap in numeracy skills between 16-20-year-olds who do not have a parent that attained an upper-secondary qualification (A-level equivalent) and those that did (approximately -60 points) is the third largest in the OECD, with England performing worse than countries including the US (-40 points) and Australia (-35 points). In 2012, England had the highest proportion of 16-19-year-olds that attained low scores in literacy in the OECD, and the second highest share (behind the US) that attained low scores in numeracy.¹³

Young people scoring low on international assessments today may also not be expected to

develop skills once in work at the same rate that their predecessors have, because they increasingly work in lower-paid roles that offer less training compared to the past.¹⁴ During 2019, just over 15 per cent of 18-34-year-old workers in elementary administrative occupations reported having received work-related training in the previous three months, compared with just over 35 per cent of workers in business and public service professional roles. In fact, training at work is something that British firms have been stepping away from: the average number of days an employee spent in training fell by 18 per cent (from 7.8 to 6.4 days) between 2011 and 2017.¹⁵

The causes of the UK's large and growing productivity gap with frontier economies have been much debated. But the consequences are clear.

Relative decline has been catastrophic for workers' wages and household incomes

It is common to hear claims that aggregate economic progress means little for ordinary workers. But the absence of much of it during this recent period of relative decline has been unambiguously bad news for workers. The direct

12 S Machin, S McNally & J Ruiz-Valenzuela, [Entry through the narrow door: The costs of just failing high stakes exams](#), *Journal of Public Economics*, 190, October 2020.

13 M Kuczera, S Field & H Catriona Windisch, [Building skills for all: A review of England](#), OECD, 2016.

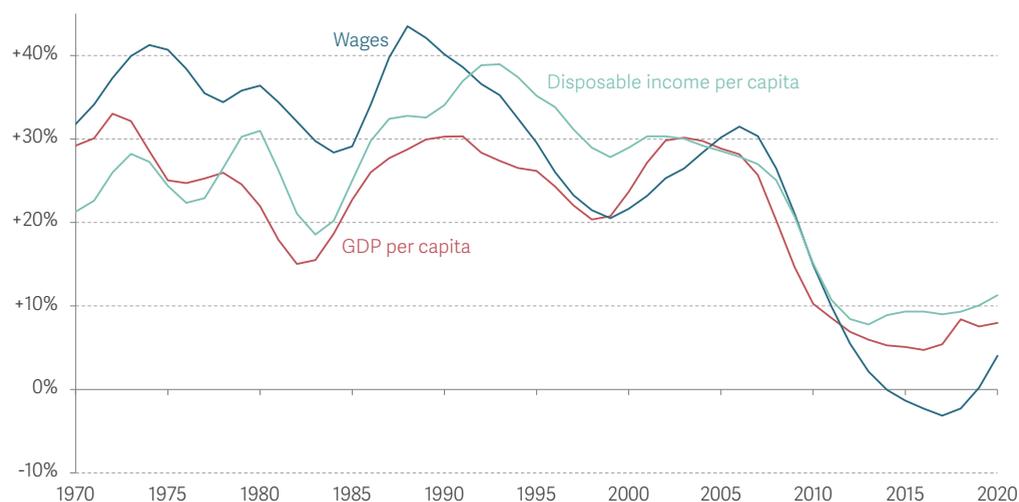
14 For further details on the growing proportion of young people in lower-paid work, see: S Clarke & N Cominetti, [Setting the record straight: How record employment changed the UK](#), Resolution Foundation, January 2019; K Henehan et al., [An intergenerational audit for the UK 2021](#), Resolution Foundation, October 2021.

15 J Li, A Valero & G Ventura, [Trends in job-related training and policies for building future skills into the recovery](#), LSE Centre for Vocational Education Research, December 2020.

effect of weak productivity growth has been stagnant real wages,¹⁶ which are currently falling again as inflation surges. One year of slow wage growth is bad but manageable, but the duration of the current pay squeeze has made it transformational. After a decade and a half of pay stagnation, wages are now at approximately the same level as they were before the financial crisis, that comes at a cost of £9,200 per worker per year, compared to a world in which pay growth had continued its pre-financial crisis trend.¹⁷ This is an historical aberration. Real wages almost quadrupled between 1945 and 2000, and decadal wage growth averaged 33 per cent from 1970 to 2007, before falling to below zero in the 2010s (see Figure 6).

Figure 6: Historically weak wage growth has been the defining feature of the past decade

Annualised decadal growth rates of real wages, real GDP per capita, and real disposable income per capita: GB/UK



Notes: Rolling average of each variable in the three years centred on the date shown, compared to the three years centred on the date 10 years previous. For example, 2020 shows growth between 2009-2011 and 2019-2021. UK data for GDP and incomes, GB data for wages.

Source: Analysis of Bank of England, Millennium of Macroeconomic Data; OBR, Economic and Fiscal Outlook, March 2022; ONS, RHD1; ONS, UK resident population.

16 N Oulton, *The Productivity-Welfare Linkage: A Decomposition*, ESCoE Discussion Paper 2022-07, March 2022.

17 Analysis of ONS, Average Weekly Earnings; ONS, Consumer Prices Index including owner occupiers' housing costs.

This feeds through into real incomes, the growth of which has also slowed since the mid-2000s (albeit offset by the welcome 2010s surge in the employment rate, which rose from around 70 per cent in 2010 to over 76 per cent before the pandemic). In contrast to weak income growth, household wealth in the UK has surged, as Box 3 explores.

Box 3: Wealth, wealth gaps, and intergenerational inequality

Weak income growth is not the only trend explaining how people have experienced the economy in recent years: increasing levels of household wealth have also been crucial. Since the end of the 1980s, the total value of household wealth in Britain has consistently risen – from around three to nearly eight times GDP by the start of the pandemic.¹⁸ The result is that while wealth inequality (which measures the share of total wealth held) has been fairly stable,¹⁹ the absolute gaps (i.e. difference in the value of wealth held) between households has risen markedly. In 2006-08, the average wealth held by an adult in a family in the richest tenth of the population was £960,000 more than an average adult in

the middle (fifth decile) of the distribution; that gap increased, in real terms, to £1.3 million by 2016-18 and is estimated to have risen further during the pandemic to £1.4 million in 2021.²⁰ Growing wealth, and wealth gaps, largely reflects rising values of existing assets (capital gains), rather than the creation of new ones via saving. Rising asset values have delivered huge windfalls to those with assets, while driving falls in home ownership (given the need for a deposit): 55 per cent of those born between 1956-1960 were home owners by the age of 30, compared to just 27 per cent for those born 1981-1985.²¹ Meanwhile, 12 per cent of people aged 60-64 own a second home (including buy-to-let

18 K Shah, [Wealth on the eve of a crisis: Exploring the UK's pre-pandemic wealth distribution](#), Resolution Foundation, January 2022.

19 The share of wealth held by the richest tenth of families has hovered around 50 per cent since the start of the 1980s, and the top 1 per cent have consistently owned a little under a fifth of total wealth. For more on this, and why these are likely underestimates given the coverage of the surveys used to estimate these wealth shares, see: A Advani, G Bangham & J Leslie, [The UK's wealth distribution and characteristics of high-wealth households](#), Fiscal Studies, October 2021.

20 J Leslie & K Shah, [\(Wealth\) gap year: The impact of the coronavirus crisis on UK household wealth](#), Resolution Foundation, July 2021.

21 L Judge & J Leslie, [Stakes and ladders: The costs and benefits of buying a first home over the generations](#), Resolution Foundation, June 2021. For further discussion of intergenerational inequality and home ownership, see: J Blanden, A Eyles & S Machin, [Trends in intergenerational home ownership and wealth transmission](#), Centre for Economic Performance Discussion Paper, April 2021.

properties).²² Wealth gaps between regions are far larger than the gaps in pay and incomes.²³

At a time of slow income growth it is not surprising these trends create deep dissatisfaction, as well as big winners and losers. The rising value of wealth relative to income means people are more dependent on what they inherit, rather than what they can

do themselves through earning pay rises and saving: the value of inheritances is expected to double by 2040.²⁴ Furthermore, as wealth has become more important for people's economic lives, political incentives may shift towards protecting that wealth, risking increased polarisation across groups.²⁵

These weak productivity and income outcomes reflect not just the common experience of advanced economies since the financial crisis, but the UK's relative decline. As Figure 7 shows, typical British household incomes have underperformed comparator countries and now sit below those in other North-West European countries. Whereas in 2007 typical UK incomes were higher than in each of the comparator countries shown, by 2018 they were lower.²⁶ Specifically, they were 16 per cent lower than in Germany and 9 per cent lower than in France.

22 Source: ONS, Wealth and Assets survey. Some of the gap between age groups will reflect life-cycle effects (e.g. older people are more likely to have been able to build up savings to purchase another property) not just cohort effects. But the wealth values of recent age cohorts have lagged behind older groups – for more see: K Henehan et al., [An intergenerational audit for the UK 2021](#), Resolution Foundation, October 2021.

23 For further discussion of wealth and income inequality, see: R Crawford, D Innes & C O'Dea, [Household Wealth in Great Britain: Distribution, Composition and Changes 2006-12](#), The Journal of Applied Public Economics, 37(1), March 2016.

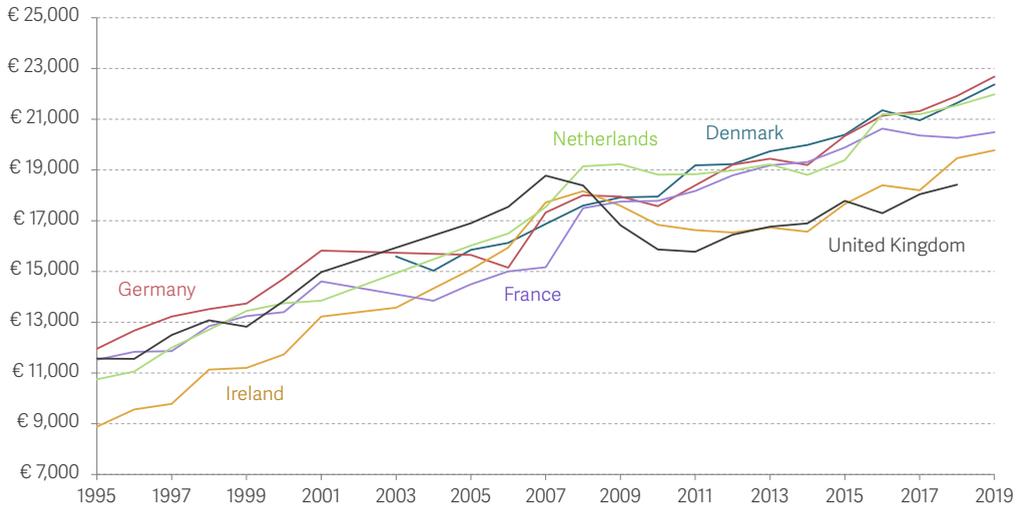
24 J Leslie & K Shah, [Intergenerational rapport fair? Intergenerational wealth transfers and the effect on UK families](#), Resolution Foundation, February 2022. For further discussion of the growth in inheritances and the links to inequality, see: P Bourquin, R Joyce & D Sturrock, [Inheritances and inequality over the life cycle: what will they mean for younger generations?](#), Institute for Fiscal Studies, April 2021.

25 A J Stewart, N McCarty & J J Bryson, [Polarization under rising inequality and economic decline](#), Science Advances, 6(50), Dec 2020.

26 The UK's comparatively poor income performance partly reflects relatively large rises in the UK price level. Over the same time period (2007 to 2018) the main UK measure of household incomes rose by 4 per cent, compared to the internationally comparable 2 per cent fall depicted here. Analysis of IFS, Living standards, poverty and inequality in the UK, median household incomes before housing costs.

Figure 7: Median household incomes in the UK are lower than in many other European countries

Median equivalised household net income: selected European countries



Notes: PPP adjusted. Some gaps are interpolated, including all countries in 2002 and the UK in 2003, 2004 and 2005.

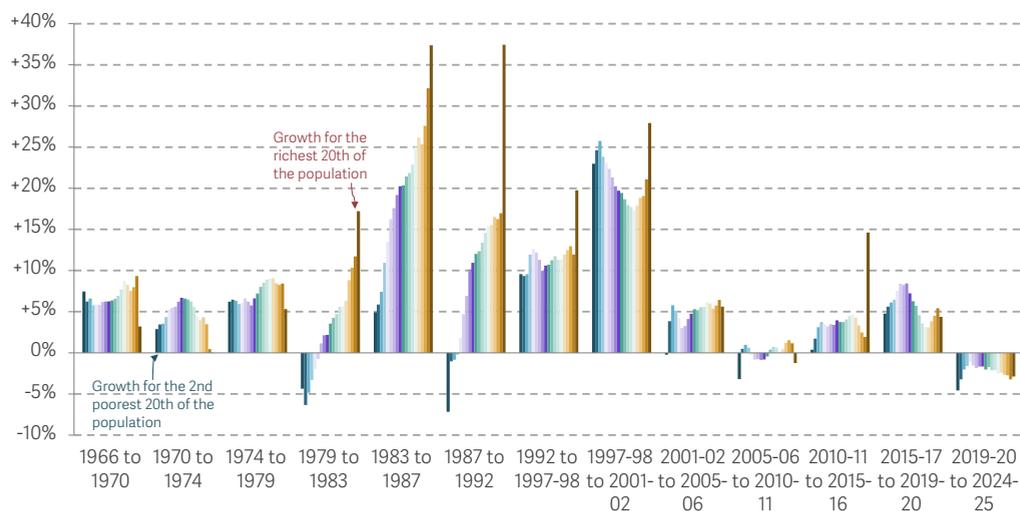
Source: EU-SILC, Mean and median income by household type.

That is the toxic background to the current cost of living crisis, where double-digit inflation means real income falls this year and next on a scale only normally seen during recessions. As Figure 8 shows, non-pensioner real incomes – for rich and poor alike – are on course to be lower in 2024-25 than in 2019-20, making this the worst parliament on record for living standards.²⁷

27 The March 2022 OBR forecast is based on inflation peaking at 8.7 per cent in 2022, and averaging only 2.4 per cent in 2023-24. Since then, official forecasts of inflation have increased, suggesting that a more up-to-date forecast for the current Parliament would look even worse.

Figure 8: This Parliament risks being the worst on record for real household income growth

Total real growth in median equivalised household disposable income per period for non-pensioners, after housing costs, by income quintile: GB/UK



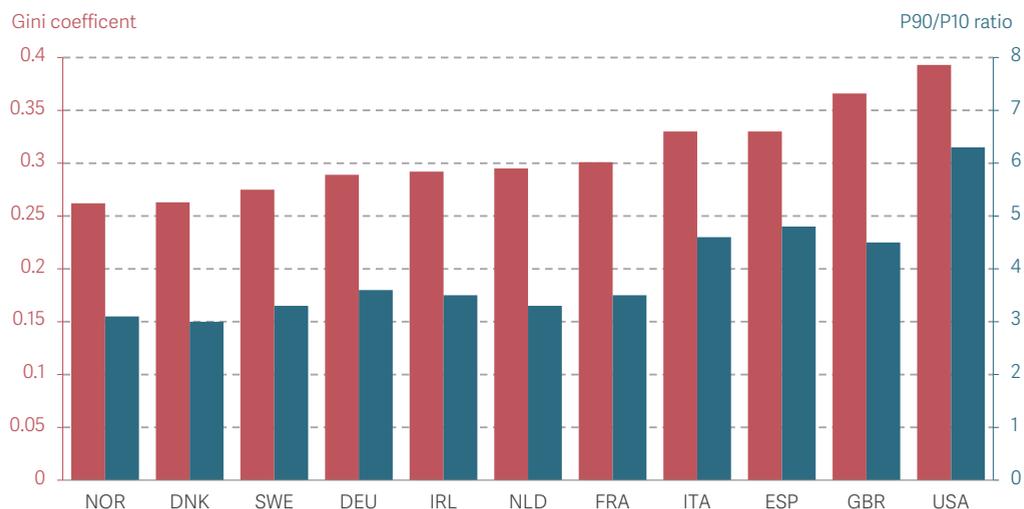
Notes: Projections as of March 2022. We exclude the bottom 5 per cent due to concerns about the reliability of data for this group. See A Corlett & L Try, *The Living Standards Outlook 2022*, March 2022, Resolution Foundation for details of our projection methodology. Some periods are four years long and others five years. The chosen time periods correspond to the years of past general elections (plus 2024), but we do not include a division for the 2017 election and nor do we try to estimate growth over the February to October Parliament of 1974. This analysis does not account for increases since March 2022 in both outturn and forecast inflation (pushing down on income growth) or the policies to assist households with energy costs announced in May 2022. Source: Analysis of DWP & IFS, *Households Below Average Income*; and RF projection including use of the IPPR Tax Benefit Model, ONS data and OBR forecasts.

Weak income growth has been combined with persistently high inequality

Living with flatlining wages has been difficult for the past 15 years, but the UK has been living with high inequality for more than twice as long. The Gini coefficient for disposable household income increased from 0.27 to 0.37 during the 1980s and has remained roughly unchanged ever since, higher than any other major European countries but below that seen in the US (Figure 9).

Figure 9: Income inequality in the UK is higher than all other large European countries

Gini coefficient and P90/P10 income ratio for post-tax disposable income: selected OECD countries, 2018



Notes: Data refers to the Gini (disposable income, post-taxes and transfers) and the P90/P10 disposable income ratio, the ratio of the upper bound value of the 90th percentile to that of the upper bound value of the 10th percentile.

Source: Analysis of OECD, Income Distribution data.

The high but stable level of income inequality measured by the Gini coefficient hides significant change.²⁸ Over the past two decades government policy has intentionally reduced hourly wage inequality between the bottom and the middle via the introduction and ramping up of the National Minimum Wage. Although this has taken place alongside some other aspects of low-paid work deteriorating, as discussed in Box 4, and experienced by workers in some of our focus groups.

“It seems to be all about how competitive we can be in this market that we’re in, but they’re just forgetting about the people on the ground that are actually generating this money. We just work at 150 miles an hour, and it just keeps going and going and going.”

(Focus group participant, Solihull)

28 M Brewer & L Wren-Lewis, *Accounting for Changes in Income Inequality: Decomposition Analyses for the UK, 1978–2008*, Oxford Bulletin of Economics and Statistics, 78(3), August 2015.

Box 4: Trends in the quality of work

When viewed in conjunction with high levels of wage and income inequality, the recent relative deterioration in several aspects of lower earners' experience of work is even more concerning. Most employees are satisfied with their jobs, and there have been only limited falls in job satisfaction overall since the early 1990s among workers as a whole. But across a range of indicators – from job satisfaction, to workplace stress, to feeling used up at the

end of the day – the experience of work for low earners has deteriorated: 70 per cent of the lowest earners were satisfied with their jobs in early 1990s compared to 56 per cent pre-pandemic, converging downwards towards the experience of higher earners (who consistently report the lowest level of job satisfaction).²⁹ Forms of job insecurity are also far more prevalent among low-paid workers and have not fallen in the way they have for higher earners.³⁰

However, the rising wage floor, even when combined with recent employment growth disproportionately benefiting those on low-to-middle incomes,³¹ has not translated into falling income inequality. The main drivers of relatively high and broadly stable inequality in the UK include:³²

- While the minimum wage has reduced wage differentials between the bottom and the middle of the pay distribution since the late 1990s, gaps between the middle and top (especially among men) have continued to grow, and are now at the highest levels ever. High wage inequality is in part driven by relatively decentralised wage-setting institutions in the UK.³³

29 K Shah & D Tomlinson, [Work experiences: Changes in the subjective experience of work](#), Resolution Foundation, May 2021.

30 N Cominetti et al., [Low Pay Britain 2022: Low pay and insecurity in the UK labour market](#), Resolution Foundation, May 2022.

31 S Clarke and N Cominetti, [Setting the record straight: How record employment has changed the UK](#), Resolution Foundation, January 2019; J Cribb, R Joyce & T Wernham, [Twenty-five years of income inequality in Britain: The role of wages, household earnings and redistribution](#), Institute for Fiscal Studies, March 2022.

32 A Corlett, F Odamtten & L Try, [The Living Standards Audit 2022](#), Resolution Foundation, July 2022.

33 U Altunbeken et al., [Power plays: The balance of employer and worker power in the UK labour market](#), Resolution Foundation, July 2022.

- Patterns of households formation, and labour supply choices within and between households, have been changing in a way that has further increased inequality. The UK has more two-earner and no-earner households than many other countries, while lower-earning men have reduced the number of hours they work, pushing up on inequality and making changes in weekly pay less progressive than those for hourly pay.
- While housing costs have been falling relative to incomes for the richest households since the early 1990s, they continued rising for poorer households, pushing up on inequality in incomes after housing costs.³⁴
- The UK's system of pensions and social benefits reduces inequality less effectively than in many other European countries, although major differences in contributory benefits make direct comparisons difficult.³⁵

Figure 10: Public concern with poverty and inequality has increased since 2010

Proportion of respondents answering “poverty/inequality” to the question: “What do you see as the most/other important issues facing Britain today?”



Notes: Data shown is five-month rolling averages.

Source: Ipsos Issues Index.

34 D Tomlinson, [Inequality street: Housing and the 2019 general election](#), Resolution Foundation, November 2019.

35 Many European countries' working-age benefits and pensions depend to a greater extent than the UK's on previous earnings-related contributions. As a result, these countries' taxes and benefits appear more redistributive within any given year, relative to the UK, than they would in a dynamic or multi-year comparison.

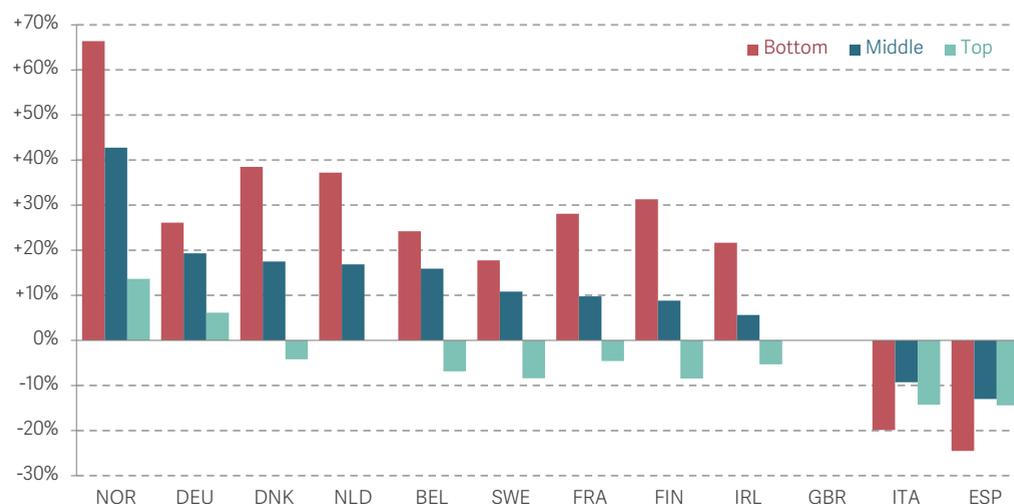
These two features of Britain's economy – high inequality and slow growth – interact in important ways. Not least, as it appears that it is the latter feature that has raised public concern with the former, as Figure 10 shows.

It is the toxic combination of high inequality and weak growth that distinguishes the UK economy today, translating into poor outcomes for low-to-middle income Britain

The interaction of weak income growth with high inequality has much more significant implications than that on public attitudes. It means that while richer UK households have higher incomes than their equivalents in all but a few European countries, the same cannot be said of the bottom or even middle of the income distribution.

Figure 11: Rich UK households compare well to those in mainland European countries, but average and poorer ones do not

Incomes at the 10th, 50th and 90th percentiles of the household disposable income distribution in selected European countries relative to the UK: 2018



Notes: Data for the 'bottom' households is for those at the 10th percentile; data for 'middle' households is for those at the 50th percentile; and data for the 'top' households is for those at the 90th percentile.

Source: EU-SILC, Distribution of income by quantiles.

As Figure 11 shows, the 90th percentile of households in the UK have higher incomes than those in France. But, in contrast to historically similar levels, typical household incomes are now 9 per cent lower. For low-income

households the combined effects of low growth and high inequality are huge: they are now 22 per cent poorer than their counterparts in France – equivalent to £3,800 a year. In fact the typical incomes of the poorest fifth of the population were almost no higher on the eve of the pandemic than they were back in 2004-05, despite GDP per person growing by 12 per cent over this period.³⁶

There is nothing resilient about an economy where the poor can barely stay afloat. In the two years leading up to the pandemic, just over one-in-four (26 per cent) of all adults would not be able to manage for a month on savings alone if their income stopped; and nor would just under four-in-ten of those in the bottom two income deciles.³⁷ Low growth combined with high inequality means poorer households immediately struggling in the face of today's surging energy bills: as Figure 12 shows, the share of spending going on essentials among the lowest-income households had already risen from 51 per cent to almost 60 per cent between 2006 and 2019. That leaves this group little margin for adjustment and explains why price rises this year are already translating into more people seeking debt advice.³⁸ In our focus groups, we heard about the day-to-day struggles of living on a low income.

“It’s impossible actually to save if on a low income...I got paid on Friday and it was gone by Monday.”

(Focus group participant, Sunderland)

Of course, the impact of those relatively low incomes among poorer households in the UK are not evenly borne. Some groups are over-represented in the bottom income quartile: 39 per cent of single parents; 37 per cent of social renters; 45 per cent of adults in Bangladeshi households, and 42 per cent in Pakistani households; and 22 per cent of people with disabilities.³⁹

36 For further discussion of international comparisons in household income levels and shares see: A Corlett, F Odamtten & L Try, [The Living Standards Audit 2022](#), Resolution Foundation, July 2022.

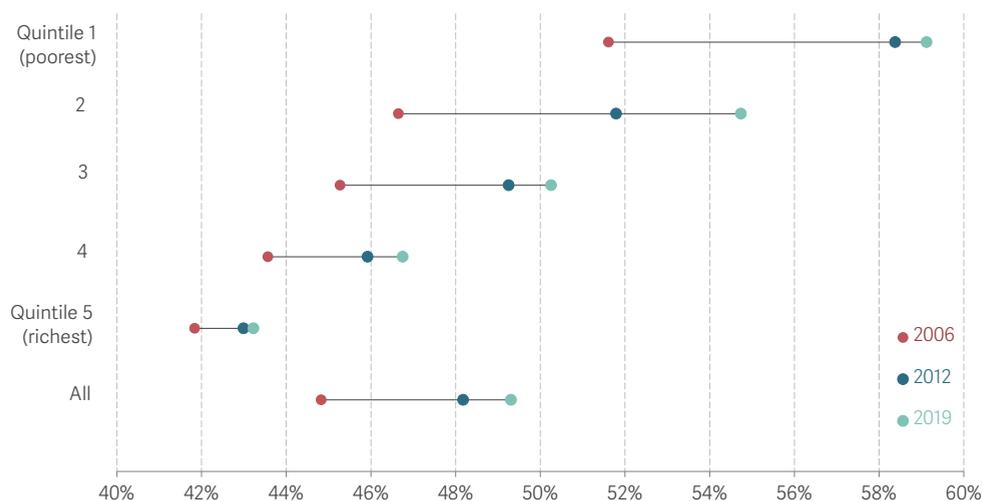
37 Analysis of ONS, Wealth and Assets Survey.

38 Citizens Advice data shows a 17 per cent rise in the number of people seeking advice on debt in May 2022 compared with the previous year. Citizens Advice, [Advice Trends](#), May 2022.

39 Analysis of DWP, Households Below Average Income, Income after housing costs in the 3 years to 2019.

Figure 12: The proportion of total spending that goes on essential items has been increasing sharply for lower-income households

Proportion of equivalised non-housing household consumption spent on 'essentials', by quintile of the working age equivalised net household income distribution: UK



Notes: 'Essentials' covers food, fuel, clothing and transport. Distribution calculated on the basis of income after housing costs. We present trends in consumption for each individual, rather than just for the head of the household.

Source: Analysis of ONS, Living Costs and Food Survey.

It is also particularly painful for the young

The young are also hard hit by this combination of slow growth and high inequality. Slow growth necessarily puts limits on absolute income, reducing the extent to which individuals can expect to see income growth as they age.⁴⁰ This has had much more of an impact on those generations entering the labour market during this phase who would have otherwise expected to see rapid earnings growth in their 20s and 30s: the cohort born in the 1980s, for example, has experienced lower levels of earnings than the 1970s cohort at the same age. As a result, cohort-on-cohort improvements in the level of household disposable income – something that would have been taken for granted throughout the second half of the 20th century – have also slowed, or stopped, for the most recent cohorts.⁴¹

40 Some of this draws on: P Bourquin, M Brewer & T Wernham, Trends in income and wealth inequalities, IFS Deaton Review of Inequalities, forthcoming.

41 K Henehan et al., *An intergenerational audit for the UK: 2021*, Resolution Foundation, October 2021.

The amount of household wealth relative to income has grown enormously over the past 50 years (discussed above in Box 3). Britain's housing market has been at the core of the rise in net household wealth, with the growth in house prices since the mid-1990s delivering windfall gains to older cohorts but also reversing the 20th century rise in home-ownership among young adults. Today's young people are less than half as likely to own, and more than twice as likely to rent privately, as their predecessors were thirty years earlier. For example, at age 30, the home ownership rate among those born in the early 1980s was 28 per cent, closer to that experienced by their grandparents' generation born in the early 1930s (29 per cent) than their parents' generation born in the early 1950s (52 per cent)).⁴² The result is that those born in the 1980s or later have borne the brunt of the UK's poor record on productivity and also missed out on the surge in the value of wealth that has principally accrued to older generations.

Furthermore, as well as being harmed by the slowdown in growth and the surge in the value of wealth, the social mobility of younger generations is also held back by high rates of inequality. There is strong international evidence that high levels of inequality also reduces relative social mobility.⁴³ In the UK, intergenerational social mobility was lower for the cohort born in 1970 than it was for the one born in 1958 (i.e. those born in 1970 are more affected by their parents' circumstances than those born in 1958).⁴⁴ The surge in wealth that is currently benefiting older individuals should, in time, be transferred down to today's younger cohorts, further reducing social mobility with the link between the living standards of the 1980s cohort and their parents' circumstances stronger than was the case for the 1960s cohort.⁴⁵

42 K Henehan et al., [An intergenerational audit for the UK: 2021](#), Resolution Foundation, October 2021.

43 The classic reference is: M Corak, '[Income inequality, equality of opportunity, and intergenerational mobility](#)', *Journal of Economic Perspectives*, 27(3), 2013. See also: M Brewer, *What Do We Know and What Should We Do about Inequality?*, SAGE Publishing, 2019, for a discussion.

44 Trends in intergenerational mobility are shown in: L Elliot Major & S Machin, *Social Mobility and Its Enemies*, Pelican, 2018. Trends in children's outcomes as they age are shown in: C Crawford, L Macmillan & A Vignoles, '[When and why do initially high-achieving poor children fall behind?](#)', *Oxford Review of Education*, 43(1), 2017. See also: S Cattan et al., '[Early childhood and inequalities](#)', IFS Deaton Review of Inequalities, June 2022.

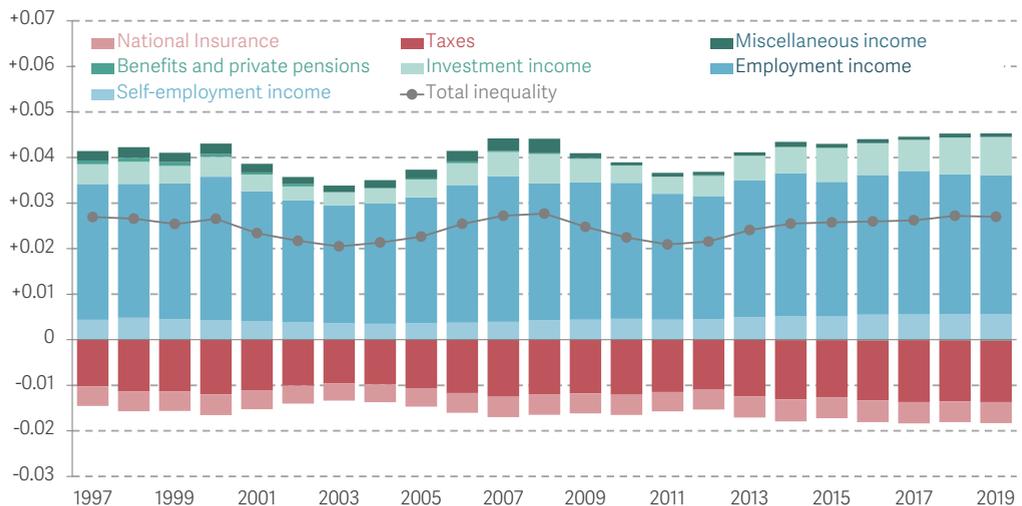
45 P Bourquin, R Joyce & D Sturrock, '[Inheritances and inequality over the life cycle: What will they mean for younger generations?](#)', Institute for Fiscal Studies, April 2021.

Inequalities between places are large and persistent on multiple measures

Just as incomes are not spread evenly across people, they are not spread evenly across places either. Income per person in the richest local authority – Kensington and Chelsea (£52,500) – was 4.5 times that of the poorest – Nottingham (£11,700) – in 2019. Income from wages and salaries largely determines spatial income disparities, but the contribution of investment income to such inequality has doubled since 1997 (see Figure 13).⁴⁶

Figure 13: Earned income largely determines spatial income disparities, but the contribution of investment income has almost doubled over time

Absolute contribution to local authority inequality (I2 measure) from different sources of income per capita (GDHI cash measure): UK



Notes: The vertical axis shows the absolute contribution to income inequality using the I2 measure.

Source: Analysis of ONS, Gross Disposable Household Income (GDHI).

⁴⁶ Income here is: PAYE earnings and benefits including state pension. For more detail on income gaps between places see: L Judge & C McCurdy, [Income Outcomes: Assessing income gaps between places across the UK](#), Resolution Foundation, June 2022.

Income from wages and salaries largely determines spatial income disparities,⁴⁷ but the contribution of investment income to such inequality has doubled since 1997 (see Figure 13). Rising inequalities in self-employment and investment income are being driven by significant income growth among those on higher incomes, particularly in London.⁴⁸ Over the past two decades, for example, average investment income per person has quintupled in Kensington and Chelsea and Westminster but only doubled for the country as a whole.

Inequalities of income and output between places are distinct, but share common features, particularly that both have been highly persistent over time. The spatial differences in incomes we observe in 1997 explain 80 per cent of the variation in the average local authority income per person in 2019. Productivity gaps across areas are significantly higher than those for income: the highest productivity place is 130 per cent more productive than the lowest compared to a 91 per cent difference for income.⁴⁹ To what extent this is exceptional internationally receives a huge amount of attention,⁵⁰ but the scale and persistence of such gaps means the case for addressing them is uncontroversial.

Productivity gaps grew with deindustrialisation in the last decades of the 20th century, and again in the first decade of the 21st as the likes of Milton Keynes and Swindon pulled ahead to become high-productivity areas (see Figure 14). As England's largest cities other than London continued to suffer from low productivity, in fact all of England's biggest cities outside the capital have productivity levels lower than the UK average. The underlying drivers of these gaps are knowledge-intensive, high productivity services thriving in larger places with access to high skilled workers, alongside large quantities of intangible and ICT capital. For example, raising the value of computer equipment per job in Manchester by 20 per cent would be expected to boost productivity by 4 per cent today, but would have made little difference in 2002.

47 We measure income inequality here using the I2 measure, which is half the squared coefficient of variation. We used the Stata package `ineqfaq`, which implements the method developed by: A Shorrocks, Inequality decomposition by factor components, *Econometrica*, 50(1), January 1982.

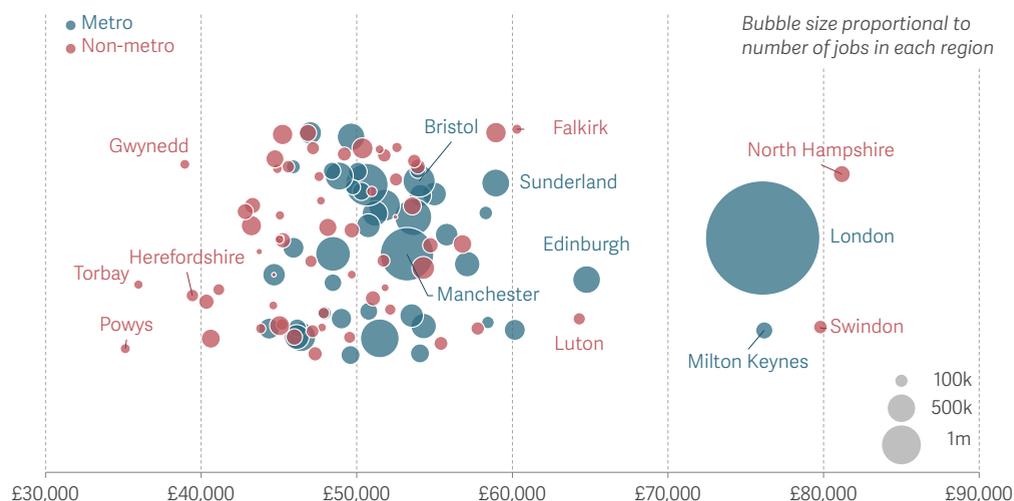
48 L Judge & C McCurdy, *Income Outcomes: Assessing income gaps between places across the UK*, Resolution Foundation, June 2022.

49 Productivity: highest, North Hampshire; lowest, Powys. Income: highest, Buckinghamshire; lowest, Nottingham.

50 The coefficient of variation between metro areas' productivity is no higher in the UK than it is in Germany. For further discussion, see: P Brandily et al., *Bridging the gap: What would it take to narrow the UK's productivity disparities?*, Resolution Foundation, June 2022.

Figure 14: Spatial disparities in productivity in the UK are large

Gross value added per job, by area: UK, 2019



Notes: GVA per job in 2019, calculated as gross value added divided by number of jobs by workplace. Spatial units are a combination of OECD metro areas and NUTS3 for non-metro areas.

Source: Analysis of ONS, Subregional Productivity, July 2021.

Britain's low growth and high inequality equates to stagnation

The UK's combination of relative decline over the past 15 years and high inequality for the past four decades is a dangerous combination. If sustained, they risk the UK entering a prolonged period of stagnation, posing serious risks to not just our economy but to our society and democracy too.

The poor and the young are especially hard hit. Those on low incomes are left with no resilience in the face of today's fast price rises, while younger workers increasingly find themselves concentrated in lower-paying work without the compensation of benefiting from surging house prices enjoyed by older generations.

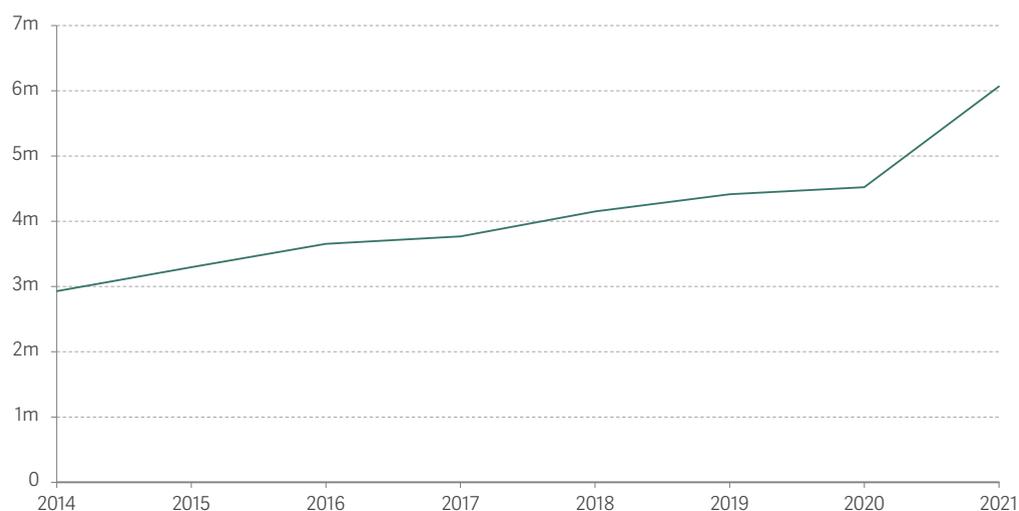
It risks public services struggling, even as the tax burden rises. Slow growth combined with cost pressures on public services mean taxes are on course to reach their highest share of GDP since 1949.⁵¹ But despite rising taxes,

51 K Shah, J Smith & D Tomlinson, *Under pressure: Managing fiscal pressures in the 2020s*, Resolution Foundation, February 2022.

the quality of public service provision is continuing to deteriorate on a range metrics. The proportion of victims who were satisfied with the police fell from 74 per cent in 2012-2013 to 66 per cent in 2017-2018,⁵² while the number of people waiting for consultant treatment following an referral has doubled between 2014 and 2021, from 3 million to 6 million, as shown in Figure 15.

Figure 15: NHS waiting lists have doubled since 2014

Total number of people waiting for NHS consultant treatment following referral: England



Source: NHS England and NHS Improvement, monthly RTT data collection.

The pandemic has of course added significantly to the strain on the public sector, particularly the NHS, and has demonstrated that high inequality puts further pressure on public services.⁵³ But even if people recognise this, the experience of stretched public services is all too common.

“The police just haven’t got the resources to deal with somebody that’s dealing drugs...But it’s just not the police that don’t do things. It’s then the courts that don’t do anything.”

(Focus group participant, Barnsley)

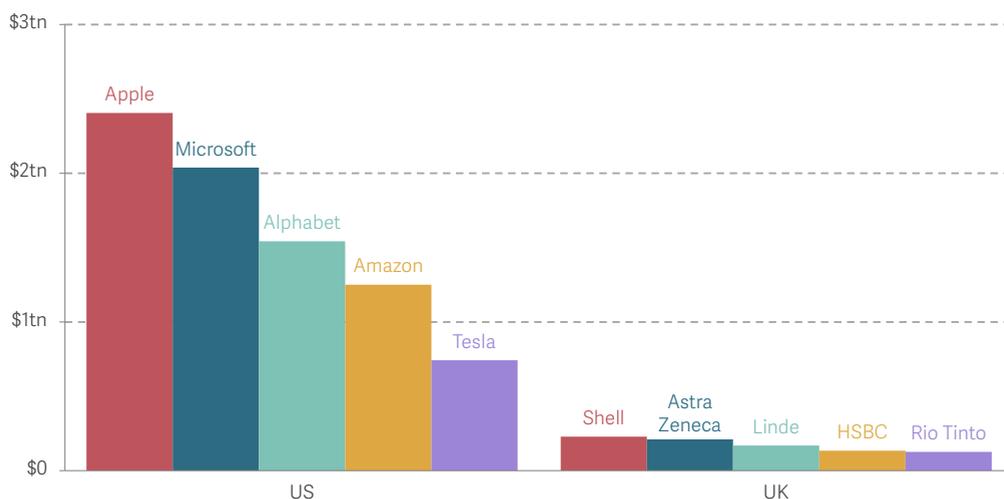
52 Institute for Government, [Performance Tracker](#).

53 M Suleman et al., [Unequal pandemic, fairer recovery: The COVID-19 impact inquiry report](#), The Health Foundation, July 2021.

A stagnating nation is also less well placed to embrace change or seize new opportunities, building on the UK's science and innovation strengths. Despite popular claims that change is speeding up, structural economic change in the UK has been slowing down, with flat or falling measures of dynamism at the level of workers⁵⁴ and firms.⁵⁵ While the UK has advantages in many growing sectors, including digital technology, it is some time since those were translated into building new large companies. As Figure 16 shows, notwithstanding the importance of AstraZeneca, the UK-listed top five firms are much smaller, much older, and weighted more heavily towards banking and extraction than their US, technology focused, counterparts.⁵⁶ An economy fossilised in areas that were important for growth in periods past is not one prioritising the future.

Figure 16: The UK stock market lacks large firms in the tech sector

Market capitalisation of 5 largest listed firms: US and UK, June 2022



Notes: The Linde Group is listed in London but headquartered in Dublin.

Source: Analysis of June 2022 market capitalisation data, from: companiesmarketcap.com.

54 N Cominetti et al., *Changing jobs?: Change in the UK labour market and the role of worker mobility*, Resolution Foundation, May 2021.

55 J Oliveira-Cunha et al., *Business time: How ready are UK firms for the decisive decade?*, The Economy 2030 Inquiry, May 2021.

56 When interpreting this chart, it is important to note that the country a company is listed in is not necessarily where most of its value is added.

Stagnation does not just risk us failing to seize new opportunities, it also makes it harder to solve old problems. High inequality makes the zero-sum nature of politics in a low growth era even more difficult, with relative positions mattering far more. With the public prioritising lower geographical inequality, high inequality between places risks being not just economically wasteful but democratically unsustainable. Average incomes in Yorkshire and the Humber fell by 2 per cent in the 15 years to 2019; at the same time, average incomes in London rose by 7 per cent as Figure 17 shows.

Figure 17: Between 2004 and 2019, average incomes fell by 2 per cent in Yorkshire but rose by 7 per cent in London

Change in real income per capita (GDHI cash measure) between 2004-2019, and level of income per capita in 2004: UK nations and regions



Notes: CPI-adjusted, 2020 prices.

Source: Analysis of ONS, Gross Disposable Household Income.

But the experience of other countries doesn't guarantee that the pressure stagnation puts on politics will lead to its economic drivers being resolved. Educated, affluent economies can stagnate for long periods – as Italy's decline from being a GDP per capita peer of Germany in the 1980s to one of Spain today shows. The status quo being democratically unsustainable can instead lead to huge pressure on your politics, in Italy's case via oscillations between governments led by populists and unelected technocracy.

It is worth pausing on the striking fact that 25 million people in the UK weren't even born at a time when inequality was at more moderate levels, when the top 10 per cent had less than five times the income share of the bottom 10 per cent – a threshold that was crossed in 1991 after decades of remaining relatively constant at three times.⁵⁷ And 8 million younger workers – around a quarter of people in employment today – have never worked in an economy with sustained average wage rises.⁵⁸

The UK has endured a period of relative economic decline while remaining a highly unequal country. The two combining and persisting is what economic stagnation looks like, posing dangers not only to our incomes but to the fabric of the country and its democratic institutions. As such, economic policy makers in the 2020s must tackle these twin challenges of low growth and high inequality. However, they need to do so amidst a decade of significant change, as the effects of Brexit, the legacy of Covid-19, and the net zero transition are felt across the economy. Some see these forces for change as representing partial answers to the questions posed by this chapter, while others argue that such significant disruption will pose challenges that are even more acute, so it is to the question of change during the 2020s that the next chapter turns.

57 Analysis of DWP & IFS, Households Below Average Income, based on non-pensioners only.

58 Analysis of Analysis of ONS, Labour Force Survey. 8 million of those employed in 2022 were not yet 16 in 2007.